INVESTMENT DEALERS ASSOCIATION OF CANADA

ASSOCIATION CANADIENNE DES COURTIERS EN VALEURS MOBILIÈRES

June 27, 2007

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AND

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Re: Comments on proposed National Instrument 31-103 *Registration Requirements* and proposed Companion Policy 31-103 *Registration Requirements*

I am pleased to provide the comments of the Investment Dealers Association of Canada (IDA) regarding the Canadian Securities Administrators' (CSA) National Instrument 31-103 *Registration Requirements* (Rule) and Proposed Companion Policy 31-103 *Registration Requirements* (Companion Policy) (collectively "Proposal").

The IDA is the national self-regulatory organization (SRO) of the securities industry. Our membership includes more than 200 investment dealers who play an essential role in the Canadian capital markets and by extension the Canadian economy. Our mandate is to protect investors and enhance the efficiency and competitiveness of the Canadian capital markets.

The Proposal has been reviewed in consultation between IDA staff and numerous IDA Committees, including the District Councils, the Education and Proficiency Committee, the Compliance and Legal Section and the Role of the Compliance Officer Subcommittee of the Compliance and Legal Section. These consultations have helped develop or confirm the IDA's positions as outlined below.

The IDA strongly supports the harmonization goals of the Proposal, the elimination of regulatory duplication through its recognition of the roles of the IDA and Mutual Fund Dealers Association of Canada (MFDA) in front-line regulation of their Members and its movement towards more principles-based regulation in areas such as compliance, record keeping, record retention and conflicts of interest. The greater flexibility of principles based rules makes sense in an industry with such a wide variety of businesses in terms of size, structure, products, services and clients.

We believe that the Proposal has many other benefits for the industry and the public, among them bringing referral arrangements within the regulatory ambit, rationalizing the process when registered individuals change firm, and extending registration and customer protections to rapidly growing sectors such as the exempt market, in which there is currently an unlevel playing field and uneven protections for customers between different types of dealers.

With regard to the exempt market, with eligibility based on economic factors as a proxy for customer sophistication, it is essential that securities regulation give investors in that market the same protections as are available in other markets. The IDA requires that its Member exercise the same degree of diligence in knowing their clients and meeting suitability standards when they deal in exempt products as in their dealing in other investment products. Exempt market dealers should be held to no lesser standard.

The IDA also appreciates the CSA's inclusion of the IDA and MFDA in the development of the Proposal and the extent of additional industry consultation during that development.

Within the context of our overall support of the Proposal, our comments below are directed at technical problems that we believe need to be corrected. They are organized by section number, except for the first, more generic comment.

References to the IDA

A number of sections refer specifically to the IDA and others that refer to an MFD SRO. Wherever possible, the IDA suggests the substitution of a generic term such as "Recognized SRO" to avoid the requirement to change provisions of the proposed rule when there is a change to the SRO structure.

At the moment, the IDA is involved in merger discussions with Market Regulation Services Inc. (RS) that will, subject to Member and regulatory approval, result in a new entity that will take over the self-regulatory responsibilities of the two organizations.

The IDA is recognized in all Provinces except New Brunswick and Prince Edward Island. It is not recognized in the Yukon, Northwest Territories or Nunavut. It has applied in New Brunswick. The other jurisdictions do not have legislation authorizing recognition, but we understand that they are preparing legislation which would allow it. On implementation of that legislation the IDA or merged IDA and RS will apply for recognition in those jurisdictions.

The only sections of the proposed Rule that require reference to specific SROs are 3.1 and 3.2. In other sections references to the IDA or MFD SRO could be changed to "Recognized SRO" so that any exemptions or exceptions will automatically apply to any new SRO on recognition. If there is a need for application of certain provisions to a new SRO, that could be put in the recognition order.

The IDA does not view this as a critical concern, but suggests that it would make the future administration of the proposed Rule more efficient.

Section 2.5 – Exemption from adviser registration for IDA members with discretionary authority

While the IDA agrees with the exemption, which is a continuation of existing exemptions in several jurisdictions, we urge the CSA not to include references to specific IDA regulations or policies within the proposed Rule.

Inclusion of specific references to IDA rules will require amendment to the proposed Rule whenever IDA rules are changed. IDA rules are likely to be changed at least twice in the foreseeable future. The pending merger between the IDA and RS will create a new organization, so that any specific reference to the IDA will have to be changed.

The IDA is also involved in an extensive rewriting of its rules to put them in plain language and re-organize them for ease of reference. While the project is not intended to change the requirements, section numbers will change and there may be language and organization changes, all of which would result in necessary changes to the Rule. It is highly unlikely that this project will be completed before the proposed merger.

The wording of section 2.5 suggests that it can accommodate amendments to those specific rules, but not the types of changes noted above. Therefore the changes noted above would require approval by all CSA members of the concomitant changes to the Rule.

As an alternative to Section 2.5 as currently drafted

- There could be a general exemption from registration as an advisor for dealers that are members of a recognized SRO, as described in the general comment above. Members providing discretionary portfolio management services will remain subject to SRO rules, and changes to SRO rules are subject to CSA review and approval. We understand that the MFDA does not currently permit discretionary account management, therefore its members could not take advantage of the exemption unless it changes its rules in this regard, or

- The condition for the exemption could be put in more general terms by a slight change to the section and elimination of the specific rule citations:

> The adviser registration requirement does not apply to a registered investment dealer that manages the investment portfolio of a client through discretionary authority granted by the client if the dealer is a member of a recognized SRO and complies with rules made by the recognized SRO governing discretionary portfolio management.

Section 2.6 – Individual Categories; Registration of the "mind and management" of a registered dealer or adviser

Question 6 of the "Notice and Request for Comment" asks for comments on registering the "mind and management" of registered dealers or advisers. The IDA supports registration of all those involved in directing at a senior level the operations of registered dealers and advisers.

IDA By-law 7 requires all senior officers and directors of IDA Members to be approved by the Association. IDA By-law 5.4 requires IDA approval of any transaction that permits an individual to obtain a significant equity interest, as defined, in an IDA Member.

The IDA submits that the owners and mind and management of registered dealers and advisers should be directly registered as individuals in order to give the CSA direct regulatory authority over such persons, including the ability (subject to due process) to deny them registration or remove them from office through removal of registration. We submit that it is critical to the CSA public protection mandate that it have the authority to deal with all key players in the capital markets. Many CSA Members are in the position of having the authority to bar individuals from being officers or directors of issuers, but not from being partners, officers or directors of registered dealers. Indeed, with the change to the business trigger, it is hard to understand how the owners and mind of management of registered dealers and advisers could be considered not to be "in the business" of dealing or advising in securities, whether or not they personally deal or advise.

Registration of senior officers, directors, partners and significant shareholders of registered dealers would more readily demonstrate that the proposed rule puts Canada in compliance with Recommendation 23 of the Financial Action Task Force:

> **23.*** Countries should ensure that financial institutions are subject to adequate regulation and supervision and are effectively implementing the FATF Recommendations. Competent authorities should take the necessary legal or regulatory measures to prevent criminals or their associates from holding or being the beneficial owner of a significant or controlling interest or holding a management function in a financial institution.

Sections 2.8 – Ultimate designated person and 2.9 – Chief compliance officer

Sections 2.8 and 2.9 define the roles of the ultimate designated person and chief compliance office. Section 2.7 of the companion policies expands on these descriptions. This structure is already in place for IDA Members in IDA By-law 38.

The IDA supports the Companion Policy's emphasis on compliance being a firm-wide responsibility. We agree that the responsibility for compliance belongs to firms generally, and that compliance should not be viewed as an isolated activity of the compliance department but as an integral part of the member firm's general business activities. However, we believe that the wording of sections 2.8 and 2.9 is inconsistent with that emphasis and with existing IDA rules.

In December 2006, the staffs of the Bourse, the IDA, the MFDA and RS published a Joint Notice on the Role of Compliance and Supervision (Joint Notice) that describes the SRO expectations of the compliance function at member firms and the role, responsibility and accountability of the member, the board of directors, management, compliance departments and compliance officers. The Joint Notice is referenced on a number of occasions in this comment letter and is attached herein as Appendix "A". We suggest that the roles described in the Rule are substantially different from those described in the Joint Notice.

The proposed Rule states that that the CCO is responsible for *discharging* the registered firm's obligations under securities legislation (section 2.9(1)), while the UDP is responsible for *ensuring* that the firm develops and implements policies and procedures for the discharge of the firm's obligations under securities legislation (section 2.8(1)).

We suggest that the description of the CCO's role as currently drafted is beyond the ability of any one person to fulfill and exceeds the authority normally granted to the CCO in a dealer. For example, calculating and maintaining adequate regulatory capital is a regulatory requirement that is best discharged by the CFO and not the CCO as the current draft contemplates. The Companion Policy, however, correctly describes that it is the entire firm's responsibility to discharge the firm's obligations under securities legislation.

In this regard, the Rule's description of the CCO's responsibilities is inconsistent with the more accurate Companion Policy, which notes in section 2.7 that the "CCO may or may not, depending on the firm, also have authority to resolve compliance issues once they have been identified". This contradicts section 2.9(1) of the Rule because a CCO should not be responsible for "discharging" the firm's obligations under securities legislation if she or he does not have the authority to resolve compliance issues.

Not only does the Rule describe the responsibilities incorrectly, but it also contradicts many of the existing SRO rules and established concepts.[1] For example, IDA By-law 38 states that the UDP is responsible to the applicable SRO for the conduct of the firm and the supervision of its employees, and for ensuring that adequate policies and procedures are developed and implemented.[2] The CCO is required to monitor adherence to the member's policies and procedures to ensure management of the compliance function and to provide reasonable assurance that the standards of the applicable SRO are met.[3,4] Clearly, the IDA By-laws require the UDP, if anyone, and *not* the CCO, to discharge the firm's obligations under securities legislation.

Similarly, the MFDA rules provide that the compliance officer is responsible for monitoring adherence by the member to MFDA rules and providing a report on the status of compliance at the member to the board of directors or partners of the firm, while it is the responsibility of

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1 Please review page 3 of the Joint Notice, *supra* note 1, for a discussion on the distinct roles of senior management, management and the chief compliance officer.

2 IDA By-law 38.1.

3 IDA By-law 38.11.

4 In fact, one of the primary reasons for the introduction of the concept of CCO and UDP into the IDA rules was to address the lack of a defined compliance officer role.

the board of directors or partners of the member to act on the report and to rectify any compliance deficiencies noted in the report.[5]

The CCO should not be assigned responsibility under the Rule for discharging the registered firm's obligations under securities legislation because compliance officers generally do not have decision-making authorities. As such, it would be unfair to impose such a duty upon CCOs.

Our view of the rule of the CCO is consistent with that of other jurisdictions. For example, the Securities Industry Association (now known as the Securities Industry and Financial Markets Association), which is an organization that represents more than 650 member firms of all sizes, in all financial markets in the U.S. and around the world, published a White Paper on the *Role of Compliance* (July 2005) [6] that provides an excellent description of the differences between the responsibilities of compliance departments and senior management. In particular, page 10 of the White Paper states:

> "The Compliance Department plays an integral support function for firm compliance programs, but ***only senior management and business line supervisors ultimately are responsible for ensuring firm compliance with laws and regulations.***
>
> ***Compliance Department personnel are not, in most cases, in a position either to remediate wrongful or potentially wrongful conduct, nor to authorize or approve business transactions; only supervisors have the authority and responsibility to make those judgments***. Compliance Department personnel will often provide advice to supervisors in making their judgments. In certain limited circumstances, Compliance Department personnel may have such authority; in those cases the authority has been delegated. There are often limits as to a Compliance professional's ability to detect situations in which employees successfully evade or circumvent compliance systems to engage in improper conduct. Further, ***Compliance personnel usually do not have the power directly to control the behavior of line employees, such as through the traditional powers to hire, fire, or discipline personnel."*** [emphasis added]

However, UDPs, who are considered senior management of the firm, do have the ability to make decisions. As such, we suggest that the Rule be revised such that the UDP is defined accountable for the conduct of the firm while the CCO is responsible for monitoring compliance within the firm and alerting management to compliance issues. We offer specific drafting revisions to Rules 2.8 and 2.9 at Appendix "B", attached.

In addition, the proposed Rule does not allow the firm the option of designating multiple UDPs and CCOs, i.e., a UDP or CCO for each separate business division where a firm is organized into two or more separate business divisions. This is problematic because some large firms are divided along departmental lines, strictly separated so that both heads of department effectively report to the Board or a management committee rather than a single CEO. It may be more appropriate to designate a UDP and CCO for each department.

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[5] MFDA Rule 2.5.2.

[6] Securities Industry Association White Paper on the Role of Compliance (July 2005). Please refer to URL address: http://www.sifmacl.org/attachments/articles/8/Role%20of%20Compliance.pdf (accessed at June 4, 2007).

For example, where a firm has both a retail and institutional division, it may be more appropriate to have one UDP responsible for the institutional division, and another UDP responsible for the retail division. The IDA allows for the designation of a UDP and CCOs for each separate business division, contingent on IDA staff being satisfied that there is a strict separation of departments, including management and compliance staff and reporting.[7] The IDA submits that this practice should be allowed to continue for all firms.

Section 2.8(2) provides that a UDP must be either:

(a) the chief executive officer (CEO) of the registered firm;

(b) an officer in charge of a division of the registered firm, if the activity that requires the firm to register occurs only within that division; or

(c) an individual acting in a capacity similar to that of an officer described in paragraph (a) or (b).

Section 2.8(2) does not expressly include the CCO, CFO or president of the registered firm, as the possible UDP designate. The IDA, however, expressly allows these individuals to be UDPs.[8]

The IDA submits that the definition of UDP is too restrictive in not allowing registered firms the flexibility to designate other senior officials with similar decision-making authority to the CEO. Firms have different operating structures and business lines, such that in some cases it may be more appropriate for a firm's president, COO or CFO to be designated UDP. In some cases the CEO designation is in fact titular, with the most significant management responsibilities being those of another senior officer such as the president.

A number of IDA member firms have already designated the president, CFO, CCO or other officers with the equivalent supervisory and decision-making responsibly as the firm's UDP. This flexible arrangement accommodates the different organization charts and business structures of firms and should be permitted to continue. While the IDA agrees that it is critical to have a member of senior management designated as having direct responsibility for compliance, it has found in its experience with By-law 38 that it is not necessary for the role to be restricted to the CEO.

In order to better illustrate these submissions, the IDA has prepared suggested drafting changes to Rules 2.8 and 2.9, for your consideration (Appendix "A", attached). These suggestions are based, for the most part, on IDA By-law 38.

Section 4.2 – Time limits on examination proficiency

While it is not an issue for the IDA because the proposed Rule does not include proficiency requirements for registered persons with IDA Members, we note that section 4.2(2) effectively lowers the time limit on courses for persons who have been registered from three years to two years, since anyone who has not been registered (or gained equivalent

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[7] IDA By-laws 38.2 and 38.5.
[8] IDA By-law 1.

experience) for two years plus a day cannot meet the requirement. Section 4.2(1) gives someone who has never been registered three years before the exam or course validity expires. We suggest that someone with both the course or exam proficiency and experience as a registered person should have at least the same period before the examination expires as someone who has no experience at all.

The IDA has extensive proficiency requirements beyond the initial course, including required training programs, a period of extra supervision and courses required to be completed within a specific time after initial registration. It also has continuing education requirements for all those approved to deal with the public.

The IDA is currently considering whether its current course and examination re-write requirements, contained in IDA Policy 6, Part II, meet their objectives. We are considering an alternative approach, maintaining the current initial requirements but revoking any re-write requirements in favour of a broader requirement that all Members ensure that their Approved Persons are proficient. There are many alternatives to repeating courses previously taken and many pathways to competence, both within and outside the industry's formal course and examination requirements. The re-write requirements are already a source of numerous case-by-case exemptions.

It is our view that a principles-based approach may be better in that it not only permits firms to make their own assessments and tailor their own training programs for those who have completed the basic requirements, but adds a broader principle that firms have a responsibility to ensure that all their representatives are and remain competent on a continuing basis, whether or not they have taken time out of the industry.

Section 5.3 – Know-your-client

Section 5.3(1)(b) requires a registrant to "take reasonable steps…to ascertain whether a client is an insider of a reporting issuer."

IDA Regulation 1300.2 requires a Member opening a new account to obtain, at a minimum, the information required by IDA Form 2. Form 2 asks whether the client is "a senior officer or director of a company whose shares are traded on an exchange or in the OTC markets" or whether the client controls such a company, alone or as part of a group. The requirement therefore covers all public companies, wherever traded.

The IDA suggests that the CSA consider expanding the requirement to include all public companies. The IDA believes that dealers' gatekeeper responsibilities should not be limited to Canadian reporting issuers, but should extend to all public markets. On that basis it is important for a registered firm to know whether a client is an insider of a public company traded in any market, domestic or foreign.

Although Section 5.3(1)(b) is new as a specific requirement, there is no discussion in the Companion Policy as to what would be considered "reasonable steps." The IDA recommends that Section 5.2 of the Companion Policy add guidance on what the CSA will consider to be reasonable steps in terms of determining whether the client is an insider of a public company.

In this regard, the IDA suggests that the minimum requirement should be a direct question to the client. Beyond that, the IDA believes that a registered dealer should be entitled to accept the client's response unless there are facts about the client that suggest further enquiries are necessary. Such facts could include the client's employment, the source of a referral to the dealer or possession of a large position in a particular issuer's shares. Where the dealer determines that further enquiries are necessary, searches of publicly available databases such as SEDAR in Canada or EDGAR in the U.S. should be deemed sufficient. The selection of databases would depend on the facts giving rise to the determination that additional steps are required.

Section 5.16 – Reduction of debit balances

Section 5.16 contains requirements regarding the transfer of debit balances between derivatives and securities accounts maintained by a registrant for a client.

The IDA does not understand the reason for this section. It provides no apparent client benefit, since dealers have suitability requirements, and can in fact cause exchange risk where the two accounts are in different currencies.

The section does not define "derivatives account." Many IDA Members maintain client accounts that can contain both securities – fixed income and equities – and options. It is unclear whether these would qualify as derivatives accounts and how the rule would apply to them.

The IDA suggests that section 5.16 is unnecessary.

Section 5.20 – Records – form, accessibility and retention

Section 5.20 sets our requirements for records retention. Subsection (4) establishes the concept of activity and relationship records. While the subsection establishes a seven year retention period for both, for activity records the retention period starts at the time of the activity and for a relationship record it starts when the client relationship with the dealer ends.

The IDA agrees with the section itself, but notes that section 5.7 of the Companion Policy includes "(iii) notes of verbal communications with a client" and "(iv) all e-mail, regular mail, fax and other written communications to clients" among relationship records.

The breadth of this definition as drafted is contradictory to the general definition of activity record in the Companion Policy, which notes that "communications between a registrant and its client about particular transactions are also activity records." Many of the notes, e-mails, etc. noted as relationship records are about particular transactions and should be counted as activity records.

The IDA also suggests that the definition should include relationship correspondence both to and from, rather than just to, the client.

Section 5.7 of the Companion Policy also defines complaint records as relationship records, meaning that they would have to be kept until seven years after the client ceases to be a client of the dealer. The IDA suggests that a complaint is in fact a type of transaction, so that the record keeping term should be seven years after the complaint has been resolved – the point at which the transaction is complete. We see little benefit in retaining a complaint file for potentially a very long period after the matter is settled if the client retains the relationship with the dealer.

It is essential that the definitions be clear and simple in this area as privacy legislation requires that firms destroy personal information that they do not have a legal obligation to retain. Any confusion or alternate interpretations of the definitions will leave a firm in an untenable and unnecessarily risky position.

Section 5.25 - Statements of account and portfolio

Section 5.25 requires registered dealers and advisers to send quarterly account statements to clients "unless the client has requested statements on a more frequent basis in which case the registered [dealer or adviser] must send statements on the basis requested by the client. As the section is currently drafted, a client could request daily or weekly statements and the registered dealer would be required to provide them.

The IDA suggests that this section be reworded to either:

- mandate quarterly statements but permit clients to request monthly statements; or
- mandate monthly statements but permit the client the option of requesting quarterly statements.

Section 5.25 requires that the statements contain only details of the debit or credit balance and the securities held in the account. There is no requirement that the statements include details of transactions that have taken place during the period. The IDA suggests that transaction reporting, currently a basic reporting requirement, should be retained.

Section 5.32 - Reporting client complaints to the regulator or securities regulatory authority

Section 5.32 requires that each year a registered firm submit to the regulator or the securities regulatory authority a report on its complaint handling policies that includes the number and nature of the complaints filed as at the end of its fiscal year or as of the date determined by the regulator or the securities regulatory authority.

Section 5.32 does not specify whether a registered firm has to report on all complaints to the securities regulatory authorities in all jurisdictions in which it is registered or only on complaints from clients in the particular jurisdiction. The IDA suggests that the Proposal clarify the requirement in this regard.

The IDA questions the necessity of an annual report on complaint handling policies. These policies tend to be established once and carried forward with little or no change from year to year, other than when new regulations come into effect. IDA and MFDA Members' policies are, like all other policies and procedures, subject to periodic review by the applicable SRO.

The IDA suggests that at most, complaint handling policies should be filed initially and whenever material changes are made.

Proposed National Instrument 11-102 establishes a passport system for registered firms and individuals under which most matters regarding registration will be handled by a Principal Regulator on behalf of the other securities regulatory authorities in jurisdictions in which a firm or individual is registered. If a requirement to file complaint handling policies is retained, the IDA suggests that it would be more administratively sensible and would relate more to the passport approach to registration to have them filed with the Principal Regulator rather than each securities regulatory authority separately.

Section 5.32 is similar to the requirement under the section 168.1.2 of the Quebec *Securities Act*[9], which provides that every securities dealer or adviser must submit to the Autorité des marchés financiers (AMF) a report on the number and nature of complaints filed with the firm.

Member firms of the IDA and MFDA are already required to file reports on written customer complaints with the IDA and MFDA on a complaint by complaint basis.[10] The IDA has entered into an agreement with the AMF under which the IDA provides the AMF with an annual report on the number and nature of certain client complaints reported to the IDA. This way IDA member firms only have to file client complaints with the IDA and not the AMF.

The IDA suggests that a similar procedure be established with the other securities regulatory authorities, so that appropriate SROs would transmit a report on the number and nature of complaints filed to the securities regulatory authorities. This would avoid the potentially cumbersome requirement for member firms to file with all 13 commissions reports that have already been filed with the SROs. However, such a procedure would be most efficient using a common reporting date for all firms rather than one based on fiscal year-end.

We are not suggesting that such an arrangement be made part of the Proposal; we are simply offering to assist in the most efficient implementation of the Section 5.32 requirement.

Section 5.34 – Notice to clients

Section 5.34 requires a registrant that is not resident in a jurisdiction in which he, she or it operates to provide a disclosure to each of his, her or its clients.

This provision appears to apply to non-resident registered individuals, even where the firm itself is resident and to firms that do business across the country but do not maintain offices in each jurisdiction, such as discount dealers that conduct most of their business on-line or by telephone.

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9 R.S.Q. c. V-1.1.

10 IDA Policy No. 8, section 1(c) and MFDA Policy No. 3 and proposed Policy No. 6 (currently seeking CSA approval).

The IDA cannot see the need for this additional disclosure. The firm itself will in many cases be resident in the jurisdiction and information like addresses for service is readily available from the securities regulatory authorities, often on-line. Furthermore, we would hope that the registration system and requirements ensure that clients are not left with the risk that legal rights are not enforceable against a registrant.

Section 6.1 – Conflicts management obligations

Question 12 of the Notice and Request for Comment asks whether the conflicts of interest requirements should include a materiality concept. The IDA supports the addition of a materiality test to the conflicts of interest management requirements.

It has been widely observed that there are numerous conflicts of interest in the securities industry, some of them built into basic structures and processes such as underwriting and commission-based compensation. In such an environment it is all too easy to identify potential conflicts of interest everywhere, even where there is little likelihood of untoward activity because of the potential.

Many material conflicts of interest are already the subject to direct requirements. For example, the supervision of accounts to ensure suitability of investment recommendations is in part designed to ensure that representatives base their recommendations on the client's best interests rather than in their own interest in generating commission income.

It is important that in looking beyond specific control requirements, registrants concentrate their attention and resources on matters of importance. Trying to anticipate and control every potential conflict, no matter how trivial, will divert their attention and attenuate the resources needed to deal with serious conflicts. A materiality concept does not remove the requirement to identify potential conflicts of interest, and the results of a materiality assessment will always be open to question, but at least it gives registrants the ability to reach reasonable decisions on their risks and apportionment of resources to deal with those risks.

Section 6.3 – Registrant relationships

Section 6.3 prohibits dual registration as a dealing, advising or associate advising registration with two or more registered firms unless they are affiliates.

While recognizing that there are circumstances in which registration with affiliated firms is appropriate, the IDA has concerns about the potential for conflicts of interest in the situation and the splitting of supervisory oversight. In the latter regard the situation may be aggravated by privacy prohibitions that prevent one affiliate from seeing information about clients and transactions at the other. Similarly, regulatory oversight may be split where the affiliates are not members of the same SRO or one is a member of a SRO and the other is not.

There is nothing in the Companion Policy about when dual registration is permissible. The IDA suggests that dual registration at affiliates should be permissible under the rule, but should be subject to guidelines. It would be appropriate for those guidelines to be part of the Companion Policy.

Section 9.17 – Sub-advisers

Section 9.17 exempts non-resident sub-advisers for registered advisers and dealers providing portfolio management services. However, section 9.17(f) removes the exemption for Canadian sub-advisers in Manitoba.

This is the sole instance in the proposed Rule of an exception in one jurisdiction. It detracts from the efforts of the CSA to harmonize registration requirements. Given that the customer protection requirements are squarely on the adviser hiring the sub-adviser, it provides no useful addition to customer protections. It may in fact limit the availability of good sub-advisers to advisers and dealers in Manitoba. The IDA urges the Manitoba Securities Commission to eliminate this unnecessary exception.

French Language Terms and Translation

The Regulation Committee of the Quebec District Council of the IDA has identified a number of issues with the terminology in the French language version which are attached as Appendix C.

Conclusion

Thank you for this opportunity to comment on proposed National Instrument 31-103 *Registration Requirements* and Proposed Companion Policy 31-103. Despite the issues raised above, the IDA believes that the overall Proposal constitutes a major step towards more harmonized and efficient regulation.

Yours truly,

Joseph J. Oliver
President

Appendix "A"

Suggested drafting amendments to rules 2.8 and 2.9 of proposed National Instrument 31-103 *Registration Requirements*:

Ultimate designated person

2.8 (1) A registered firm must designate its chief executive officer, its president, its chief operation officer or its chief financial officer (or such other officer designated with the equivalent supervisory and decision-making responsibility) to act as the ultimate designated person (UDP).

(2) The UDP shall be responsible to the applicable regulator for the conduct of the registered firm and the supervision of its employees.

(3) The UDP must ensure that the registered firm develops and implements policies and procedures that adequately reflect the regulatory requirements of the registered firm.

(4) Where the registered firm is organized into two or more separate business units or divisions, a registered firm may designate a UDP for each separate business unit or division.

(5) An individual designated under subsection (1) must be registered by the regulator in the category of UDP.

Chief compliance officer

2.9 (1) A registered firm must designate an officer, director or partner of the registered firm, or if the registered firm is a sole proprietorship, the sole proprietor, to act as the chief compliance officer (CCO).

(2) The CCO shall be responsible for monitoring adherence to the registered firm's policies and procedures as necessary to ensure that the management of the compliance function is effective and to provide reasonable assurance that the registered firm meets its obligations under securities legislation.

(3) Where a registered firm is organized into two or more separate business units or divisions, the registered firm may designate a CCO for each separate business unit or division.

(4) An individual designated under subsection (1) must be registered by the regulator in the category of CCO.

Appendix "B"

MEMBER REGULATION

notice

INVESTMENT DEALERS ASSOCIATION OF CANADA

ASSOCIATION CANADIENNE DES COURTIERS EN VALEURS MOBILIÈRES

ATTENTION:
Ultimate Designated Persons
Chief Financial Officers
Panel Auditors

Please distribute internally to:
Corporate Finance
Credit
Internal Audit
Legal & Compliance
Operations
Registration
Research
Retail
Senior Management
Trading Desk

Contact:

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MR0435

November 30, 2006

Joint Notice of the Staff of Market Regulation Services Inc., Mutual Fund Dealers Association of Canada, Bourse de Montréal Inc., and the Investment Dealers Association of Canada

The Role of Compliance and Supervision

Introduction

Industry compliance professionals play an important role in the system of securities regulation. Self regulatory organizations ("SRO") and industry compliance professionals have a common objective to promote compliance at firms and set industry standards. In order to achieve this objective, SROs need to be absolutely clear in their expectations of the chief compliance officer ("Chief Compliance Officer"), the compliance department ("Compliance Department") and the member firm, including its management.

The purpose of this Notice is to provide Members and Participants (collectively, "Member" or "Members") with SRO expectations of the compliance function at Members and the role, responsibility and accountability of the Member, the board of directors, management, Compliance Departments and compliance officers ("Compliance Officer").

The SROs have issued notices and bulletins in the past that address many of the matters outlined below.[11] In addition, there are specific SRO rules that deal with supervisory and compliance responsibilities. This Notice should be read in conjunction with those regulatory instruments.

Responsibility for compliance

The responsibility for compliance belongs to the Member generally: the board of directors, management, supervisors and those fulfilling the compliance function. Compliance should not be viewed as an isolated activity of the Compliance Department but as an integral part of a Member's general business activities. Within that general framework, it is the responsibility of the board of directors, management and supervisors to consider and implement the advice from those performing a compliance function.

The role of the Compliance Department is to identify, assess, advise on, communicate, monitor and report on the Member's compliance with regulatory requirements.

Distinction between supervisory and compliance roles

Compliance Departments and Compliance Officers, while they carry out similar functions across firms, have responsibilities tailored to the size, resources and business needs of the particular Member. In some cases their sole responsibility will be fulfilling the compliance function; in others they may also have supervisory roles.

In contrast to the compliance role described above, a person in the role of "supervisor" has authority for the day-to-day management of a business function or area which includes the supervision of individuals and the authority to implement changes to how the business function or area is run. The difference between supervisory and compliance roles is defined by who has the authority to resolve issues once they are identified.

For example, if an issue is identified by a Compliance Officer and referred to a branch manager for resolution, the Compliance Officer is executing a compliance function only. In doing so, the Compliance Officer may also, while still conducting a compliance function, be checking on the efficacy of the branch manager's reviews. As long as the authority to effect change resides with the branch manager, he or she is in the supervisory role. In those circumstances where Compliance Officers have the express authority to effect change they are also exercising a supervisory role.

In determining whether an individual is acting in a supervisory role, the SROs will look at the individual's responsibilities, authority and the functions he or she performs for the Member, not simply at his or her title. While the SROs will consider documentation setting out an individual's responsibilities and authority, they will also look to confirm whether these are reflected in the day-to-day operations of the firm. In other words, it is a two-fold test: documentation and practice.

The activities of those exercising compliance functions should not be viewed by supervisors as a substitute for their responsibility to supervise the business of the firm. Supervisors still retain ultimate authority over, and are ultimately accountable for, business activities and the people they supervise when issues arise, and supervisors must remain vigilant in carrying out their responsibilities.

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[11] IDA Compliance Interpretation Bulletin C-130, July 12, 1999 *Accountability of Compliance Officers in Disciplinary Actions*

Bourse's Circular No. 017-2003, February 18, 2003 *Surveillance and Compliance*

MFDA Member Regulation Notice MR –0037, March 16, 2005 *Compliance Responsibilities*

RS Market Integrity Notice No. 2003-025, November 28, 2003 *Guidelines on Trading Supervision Obligations*

RS Market Integrity Notice No. 2005-011, April 1, 2005 *Provisions Respecting Manipulative and Deceptive Activities*

In some instances, the Compliance Officer may also have supervisory responsibility, for example, as a branch manager. The risks of such consolidation should be carefully considered when outlining the responsibilities of each position.

Role of the Member, board of directors, management and the Compliance Officer

The Member

The Member is responsible for establishing, implementing, communicating and maintaining effective compliance programs to ensure compliance with applicable laws and regulations. This responsibility extends to all directors of the Member with respect to their corporate governance responsibilities and all officers of the Member with regard to areas of their management responsibility.

The Board of Directors

The board of directors must ensure that the Member maintains a compliance program that identifies and addresses material risks of non-compliance and that appropriate supervision and compliance procedures to manage those risks have been implemented. The board has responsibility to act on reports from the Compliance Department as outlined below.

Management

Senior management has responsibility to establish and maintain a Member's overall compliance system. All management has the responsibility to supervise and to direct the activities of the Member and the individuals within the Member firm to achieve compliance with applicable laws and regulation with respect to areas of their management responsibility.

The Chief Compliance Officer[12]

The Chief Compliance Officer must report the results from its monitoring to management and the board of directors at least annually, but should have direct access to senior management as needed to report significant issues as they arise. The mandate of the Chief Compliance Officer is to provide the board of directors with *reasonable* assurance that all standards and requirements of applicable laws and regulations are met.

The Compliance Officer

A Compliance Officer's responsibility is to monitor compliance and take appropriate steps to assist in ensuring that corrective measures are being taken by supervisors or managers to remedy any issues that are identified. It is not enough to simply identify issues. Compliance Officers in their advisory capacity should communicate their findings to the appropriate manager and recommend appropriate corrective measures. If performing solely a compliance function, the steps will involve advising supervisors or managers who have the authority to direct what must be done.

Compliance Officers must also monitor the corrective measures taken. If supervisors do not adequately address problems, the Compliance Officer must escalate the problem as appropriate. Escalation procedures should be detailed in the firm's procedures. In some cases the Compliance Officer may raise the issue with a higher level supervisor, in others, to the Chief Compliance Officer, who must ensure that the problem is escalated within the Member to a higher management level or, where appropriate, the board of directors.

The steps taken by Compliance Officers and corrective actions taken by supervisors must be documented, maintained and auditable.

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[12] The term "Chief Compliance Officer" is not used by the MFDA or RS. Unless otherwise indicated, references to "compliance officer" in this Notice include individuals designated as the Chief Compliance Officer.

Other Individuals

Other individuals in the Member firm must also comply with the Member's compliance program.

When individuals will be subject to enforcement action by SROs

The standard against which the conduct of board members, management, Compliance Officers and other individuals will be measured in a discipline hearing is that of a reasonably proficient and diligent individual in that position. The standard is an objective one; it is not what the respondent actually knew or did but rather what he or she ought to have known or done. It is always open to the individual to demonstrate that they exercised due diligence to prevent the harm that occurred.

A Compliance Officer may be subject to enforcement action if she or he violates securities laws or aids and abets another in such violations. A Compliance Officer may be subject to enforcement action for failing to supervise if she or he has been specifically delegated, or has assumed, supervisory authority for particular business activities or situations, and therefore has the requisite degree of responsibility, ability or authority to affect the conduct of the individual in the Member firm whose behavior is at issue. A Compliance Officer may be subject to enforcement action if she or he fails to identify rule violations according to the standard of a reasonably proficient and diligent Compliance Officer, or, if after identifying the violation, he or she fails to sufficiently escalate and follow up the issue with management, in accordance to the standard of a reasonably proficient and diligent Compliance Officer. What is sufficient escalation and follow-up will often be fact specific. If the SRO is satisfied that the Compliance Officer has met these regulatory expectations he or she will not be subject to an enforcement action.

Creating an Effective Compliance Program

In order to be effective, compliance programs must be reasonably designed to identify and control the risk of compliance failure that could result in investor and/or market harm and financial losses and reputational damage to the Member.

Members have an obligation to develop and implement effective compliance programs, which includes: allocating sufficient resources; creating measures and systems that encourage and reward compliant behaviour and discourage non-compliant behaviour; and ensuring that Compliance Officers have appropriate access to senior management. There are many steps that a Member can take to promote the importance of compliance, including the following:

(i) Promote a culture of compliance by clearly identifying, prioritizing and communicating compliance goals.

(ii) Insist on compliance and high ethical standards throughout the Member with senior management leading by example.

(iii) Ensure that effective execution of compliance and supervisory roles is an explicit element of compensation and promotion decisions.

(iv) Ensure that others in the firm have a clear understanding of the role of Compliance Officers and the Compliance Department.

(v) Communicate compliance and regulatory information to individuals within the Member. Emphasize compliance and regulatory subjects in training. Training should include educating individuals about their compliance responsibilities on an ongoing basis.

(vi) Make available to all individuals an effective means of communicating (confidential or anonymous, if appropriate) compliance, regulatory or ethical concerns to Compliance Officers , senior management or the board of directors if necessary without fear of retaliation.

(vii) Encourage the development, training, professionalism and retention of the Member's Compliance Officers with compensation, benefits and recognition in keeping with their contributions; and implement sanctions or other corrective actions for non-compliant behaviour. Further, staff the Compliance Department with sufficient, qualified, experienced and knowledgeable professionals.

(viii) Ensure sufficient access to information for Compliance Officers to enable them to carry out their responsibilities.

(ix) Develop a cooperative relationship between regulators and Members.

Tips for Compliance Officers

There are many steps that Compliance Officers can take to ensure that they have discharged their responsibilities in connection with the expectations of SROs including the following:

(i) Ensure that they have a clear understanding of the nature of their responsibilities. This includes having a detailed job description with clearly established reporting lines and a clear understanding of whether they are expected to act in a supervisory capacity.

(ii) Maintain written records that detail all steps that were taken to either correct, report or escalate issues that were identified along with any supporting documentation which demonstrates actions taken.

(iii) Lawyers who perform compliance functions in additional to legal functions should make it clear to other individuals when they are acting as legal counsel and providing legal advice.

(iv) Compliance Officers should be active in promoting compliance related initiatives both inside and outside the Member and be available to individuals within the Member for consultation on compliance issues.

(v) Ensure steps in the compliance process are appropriately tailored to the size and nature of the Member's business and that they are tested to ensure that they adequately address any compliance gaps.

(vi) Ensure that SRO rule changes, bulletins and notices are reviewed and incorporated into the Member's compliance policies and procedures in a timely and effective manner which addresses the nature and size of the Member's business.

(vii) Compliance policies and procedures should be constantly reviewed, tested and updated to ensure that existing procedures continue to effectively reflect the business practices of the Member and are in compliance with new rules and regulations.

(viii) Periodically review the websites of provincial regulators and the SROs and where possible attend SRO meetings or seminars devoted to regulatory issues. Doing so will give Compliance Officers advance notice of proposed and imminent rule changes that may affect the Compliance Officer and the Member firm.

(ix) Develop a cooperative relationship between regulators and Members.

Appendix C

1. Définitions et interprétation :

Plusieurs notions essentielles du projet de règlement ne sont pas définies à l'article 1.1 ni à la norme canadienne 14-101. Dans le cadre de cette importante réforme, il serait important de définir les termes utilisés dans le règlement. Nous avons aussi constaté l'utilisation de termes différents référant aux mêmes concepts. Nous recommandons de procéder à une réévaluation des termes utilisés dans le cadre du projet de règlement afin de s'assurer que les mêmes termes réfèrent aux notions similaires. (Par exemple, personne physique inscrite et personne inscrite à la partie 5 semblent référer aux mêmes personnes; 4.13 Société de gestion - chef de la conformité : la notion de société de gestion n'est pas présente dans le règlement. On trouve uniquement le terme société de gestion inscrite – voir art. 1.1). Afin de faciliter la compréhension des termes utilisés, nous recommandons aussi de regrouper les définitions dans un seul instrument – soit au début du projet de règlement ou dans le Règlement 14-101. Le regroupement des définitions facilite la compréhension de la règle édictée.

2. Catégories d'inscription :

L'exercice entrepris dans le cadre de ce projet d'inscription constitue une opportunité unique de revoir la dénomination des catégories d'inscription de manière à s'assurer qu'elles traduisent clairement les activités que les firmes ou les individus sont autorisés à effectuer. Nous croyons que le choix des dénominations, tant pour les personnes physiques que morales, doit faciliter la compréhension et surtout les distinctions entre les uns et les autres.

2.1 Catégories liées aux Sociétés :

2.1.1 Distinguer les personnes morales des personnes physiques

Notre premier commentaire a trait à la catégorie d'inscription des firmes. Les termes 'courtier' et 'conseiller' ne reflètent pas, de prime abord, le caractère moral des entités visées. En fait, pour une large partie de la population, les notions de 'courtier' et de 'conseiller' réfèrent à des personnes physiques et non à des personnes morales. Pour éviter toute confusion et surtout pour assurer que les titres de catégories retenus permettent de bien cerner les distinctions entre les personnes morales et les personnes physiques, nous recommandons d'identifier les personnes morales en référant à une notion telle que Société de courtage, ou Maison de courtage, ou Firme de courtage.

2.1.2 Refléter les activités permises

Nous croyons aussi que les sous-catégories d'inscription dans le secteur du courtage auraient avantage à être regroupées et renommées afin de refléter la nature des services offerts de même que la réalité de notre industrie. Le terme ‘courtier en placement’ ne reflète en rien la pratique actuelle. Alors que le titre ‘investment dealer’ est usuel dans le reste du Canada, la référence à ‘courtier en placement’ est étrangère à notre industrie au Québec. En fait, cette nouvelle nomenclature est de nature à susciter de la confusion – le terme placement référant entre autres au secteur de l’emploi – et est très réductionniste par rapport à l’éventail des fonctions exercées par un courtier en valeurs mobilières de plein exercice.

En outre, les différentes catégories d’inscription pour les personnes morales écartent toute référence à la notion d’exercice de la profession restreint à certains produits. Cette référence donne pourtant à un investisseur de l’information sur le caractère limité des activités qu’une firme est en droit d’exercer. Nous constatons aussi que les catégories actuelles placent sur un même pied les ‘courtiers en placement’ qui peuvent conseiller et vendre plusieurs produits et les autres catégories de courtiers qui sont restreints dans le choix des produits qu’ils peuvent offrir à leurs clients.

- Nous proposons plutôt deux sous-catégories se subdivisant:
  - Firmes de courtage en valeurs mobilières
  - Firmes de courtage d’exercice restreint :
    - Firmes de courtage en épargne collective
    - Firmes de courtage en plans de bourses d’étude
    - Firmes de courtage sur le marché dispensé
    - Firmes de courtage de titres déterminés

2.1.3 La catégorie de conseiller

Le projet propose de regrouper sous la catégorie ‘conseiller’, les gestionnaires de portefeuille. Nous ne comprenons pas la logique sous-jacente au choix de cette dénomination pour désigner les firmes de gestion de portefeuille.

La référence à la notion de conseiller est de nature à générer de la confusion. En effet, les firmes de courtage peuvent aussi et doivent dans certains cas prodiguer des conseils à leurs clients. Tel que présenté, cette catégorie d’inscription semble limiter la fonction de conseils aux seuls gestionnaires de portefeuille. Pourtant tel n’est pas le cas. Nous croyons qu’il y aurait lieu de revoir cette formulation et d’identifier cette catégorie sous le vocable de ‘Firme de gestion de portefeuille’ ou ‘Firme de gestion de patrimoine’.

Le caractère discrétionnaire du mandat confié aux gestionnaires de portefeuille pourrait aussi être spécifié dans le titre de la catégorie d’inscription lorsqu’il s’applique. Cette mention assurerait une meilleure compréhension de la distinction qui existe entre les firmes qui offrent un tel service et les autres catégories d’inscription.

2.2 Catégories liées aux individus :

Les cinq catégories d'inscription liées aux individus pourraient se diviser en deux sections, dans un souci de faciliter la compréhension du texte :

Les personnes qui conseillent leurs clients :

a) Représentant de courtier
b) Représentant-conseil
c) Représentant-conseil adjoint

Les personnes qui occupent des fonctions de responsabilités :

d) Personne désignée responsable
e) Chef de la conformité

Nous constatons aussi que le choix de la dénomination des catégories d'inscription, pour les individus, n'est nullement en lien avec la réalité, du moins celles identifiées sous le titre de 'représentant de courtier'.

Il nous apparaît important, tant pour notre industrie que dans l'intérêt public, de s'assurer que la dénomination des catégories retenues soient en lien avec les fonctions exercées. Le terme 'courtier' suivi du secteur de services offerts est courant dans d'autres secteurs d'activités. En pareille circonstance, le terme courtier réfère à un individu. Ainsi, une catégorie courtier en valeurs mobilières plutôt que représentant de courtier, nous apparaît plus près de la réalité et plus significatif pour un investisseur qui prend connaissance du règlement.

La notion de représentant-conseil suscite plusieurs questions et de l'incompréhension. Si vous faites référence à un gestionnaire de portefeuille ou à un gestionnaire de patrimoine, il serait plus approprié de changer le titre de cette catégorie pour une dénomination qui permet une meilleure compréhension des activités que peut exercer cette personne physique. La dénomination retenue pour les personnes physiques devrait être en lien avec la dénomination retenue pour les firmes. Si la catégorie de représentant-conseil vise d'autres activités, nous considérons qu'il serait approprié de s'assurer que le titre permette d'identifier facilement les activités qu'il lui est permis d'exercer.

Nous avons de la difficulté à saisir la catégorie de personnes visées sous la dénomination représentant-conseil adjoint. Le paragraphe 2.5 de l'Instruction générale indique que cette catégorie vise les personnes physiques qui ne satisfont pas aux obligations de formation et d'expérience lui permettant de s'inscrire comme représentant-conseil d'un gestionnaire de portefeuille. S'agit-il d'une catégorie équivalente aux gestionnaires adjoints de portefeuille approuvée par l'ACCOVAM ? Inclut-on dans cette catégorie des personnes physiques qui agissent comme apprentis ? Doit-on comprendre que cette catégorie n'est assortie d'aucune exigence de formation ou d'expérience ?

L’exigence d’inscription devrait aussi viser les personnes qui dans leurs fonctions sont en relation avec les clients. L’absence de formation et d’expérience qui semble s’appliquer à cette catégorie d’inscription nous laisse perplexes si les personnes visées par cette catégorie sont autorisées à donner des conseils à des clients et ce même si pareils conseils doivent être pré-approuvés par le ‘représentant-conseil’. Les personnes dont les fonctions sont de nature purement administrative – les adjoints au gestionnaire de portefeuille par exemple – ne devraient pas être visées par cette catégorie d’inscription.

Nous aimerions obtenir plus d’information sur l’identité des personnes visées par cette catégorie d’inscription.

3. Identification d’erreurs typographiques et autres :

Partie 2, 2.1, Lorsque le courtier s’inscrit auprès de l’agent responsable, il doit…

Partie 5; 5.2 La société inscrite ~~tient~~ maintient la documentation d’ouverture…

Partie 8, 81.3)c. à un marché, à un OAR ou à un organisme ~~ou~~ de réglementation

Réécriture :
L’article 6.9 Règlement des opérations sur titres
Cet article appelle une réécriture tant en anglais qu’en français. Tel que rédigé, il s’avère extrêmement difficile à comprendre.