CSA/ACVM Canadian Securities Administrators Autorités canadiennes en valeurs mobilières

CSA Staff Notice 31-334
CSA Review of Relationship Disclosure Practices

July 18, 2013

Introduction

Staff from the Canadian Securities Administrators in various provinces (CSA staff or we) reviewed the relationship disclosure practices of registered portfolio managers (PMs) and exempt market dealers (EMDs) (the review). This notice summarizes our findings from the review and provides staff guidance on relationship disclosure information (RDI) practices. We will apply the guidance in this notice when assessing the relationship disclosure practices of registered firms, where appropriate. We also encourage registered firms to use this notice as a self-assessment tool to determine how they can improve their relationship disclosure practices.

Background

Section 14.2 of *Regulation 31-103 respecting Registration Requirements, Exemptions and Ongoing Registrant Obligations* (Regulation 31-103) requires PMs and EMDs to provide clients with RDI. *Policy Statement to Regulation 31-103 respecting Registration Requirements, Exemptions and Ongoing Registrant Obligations* (Policy Statement 31-103) provides guidance on relationship disclosure requirements.

Objectives of the Review

The main objectives of the review were to:

- assess compliance by PMs and EMDs with relationship disclosure requirements and related securities legislation
- broaden our understanding of the current practices surrounding relationship disclosure (i.e. preparing, reviewing, delivering and revising disclosure documents)
- develop a harmonized compliance approach across Canada when reviewing a firm's relationship disclosure practices

Scope and Methodology

In November 2011, we sent a questionnaire to a representative sample of 124 registered firms across Canada. The sample included:

- 46 firms registered only as PMs
- 26 firms registered only as EMDs
- 52 firms registered in multiple categories, such as PM, EMD and investment fund manager (IFM)

The firms sampled primarily provided products and services to retail, private and institutional clients. The questionnaire asked the firms to provide information about how they meet the relationship disclosure requirements. We assessed the firms' responses against the requirements

in applicable securities legislation, including subsections 14.2(1) and 14.2(2) of Regulation 31-103.

Outcome

Where we identified deficiencies, we sent a compliance deficiency report to the firm. Most CSA jurisdictions required firms to submit a written response to the deficiencies and any revised RDI documents. CSA staff reviewed these responses to ensure that each firm addressed any RDI deficiencies. Firms in certain CSA jurisdictions were notified that we would review the identified deficiencies on the next scheduled compliance examination. Where we continue to have concerns with a firm's actions in resolving the deficiencies, we may consider appropriate regulatory action.

Regulatory Requirements

When assessing the responses to our questionnaire, we primarily considered the requirements in Regulation 31-103. Subsection 14.2(1) of Regulation 31-103 requires a registered firm to deliver to a client all information that a reasonable investor would consider important about the client's relationship with the registrant. Given this, it is not our intention to prescribe all of the RDI that a registered firm may provide to their clients. Registered firms should consider what other RDI should be provided to their clients to meet the requirements of subsection 14.2(1).

Our intention is to provide guidance on subsection 14.2(2) which requires a registered firm to deliver specific information to a client, and subsections 14.2(3) and (4) which prescribes when the registered firm must deliver and revise RDI to clients. We also considered the requirement that a registrant deal fairly, honestly and in good faith with clients[1].

Since the review, the relationship disclosure requirements in Regulation 31-103 have been amended, with the implementation of the new amendments under Phase 2 of the Client Relationship Model Project starting on July 15, 2013 (the CRM2 Amendments). Policy Statement 31-103 has also been amended with expanded discussion of the RDI requirements, as well as with the addition of guidance corresponding to the new requirements in the CRM2 Amendments. For more information, please refer to the CSA Notice of Amendments to *Regulation 31-103 respecting Registration Requirements, Exemptions and Ongoing Registrant Obligations* and to *Policy Statement to Regulation 31-103 respecting Registration Requirements, Exemptions and Ongoing Registrant Obligations* (Cost Disclosure, Performance Reporting and Client Statements) published on March 28, 2013 (CRM2 Notice)[2].

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[1] In the participating jurisdictions, this requirement is in section 75.2 of the Securities Act (Alberta), section 14 of the Securities Rules (British Columbia), subsection 154.2(2) of the Securities Act (Manitoba), subsection 54(1) of the Securities Act (New Brunswick), section 39A of the Securities Act (Nova Scotia), section 2.1 of Ontario Securities Commission Rule 31-505 Conditions of Registration, section 160 of the Securities Act (Quebec), section 26.2 of the Securities Act (Newfoundland and Labrador), and subsection 33.1(1) of the Securities Act (Saskatchewan). In Manitoba, subsection 154.2(2) further requires registered firms with discretionary authority to act in the client's best interests.

[2] CRM2 Notice is available on websites of CSA jurisdictions.

This staff notice identifies the relationship disclosure requirements at the time of the review, and we also draw attention to clarifications and changes that are effective as of July 15, 2013. Note that there are other new requirements in the CRM2 Amendments that will come into effect starting on July 15 in each of 2013, 2014, 2015 and 2016. Registrants should refer to the CRM2 Notice for more detail about all of the CRM2 Amendments. Firms are expected to identify and implement all necessary steps to ensure their compliance with these amendments.

Concerns with Deficient Client Relationship Disclosure Information

Clients may rely on and make decisions based on a registered firm's RDI. As a result, the RDI should be fulsome and provide meaningful information. If the RDI is deficient, clients may:

- misunderstand the type of services and investment products the registered firm offers and is authorized and able to provide
- incorrectly gauge the level of risk of an investment product or strategy
- not be aware of the fees and costs associated with an investment product or account
- not be aware of conflicts of interest between the registered firm and the client

Preparing, reviewing, delivering and revising relationship disclosure information

Practices

As part of the review, we asked registered firms how they prepared, reviewed, delivered and revised RDI. We found the following acceptable practices:

- firms provided RDI in separate documents, such as the Investment Management Agreement (IMA), Advisory Agreement, Investment Policy Statement (IPS), Know Your Client (KYC) forms and offering documents, which together gave the client the required information
- firms typically provided RDI to clients at the time of account opening, and at the very least, before making or advising the client to make an investment
- firms personally delivered RDI to the client, and if that was not possible, sent it to the client by mail, electronically or by fax
- firms required clients to acknowledge receipt of the disclosure documents
- firms kept signed copies of all relationship disclosure documents either in hard copy or electronic format
- firms advised clients in a timely manner if there was a significant change to the RDI by letter, phone or email, and required clients to acknowledge the change

While most registered firms had a process for reviewing the disclosures provided to clients, some did not have policies and procedures specifically designed to address the requirements under section 14.2 of Regulation 31-103. This practice is not consistent with the requirements in section 11.1 of Regulation 31-103 (compliance system).

Guidance

We intend the following guidance to assist registered firms with preparing, reviewing, delivering and revising RDI:

- Under section 11.1 of Regulation 31-103, registered firms must have policies and procedures that establish a system of controls and supervision sufficient to provide reasonable assurance

that the firm and each individual acting on its behalf complies with securities legislation. This extends to the relationship disclosure requirements. Written policies and procedures should reflect the registered firm's practices when preparing, reviewing, delivering and revising relationship disclosure documents.

- RDI should contain accurate, complete and up-to-date information. We suggest that registered firms review their RDI annually or more frequently, as necessary. Subsection 14.2(4) requires registered firms to take reasonable steps to notify clients, in a timely manner, of significant changes in respect of the RDI delivered to a client.
- The RDI that registered firms provide to clients should contain meaningful, understandable information that enables clients to make informed investment decisions.
- Registered firms should ensure that the RDI clearly explains the products and services the firm offers, contains adequate description of the fees and costs associated with those products and services, and provides sufficient explanations of the risks a client should consider when making investment decisions.

In addition to the foregoing, please note that as of July 15, 2013:

- Subsection 14.2(3) of Regulation 31-103 prescribes when RDI is to be delivered to the client. As of July 15, 2013, it specifies that registered firms must deliver the information referred to in subsection 14.2(1), if applicable, and subsection 14.2(2) to the client in writing. However, the firm may provide the information in paragraph 14.2(2)(b) orally or in writing. If firms choose to provide the information in paragraph 14.2(2)(b) orally, they should maintain evidence of the discussion[3].
- The language of certain requirements in section 14.2 is amended to clarify where a general description of RDI is sufficient.
- The guidance about RDI communication in Policy Statement 31-103 is expanded.
- New subsection 14.2(5.1) prohibits registered firms from imposing any new or increased operating charge in respect of a client's account unless 60 days prior written notice is provided.
- The cost disclosure requirements are now more specific, and firms are now required to separately disclose applicable information about "operating charges" and "transaction charges" (paragraphs 14.2(2)(f) and (g)). These terms are defined in section 1.1 of Regulation 31-103 and there is guidance on their meanings in section 14.2 of Policy Statement 31-103. The term "costs" in section 14.2 of Regulation 31-103 is replaced with the term "charges" to avoid confusing the charges associated with the operation of an account or executing transactions with the purchase cost of a security.

Summary of Results

We identified a number of deficiencies in the RDI that registered firms must deliver to clients under subsection 14.2(2) of Regulation 31-103. The following is a list of these requirements ranked in order of most to least identified deficiencies:

[3] The CRM2 Amendments include guidance in section 14.2 of Policy Statement 31-103 about keeping evidence of compliance with client disclosure requirements.

- Description of the risks of using borrowed money to finance a purchase of a security – paragraph 14.2(2)(d)
- Information a firm must collect about the client (Know Your Client) – paragraph 14.2(2)(l)
- Statement that the firm has an obligation to assess suitability prior to executing a transaction – paragraph 14.2(2)(k)
- Description of the content and frequency of reporting for each account or portfolio of a client – paragraph 14.2(2)(i)
- Description of the types of risks that a client should consider when making investment decisions – paragraph 14.2(2)(c)
- Description of the nature or type of client account –paragraph 14.2(2)(a)
- Description of the conflicts of interest the firm is required to disclose to a client – paragraph 14.2(2)(e)
- Disclosure of all costs to a client for the operation of an account, and description of the costs clients will pay in making, holding and selling investments – paragraphs 14.2(2)(f) and 14.2(2)(g)
- Discussion that identifies the products or services offered by the firm – paragraph 14.2(2)(b)
- Description of the compensation paid to the firm in relation to different types of products that a client may purchase – paragraph 14.2(2)(h)

Specific Issues and Guidance

The following section discusses the requirements under subsection 14.2(2) in the order they are stated in that subsection, and provides details about the findings, as well as guidance to registered firms in order to meet their obligations.

1. Describe the Nature or Type of the Client's Account

Under paragraph 14.2(2)(a), a registered firm must provide clients with a description of the nature or type of account that the client has with the firm. In particular, the registered firm should provide the client with sufficient information to enable the client to understand the type of accounts they hold, how the accounts will operate, and the services associated with the accounts.

22% of registered firms sampled were deficient in this area.

We found the following deficiencies:

- Firms did not disclose the type or nature of account that they managed for the client, or the disclosure was unclear.
- The disclosure did not discuss in what capacity the firm was acting on behalf of the client, for example, if the PM had discretion over the account or if the firm was acting as an EMD for the client.
- Some EMDs did not think they were required to disclose this information since their relationship with the client existed only on a transactional basis.

Guidance

PMs

RDI should disclose that the registered firm acts as a PM for the client and indicate whether the client has a discretionary or non-discretionary account. While there is no need to specify the type of account that the client holds (for example, registered, cash, etc.), PMs should describe the type of services that they will provide to the client and disclose where the client assets are held (for example, if they are held at a custodian).

EMDs

RDI should disclose that the firm acts as an EMD for the client. EMDs should describe how they will operate client accounts and outline the services that they will provide to their clients. EMDs should disclose where and how assets are held, for example, that they will be held in client name with the issuer of the exempt securities.

2. Identify the Products or Services the Registered Firm Offers

Paragraph 14.2(2)(b) requires a registered firm to include a discussion that identifies the products or services the registered firm offers to clients[4]. The registered firm should provide and disclose:

- sufficient information to identify the types of products or services the firm is registered to provide
- what parameters the firm will use to select investments
- information about all registerable activities or types of business involving the registered firm

11% of registered firms sampled were deficient in this area.

We found the following deficiencies:

- PMs provided information about their investment mandate, but did not specifically discuss the types of securities that they invest in to fulfill that mandate.
- Registered firms did not explain to clients that the description of products or services was located elsewhere than in the RDI (i.e., in their engagement letter, on their website or in a related offering document).
- Firms registered in multiple categories provided disclosure relating to one segment of their business, but not for other activities they are registered to provide.
- Registered firms identified the products that they offered, but did not discuss the services.

Guidance

PMs

PMs should disclose that they will advise in securities for the client, for example, in accordance with an IPS.

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[4] Paragraph 14.2(2)(b) changed as follows since the review: a general description of the products and services the registered firm offers to the client.

EMDs
EMDs should indicate that they sell third party or proprietary prospectus-exempt products. EMDs may refer clients to another entity's offering documents (typically prepared by an issuer) provided the disclosure is adequately fulfilling the dealer's disclosure obligations. EMDs should also indicate that products are not offered by prospectus, rather than just indicating that they sell "exempt products".

3. Describe the Types of Risks that a Client Should Consider

Paragraph 14.2(2)(c) requires registered firms to provide clients with a description of the types of risks a client should consider when making investment decisions[5].

32 % of registered firms sampled were deficient in this area.

We found the following deficiencies:

- Registered firms provided only a generic list of the risks, but did not describe the risk implications on the client's investment decisions.
- Registered firms verbally discussed the risks with the client (i.e., during the KYC and IPS development process), but did not provide anything to the client in writing or maintain evidence of the discussion.
- Where a registered firm undertook a particular investment strategy for a client, the firm did not discuss or document the potential risks of participating in that strategy.
- Descriptions of risk were vague and did not provide sufficient detail for clients.
- Some EMDs did not provide risk disclosure or refer clients to the risks discussed in the issuer's offering documents.

Guidance[6]
PMs
A PM should either provide an explanation of the risks associated with making investment decisions to the client (i.e., currency, interest rate, margin, leverage, liquidity, etc.) or refer to the risks discussed in the IPS. The risks described should be relevant to the PM's business environment, the investments offered, and the investment strategies recommended for the client.

EMDs
An EMD should either explain the specific risks of each product clearly in the relationship disclosure document or refer to the risk disclosure contained in the Offering Memorandum or other offering documents, provided that the EMD is satisfied that the disclosure is adequate. EMDs should ensure that the RDI provided to clients also includes a discussion of the risks of investing in the exempt market in general.

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[5] As of July 15, 2013, paragraph 14.2(2)(c) is amended as follows: a general description of the types of risks that a client should consider when making an investment decision.
[6] As of July 15, 2013, subsection 14.2(3) requires a registered firm to deliver the information in paragraph 14.2(2)(c) in writing.

4. Describe the Risks to a Client of Using Borrowed Money

Paragraph 14.2(2)(d) requires registered firms to provide a description of the risks of using borrowed money to finance a purchase of a security.

41% of registered firms sampled were deficient in this area.

We found the following deficiencies:

- Registered firms thought this requirement did not apply to them because they:
  - did not purchase investments on margin, recommend leverage strategies to clients, or provide service to or accept clients who borrow to invest
  - only dealt with accredited investors who are aware of the risks of investing using borrowed money
- Registered firms did not provide this disclosure and instead relied on disclosure provided by other entities (such as the issuer or the custodian).
- Registered firms noted they discussed the risks associated with leverage verbally with clients, but did not include this information in their written disclosure or maintain evidence of the discussion.

Guidance[7]

PMs and EMDs

PMs and EMDs must disclose the risks of using borrowed money to invest to all clients, regardless of whether or not the client uses leverage or the firm recommends the use of borrowed money to purchase investments. This disclosure is important, as the firm may not be aware that the client is making an investment with borrowed funds.

In circumstances where a firm recommends the use of borrowed money to finance any part of a purchase of a security, the following disclosure found in section 13.13 of Regulation 31-103 must be included, or disclosure that is substantially similar:

> *Using borrowed money to finance the purchase of securities involves greater risk than a purchase using cash resources only. If you borrow money to purchase securities, your responsibility to repay the loan and pay interest as required by its terms remains the same even if the value of the securities purchased declines.*

5. Describe the Conflicts of Interest

Under paragraph 14.2(2)(e), registered firms must provide a description of the conflicts of interest that the registered firm is required to disclose to a client under securities legislation. One such requirement is in section 13.4 of Regulation 31-103, which provides that a registered firm must take reasonable steps to identify and then respond to existing and potential material conflicts of interest between the firm and the client. Policy Statement 31-103 provides guidance on the conflict of interest requirements under section 13.4 and includes examples of situations where registered firms can be in a conflict of interest and how to manage the conflict.

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[7] As of July 15, 2013, subsection 14.2(3) requires a registered firm to deliver the information in paragraph 14.2(2)(d) in writing.

Registered firms should provide clients with information about relationships with related or connected issuers, competing interests of clients, compensation practices, fair allocation, soft dollar arrangements, etc. If a firm has determined it has no conflicts that they are required to disclose, the firm should maintain written documentation to evidence that they have considered the issue.

21% of registered firms sampled were deficient in this area.

We found the following deficiencies:

- Registered firms considered themselves to operate independently, and assumed that they did not have relationships that could potentially present a conflict of interest requiring disclosure, but this was not the case.
- Registered firms indicated that their policies and procedures manual or other internal policies described their conflicts, but acknowledged that they did not disclose these conflicts to clients.
- EMDs indicated that the issuer's offering documents adequately described the conflicts of interest, but this was not the case.
- Registered firms disclosed that they had conflicts, but they did not describe the conflicts or explain how they were addressing them.
- Registered firms provided an insufficient or unclear explanation about their conflicts and did not discuss the potential impact on clients.
- Registered firms disclosed the conflicts of interest at the individual dealing or advising level, but did not consider and disclose conflicts of interest at the firm level.

Guidance

PMs

PMs must identify and respond to conflicts of interest. Most PMs will have some conflicts that require disclosure, such as soft dollar arrangements, fair allocation and personal trading. PMs should disclose and describe all potential or existing material conflicts in detail. If PMs determine that they have no conflicts that they are required to disclose, they should maintain written documentation to evidence that they have considered this issue.

EMDs

EMDs must identify and respond to conflicts of interest. Most EMDs will have some conflicts that require disclosure, such as compensation received from issuers or an affiliation with an issuer. Similar to risk disclosure, an EMD may refer a client to an offering memorandum when disclosing conflicts, if the EMD is satisfied that the disclosure is adequately fulfilling the dealer's disclosure obligations. EMDs should consider whether the disclosure in the offering memorandum relates to the issuer's conflicts, which are not necessarily reflective of the conflicts of interest of the registered firm. In particular, EMDs must also consider the conflicts of interest that exist when selling securities of related or connected issuers. Where EMDs can address the conflict by disclosure, they should ensure that they adequately disclose the nature and extent of the conflict to clients. If EMDs determine that they have no conflicts that they are required to disclose, they should maintain written documentation to evidence that they have considered this issue.

6. Disclose all Costs to Clients

Under paragraph 14.2(2)(f), registered firms must provide disclosure of all costs to clients for the operation of an account[8]. Under paragraph 14.2(2)(g), they must provide a description of the costs a client will pay in making, holding and selling an investment[9]. These two requirements ensure that clients receive all relevant information to evaluate all of the costs associated with the products and services they receive from a registered firm.

16% of registered firms sampled were deficient in this area.

We found the following deficiencies:

- Registered firms only referred to costs and fees generally rather than providing specific and meaningful information.
- PMs disclosed details about the management fees they charge in their advisory agreement, but did not discuss that there may be third party costs associated with the operation of the account, such as custodial or brokerage fees.
- Registered firms disclosed information about costs and fees verbally at the time of account opening, but did not maintain evidence in writing that they had verbally provided the client with the disclosure.
- Registered firms indicated in their disclosure that they could change fees without notice to the client. However, under subsection 14.2(4), if there is a significant change to the information delivered to a client under subsection (1), the registered firm must take reasonable steps to notify the client of the change in a timely manner.
- Some EMDs did not disclose fees that they directly charged to the client. Instead, the only disclosure about fees associated with the investment was in the issuer's offering documents.
- Some EMDs did not clearly state the details of compensation or explain that the offering memorandum or subscription agreement may also disclose the amount of compensation.
- Some EMDs' disclosure did not clearly state that the client would be paying fees on a transactional basis, and that costs could differ depending on the investment purchased.

Guidance[10]

PMs

PMs should provide clients with a clear description, and calculation method where applicable, of any fees that the PM charges. We would also expect that if a firm facilitates a clients' entering into third party service arrangements for custody or brokerage, disclosure of the details of any costs associated with these services would be provided at the time the client account is opened. If the PM has negotiated fixed fees for clients (i.e., bundled fees, flat rate for custodial or brokerage charges), the PM should disclose this to clients.

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[8] As of July 15, 2013, paragraph 14.2(2)(f) is amended as follows: (f) disclosure of the operating charges the client might be required to pay related to the account.

[9] As of July 15, 2013, paragraph 14.2(2)(g) is amended as follows: (g) a general description of the types of transaction charges the client might be required to pay.

[10] As of July 15, 2013, subsection 14.2(3) requires a registered firm to deliver the information in paragraphs 14.2(2)(f) and (g) in writing.

EMDs

EMDs should clearly disclose all trading costs for a client. This includes direct compensation that the EMD or dealing representative receives, and any embedded compensation as disclosed in the offering memorandum. If EMD clients will incur custodial fees, EMDs should provide a description of these fees. If EMDs disclose information in separate documents, they should provide a list of these documents to clients and set out where they can find them. EMDs should disclose all transaction costs incurred by a client when buying or selling the investment, as well as any holding costs associated with the investment (for example, the cost of holding an exempt product in a registered account). EMDs should clearly state whether they charge a fee to operate an account (for example, if any fees are required to open, maintain, close or transfer an account).

7. Describe Compensation Paid for Different Types of Products

Paragraph 14.2(2)(h) requires that registered firms provide clients with a description of the compensation paid to the firm in relation to the different types of products that a client may purchase through the firm[11]. This requirement clarifies the compensation that a registered firm receives, particularly when a firm:

- receives varying levels of compensation for providing the same service or product, or
- provides a varied range of investment services and products to their clients.

6% of registered firms sampled were deficient in this area.

We found the following deficiencies:

- Some EMDs did not explain the compensation that they receive. For example, the issuer may pay an EMD to maintain a product on the firm's shelf, sales incentive bonuses, or to perform due diligence activities relating to their products.
- Some EMDs did not disclose and explain the commissions that they and the dealing representative receive. Rather, EMDs referred the client to the offering document, which in some cases contained insufficient information.

Guidance

EMDs and PMs

While this deficiency was found in 23% of the EMD samples, it is important for both EMDs and PMs to provide clear and meaningful disclosure about the compensation that they receive from any other parties. For example, EMDs should disclose any commission, sales bonuses, and trailer fees they receive from issuers. When providing such disclosure, EMDs may refer a client to an offering document, if the EMD is satisfied that the disclosure is clear and fulsome and adequately fulfills the dealer's disclosure obligations. If the disclosure in the offering document is vague (i.e., "the fee on this purchase is up to 10%"), the EMD should provide more specific disclosure information.

Registrants should also refer to the guidance on the requirements in paragraphs 14.2(2)(f), (g)

[11] As of July 15, 2013, this paragraph is amended as follows: (h) a general description of any compensation paid to the registered firm by any other party in relation to the different types of products that a client may purchase through the registered firm.

and (h) that is provided under subsection 14.2 of Policy Statement 31-103 as amended as of July 15, 2013.

8. Describe the Content and Frequency of Reporting

Under paragraph 14.2(2)(i), registered firms must provide a description of the content and frequency of reporting for each account or portfolio of a client. Subsections 14.14(1) and (3) of Regulation 31-103 require registered dealers and advisers to deliver account statements to clients at least once every three months[12]. Although there is no prescribed form for these statements, they must contain the information set out in subsections 14.14(4) and 14.14(5) of Regulation 31-103.

33% of registered firms sampled were deficient in this area.

We found the following deficiencies:

- The registered firm's RDI discussed the frequency of the reporting, but not the content.
- The description of the content of the quarterly reporting was insufficient and did not encompass everything required under subsections 14.14(4) and 14.14(5).
- Registered firms stated in the disclosure information that the custodian would provide the reporting, without explaining the frequency or the content.
- EMDs thought that quarterly account reporting was not required on the basis that they did not have client "accounts" but rather offered a transactional service only.

Guidance

PMs and EMDs

PMs and EMDs RDI must include a description of the content of the statement and the correct reporting frequency in accordance with section 14.14. Under subsections 14.14(1) and (3), a registered firm must deliver an account statement to a client at least once every three months, or monthly, if the client requests it. Registered firms can increase the frequency of account statement delivery to more than every three months.

CSA Staff Notice 31-324 *Exempt Market Dealers and Account Statement Requirements in Regulation 31-103 respecting Registration Requirements and Exemptions* sets out expectations for EMDs' compliance with the account statement delivery requirements. The CRM2 Amendments introduce new requirements for account statements and additional statements that will be applicable to PMs and EMDs, effective July 15, 2015. Until then, EMDs should continue to refer to Staff Notice 31-324 which, among other guidance, states that

> *We will expect an EMD to deliver quarterly account statements containing:*
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> - *transaction information [i.e., information required under subsection 14.14(4)] covering each transaction it made for a client during the quarter, and*

[12] As of July 15, 2013, subsection (3) is amended as follows: A registered adviser must deliver a statement to a client at least once every 3 months, except that if the client has requested to receive statements on a monthly basis, the adviser must deliver a statement to the client every month. On July 15, 2015, section 14.14 is further amended and new sections 14.14.1, 14.14.2, 14.15 and 14.16 are added. For further information, see CRM2 Notice.

- *account balance information [i.e., information required under subsection 14.14(5)] for all cash and securities of the client that it holds or controls*

If an EMD does not hold or control any cash or securities of a client, and it makes no transactions for the client during a quarter, we will not expect the EMD to send an account statement for that quarter to the client.

9. Disclose that Independent Dispute Resolution or Mediation is Available

Under paragraph 14.2(2)(j), if section 13.16 of Regulation 31-103 (dispute resolution service) applies, registered firms must disclose that independent dispute resolution or mediation services are available at the firm's expense to resolve any dispute that might arise between the client and the firm about any trading or advising activity of the firm or one of its representatives[13].

Section 13.16 requires that registered firms make available an independent dispute resolution or mediation service to clients, at the firms' expense. At the time of the review, section 13.16 did not apply to firms which were registered when Regulation 31-103 came into force.[14] As the requirement did not apply to most of the firms we sampled, we do not have information to report on this aspect of relationship disclosure requirements.

10. State the Obligation to Assess Whether a Purchase or Sale of a Security is Suitable for a Client

Under paragraph 14.2(2)(k), registered firms are required to deliver a statement to clients that the firm has an obligation to assess whether a purchase or sale of a security is suitable for a client prior to executing the transaction or at any other time. This requirement is straightforward, and directly relates to the obligation of a registered firm to meet their suitability obligations under sections 13.2 and 13.3 of Regulation 31-103.

35% of registered firms sampled were deficient in this area.

We found the following deficiencies:

- The registered firm's disclosure information did not include the specific statement required under paragraph 14.2(2)(k). Some firms thought it was sufficient to:
    - Have policies and procedures in place for assessing suitability
    - Manage client accounts consistent with the KYC information and investment objectives for each client but not provide the statement
    - Include language other than what is required in paragraph14.2(2)(k) or no statement at all

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[13] In Québec, a registered firm is deemed to comply with section 13.16 if it complies with sections 168.1.1 to 168.1.3 of the *Securities Act* (Québec). These provisions set out a complaint handling regime whereby the Autorité des marchés financiers (the AMF) may act as a mediator (the Québec regime).

[14] On July 5, 2012, the CSA published parallel orders further extending the temporary relief from Section 13.16 until the earlier of: (i) the coming into force of amendments to section 13.16, and (ii) September 28, 2014. The temporary relief does not apply in Quebec. On November 15, 2012, the CSA published proposed amendments to Regulation 31-103 about the dispute resolution service. The comment period ended February 15, 2013.

Guidance
PMs and EMDs
PMs and EMDs must include the specific statement required in paragraph 14.2(2)(k) in their RDI[15].

11. Disclose the Information that must be collected About Clients
Under paragraph 14.2(2)(l), a registered firm is required to disclose the information that they must collect about their clients as required by section 13.2 of Regulation 31-103 (know your client). Section 13.2 sets out the information a registrant must obtain and document to establish the identity of a client, determine if the client is an insider, and assess the suitability of proposed investments.

39% of registered firms sampled were deficient in this area.

We found the following deficiencies:
- Registered firms routinely collected adequate KYC information and provided a copy of the completed KYC form to clients, but did not explain in their RDI the terms in the KYC form or state that the firm uses this information to assess suitability.
- Registered firms indicated that they only dealt with accredited investors, and therefore this requirement was not applicable.
- Registered firms did not set out the KYC information that it is required to collect under section 13.2.

Guidance
PMs and EMDs
Registered firms should provide clients with a statement that lists and describes the information that they must collect, and an explanation of how the firm uses this information to assess the suitability of investments for clients.

Registrants should also refer to the guidance on the requirements in paragraphs 14.2(2)(l) that is provided under subsection 14.2 of Policy Statement 31-103 as amended as of July 15, 2013.

New Requirements

We draw your attention to the new RDI requirements in paragraphs 14.2(2)(m) and (n) that come into force on July 15, 2014. Specifically, paragraph 14.2(2)(m) requires firms to provide each client with a general explanation of benchmarks and whether the firm offers any options for benchmark reporting to clients. Guidance on the new requirements is provided in the amended Policy Statement 31-103. See the CRM2 Notice for further information.

[15] As of July 15, 2013, subsection 14.2(3) requires a registered firm to deliver the information in paragraph 14.2(2)(l) in writing.

Next Steps

We will review the relationship disclosure practices of registered firms during our ongoing compliance reviews and will apply the guidance in this notice when assessing whether a firm is complying with relationship disclosure requirements, and the guidance in the amended Policy Statement 31-103.

Please refer your questions to any of the following people:

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