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POLICY STATEMENT TO REGULATION 31-103 RESPECTING REGISTRATION REQUIREMENTS, EXEMPTIONS AND ONGOING REGISTRANT OBLIGATIONS

PART 1 DEFINITIONS AND FUNDAMENTAL CONCEPTS

1.1. Introduction

Purpose of this Policy Statement

This Policy Statement sets out how the Canadian Securities Administrators (the CSA or we) interpret or apply the provisions of *Regulation 31-103 respecting Registration Requirements, Exemptions and Ongoing Registrant Obligations* (chapter V-1.1, r. 10) (Regulation 31-103) and related securities legislation.

Numbering system

Except for Part 1, the numbering of Parts, Divisions and sections in this Policy Statement corresponds to the numbering in Regulation 31-103. Any general guidance for a Part or a Division appears immediately after the Part or Division name. Any specific guidance on sections in Regulation 31-103 follows any general guidance. If there is no guidance for a Part, Division or section, the numbering in this Policy Statement will skip to the next provision that does have guidance.

All references in this Policy Statement to sections, Parts and Divisions are to Regulation 31-103, unless otherwise noted.

Additional requirements applicable to registrants

For additional requirements that may apply to them, registrants should refer to:

- *Regulation 31-102 respecting National Registration Database* (chapter V-1.1, r. 9) (Regulation 31-102) and the Policy Statement to Regulation 31-102 respecting National Registration Database (Decision 2009-PDG-0132, 2009-09-04) (Policy Statement to Regulation 31-102)

- *Regulation 33-109 respecting Registration Information* (chapter V-1.1, r. 12) (Regulation 33-109) and the Policy Statement to Regulation 33-109 respecting Registration Information (Decision 2014-PDG-0142, 2014-11-14) (Policy Statement to Regulation 33-109)

- *Policy Statement 11-204 respecting Process for Registration in Multiple Jurisdictions* (Decision 2009-PDG-0115, 2009-0904) (Policy Statement 11-204), and

- securities and derivatives legislation in their jurisdiction

Registrants that are members an SRO must also comply with their SRO's requirements.

Disclosure and notices

Delivering disclosure and notices to the principal regulator

Under section 1.3, registrants must deliver all disclosure and notices required under Regulation 31-103 to the registrant's principal regulator. This does not apply to notices under sections 8.18 and 8.26. Registrants must deliver these notices to the regulator in each jurisdiction where they are registered or relying on an exemption from registration.

Electronic delivery of documents

These documents may be delivered electronically. Registrants should refer to *Policy Statement 11-201 respecting Electronic Delivery of Documents* (Decision 2011-PDG-0183, 2011-11-17) (Policy Statement 11-201).

See Appendix A for contact information for each regulator.

Clear and meaningful disclosure to clients

We expect registrants to present disclosure information to clients in a clear and meaningful manner in order to ensure clients understand the information presented. Registrants should ensure that investors can readily understand the information. These requirements are consistent with the obligation to deal fairly, honestly and in good faith with clients.

1.2. Definitions

Unless defined in Regulation 31-103, terms used in Regulation 31-103 and in this Policy Statement have the meaning given to them in the securities legislation of each jurisdiction or in *Regulation 14-101 respecting Definitions* (chapter V-1.1, r. 3). See Appendix B for a list of some terms that are not defined in Regulation 31-103 or this Policy Statement but are defined in other securities legislation.

In this Policy Statement "regulator" means the regulator or securities regulatory authority in a jurisdiction.

Permitted client

The following discussion provides guidance on the term "permitted client", which is defined in section 1.1.

"Permitted client" is used in the following sections:

- 8.18

- 8.22.1
- 8.26
- 13.2
- 13.3
- 13.2.1
- 13.13
- 14.2
- 14.2.1
- 14.4
- 14.5.2
- 14.14.1
- 14.14.2
- 14.17
- 14.18

Exemptions from registration when dealing with permitted clients

Sections 8.18 and 8.26 exempt international dealers and international advisers from the registration requirement if they deal with certain permitted clients and meet certain other conditions.

Section 8.22.1 exempts certain financial institutions from the dealer registration requirement when dealing in a short-term debt instrument with permitted clients.

Exemptions from other requirements when dealing with permitted clients

Under section 13.3.1, permitted clients may waive their right to have a registrant determine that a trade is suitable. In order to rely on this exemption, the registrant must determine that a client is a permitted client at the time the client waives their right to suitability.

Under sections 13.13 and 14.4, registrants do not have to provide certain disclosures to permitted clients. In order to rely on these exemptions, registrants must determine that a client is a permitted client at the time the client opens an account.

Under sections 14.2, 14.2.1, 14.14.1, 14.14.2, 14.17 and 14.18, registrants do not have to provide certain disclosures or reports to a permitted client that is not an individual.

Under paragraph 14.5.2(7)(d), registered firms are not required to ensure that cash or securities of permitted clients, that are not individuals or investment funds, are held with a qualified custodian if the permitted client has acknowledged in writing that the permitted client is aware that this qualified custodian requirement will not apply to the firm. In order to rely on this exemption, we expect registered firms to determine that the client is a permitted client that is not an individual or investment fund at the time the client acknowledges that its right to a qualified custodian will not apply.

Determining assets

The definition of permitted client includes monetary thresholds based on the value of the client's assets. The monetary thresholds in paragraphs (o) and (q) of the definition are intended to create "bright-line" standards. Investors who do not satisfy these thresholds do not qualify as permitted clients under the applicable paragraph.

Paragraph (o) of the definition

Paragraph (o) refers to an individual who beneficially owns financial assets with an aggregate realizable value that exceeds $5 million, before taxes but net of any related liabilities.

In general, determining whether financial assets are beneficially owned by an individual should be straightforward. However, this determination may be more difficult if financial assets are held in a trust or in other types of investment vehicles for the benefit of an individual.

Factors indicating beneficial ownership of financial assets include:

- possession of evidence of ownership of the financial asset
- entitlement to receive any income generated by the financial asset
- risk of loss of the value of the financial asset, and
- the ability to dispose of the financial asset or otherwise deal with it as the individual sees fit

For example, securities held in a self-directed RRSP for the sole benefit of an individual are beneficially owned by that individual. Securities held in a group RRSP are not beneficially owned if the individual cannot acquire and deal with the securities directly.

"Financial assets" is defined in section 1.1 of *Regulation 45-106 respecting Prospectus Exemptions* (chapter V-1.1, r. 21) (Regulation 45-106).

Realizable value is typically the amount that would be received by selling an asset.

Paragraph (q) of the definition

Paragraph (q) refers to a person that has net assets of at least $25 million, as shown on its last financial statements. “Net assets” under this paragraph is total assets minus total liabilities.

Definitions related to sections 13.2.01 and 13.19

Appendix G provides guidance on the terms “financial exploitation”, “temporary hold”, “trusted contact person” and “vulnerable client”.

1.3. Fundamental concepts

This section describes the fundamental concepts that form the basis of the registration regime:

- requirement to register
- business trigger for trading and advising, and
- fitness for registration

A registered firm is responsible for the conduct of the individuals whose registration it sponsors. A registered firm

- must undertake due diligence before sponsoring an individual to be registered to act on its behalf (see further guidance in Part 4 of the Policy Statement to Regulation 33-109)
- has an ongoing obligation to monitor, supervise and train its registered individuals in an effective manner (see further guidance in section 11.1 of this Policy Statement)

Failure of a registered firm to take reasonable steps to discharge these responsibilities may be relevant to the firm’s own continued fitness for registration.

Requirement to register

The requirement to register is found in securities legislation. Firms must register if they are:

- in the business of trading
- in the business of advising

- holding themselves out as being in the business of trading or advising
- acting as an underwriter, or
- acting as an investment fund manager

Individuals must register if they trade, underwrite or advise on behalf of a registered dealer or adviser, or act as the ultimate designated person (UDP) or chief compliance officer (CCO) of a registered firm. Except for the UDP and the CCO, individuals who act on behalf of a registered investment fund manager do not have to register.

However, all permitted individuals of any registrant must file Form 33-109F4 *Registration of Individuals and Review of Permitted Individuals* (Form 33-109F4).

There is no renewal requirement for registration, but fees must be paid every year to maintain registration.

Multiple categories

Registration in more than one category may be necessary. For example, an adviser that also manages an investment fund may have to register as a portfolio manager and an investment fund manager. An adviser that manages a portfolio and distributes units of an investment fund may have to register as a portfolio manager and as a dealer.

Registration exemptions

Regulation 31-103 provides exemptions from the registration requirement. There may be additional exemptions in securities legislation. Some exemptions do not need to be applied for if the conditions of the exemption are met. In other cases, on receipt of an application, the regulator has discretion to grant exemptions for specified dealers, advisers or investment fund managers, or activities carried out by them if registration is required but specific circumstances indicate that it is not otherwise necessary for investor protection or market integrity.

Business trigger for trading and advising

We refer to trading or advising in securities for a business purpose as the "business trigger" for registration.

We look at the type of activity and whether it is carried out for a business purpose to determine if an individual or firm must register. We consider the factors set out below, among others, to determine if the activity is for a business purpose. For the most part, these factors are from case law and regulatory decisions that have interpreted the business purpose test for securities matters.

Factors in determining business purpose

This section describes factors that we consider relevant in determining whether an individual or firm is trading or advising in securities for a business purpose and, therefore, subject to the dealer or adviser registration requirement.

This is not a complete list. We do not automatically assume that any one of these factors on its own will determine whether an individual or firm is in the business of trading or advising in securities.

(a) Engaging in activities similar to a registrant

We usually consider an individual or firm engaging in activities similar to those of a registrant to be trading or advising for a business purpose. Examples include promoting securities or stating in any way that the individual or firm will buy or sell securities. If an individual or firm sets up a business to carry out any of these activities, we may consider them to be trading or advising for a business purpose.

(b) Intermediating trades or acting as a market maker

In general, we consider intermediating a trade between a seller and a buyer of securities to be trading for a business purpose. This typically takes the form of the business commonly referred to as a broker. Making a market in securities is also generally considered to be trading for a business purpose.

(c) Directly or indirectly carrying on the activity with repetition, regularity or continuity

Frequent or regular transactions are a common indicator that an individual or firm may be engaged in trading or advising for a business purpose. The activity does not have to be their sole or even primary endeavour for them to be in the business.

We consider regularly trading or advising in any way that produces, or is intended to produce, profits to be for a business purpose. We also consider any other sources of income and how much time an individual or firm spends on all activities associated with the trading or advising.

(d) Being, or expecting to be, remunerated or compensated

Receiving, or expecting to receive, any form of compensation for carrying on the activity, including whether the compensation is transaction or value based, indicates a business purpose. It does not matter if the individual or firm actually receives compensation or in what form. Having the capacity or the ability to carry on the activity to produce profit is also a relevant factor.

(e) Directly or indirectly soliciting

Contacting anyone to solicit securities transactions or to offer advice may reflect a business purpose. Solicitation includes contacting someone by any means, including advertising that proposes buying or selling securities or participating in a securities transaction, or that offers services or advice for these purposes.

Business trigger examples

This section explains how the business trigger might apply to some common situations.

(a) Securities issuers

A securities issuer is an entity that issues or trades in its own securities. In general, securities issuers with an active non-securities business do not have to register as a dealer if they:

- do not hold themselves out as being in the business of trading in securities
- trade in securities infrequently
- are not, or do not expect to be, compensated for trading in securities
- do not act as intermediaries, and
- do not produce, or intend to produce, a profit from trading in securities

During the start-up stage, securities issuers may not yet be actively carrying on their intended business. We consider a start-up securities issuer to have an "active non-securities business" if the entity is raising capital to start a non-securities business. Although the entity does not need to be producing a product or delivering a service, we would expect it to have a bona fide business plan to do so, containing milestones and the time anticipated to reach those milestones. For example, technology companies may raise money with only a business plan for many years before they start producing a product or delivering a service. Similarly, junior exploration companies may raise money with only a business plan long before they find or extract any resources.

However, securities issuers may have to register as dealers if they are in the business of trading. Conduct that would indicate that security issuers are in the business includes frequently trading in securities. While frequent trading is a common indicator of being in the business of trading, we recognize that trading may be more frequent during the start-up stage, as an issuer needs to raise capital to launch and advance the business. If the trading is primarily for the purpose of advancing the issuer's business plan, then the frequency of the activities alone should not result in the issuer being in the business of trading in securities. If the capital raising and use of that capital are not advancing the business, the issuer may need to register as a dealer.

Securities issuers may also have to register as a dealer if they

- employ or contract individuals to perform activities on their behalf that are similar to those performed by a registrant (other than underwriting in the normal course of a distribution or trading for their own account)

- actively solicit investors, subject to the discussion below, or

- act as an intermediary by investing client money in securities

For example, an investment fund manager that carries on the activities described above may have to register as a dealer.

Many issuers actively solicit through officers, directors or other employees. If these individuals' activities are incidental to their primary roles with an issuer, they would likely not be in the business of trading. Factors that would suggest that the issuer and these individuals are in the business of trading are:

- the principal purpose of the individual's employment is raising capital through distributions of the issuer's securities;

- the individuals spend the majority of their time raising capital in this manner;

- the individuals' compensation or remuneration is based solely or primarily on the amount of capital they raise for the issuer.

Securities issuers that are distributing securities are subject to the prospectus requirements unless an exemption is available. Regulators have the discretionary authority to require an underwriter for a prospectus distribution.

(b) Venture capital and private equity

This guidance does not apply to labour sponsored or venture capital funds as defined in *Regulation 81-106 respecting Investment Fund Continuous Disclosure* (chapter V-1.1, r. 42) (Regulation 81-106).

Venture capital and private equity investing are distinguished from other forms of investing by the role played by venture capital and private equity management companies (collectively, VCs). This type of investing includes a range of activities that may require registration.

VCs typically raise money under one of the prospectus exemptions in Regulation 45-106, including for trades to "accredited investors". The investors typically agree that their money will remain invested for a period of time. The VC uses this money to invest in securities of companies that are usually not publicly traded. The VC usually becomes actively involved in the management of the company, often over several years.

Examples of active management in a company include the VC having:

- representation on the board of directors
- direct involvement in the appointment of managers
- a say in material management decisions

The VC looks to realize on the investment either through a public offering of the company's securities, or a sale of the business. At this point, the investors' money can be returned to them, along with any profit.

Investors rely on the VC's expertise in selecting and managing the companies it invests in. In return, the VC receives a management fee or "carried interest" in the profits generated from these investments. They do not receive compensation for raising capital or trading in securities.

Applying the business trigger factors to the VC activities as described above, there would be no requirement for the VC to register as:

- a portfolio manager, if the advice provided in connection with the purchase and sale of companies is incidental to the VC's active management of these companies, or
- a dealer, if both the raising of money from investors and the investing of that money by the VC (in securities of companies that are usually not publicly traded) are occasional and uncompensated activities

If the VC is actively involved in the management of the companies it invests in, the investment portfolio would generally not be considered an investment fund. As a result, the VC would not need to register as an investment fund manager.

The business trigger factors and investment fund manager analysis may apply differently if the VC engages in activities other than those described above.

(c) One-time activities

In general, we do not require registration for one-time trading or advising activities. This includes trading or advising that:

- is carried out by an individual or firm acting as a trustee, executor, administrator, personal or other legal representative, or
- relates to the sale of a business

(d) Incidental activities

If trading or advising activity is incidental to a firm's primary business, we may not consider it to be for a business purpose.

For example, merger and acquisition specialists that advise the parties to a transaction between companies are not normally required to register as dealers or advisers in connection with that activity, even though the transaction may result in trades in securities and they will be compensated for the advice. If the transaction results in trades in the securities of the company to an acquirer, this is considered incidental to the acquisition transaction. However, if the merger and acquisition specialists also engage in capital raising from prospective investors (including private placements), they will need to consider whether such activity would be in the business of trading and require registration.

Another example is professionals, such as lawyers, accountants, engineers, geologists and teachers, who may provide advice on securities in the normal course of their professional activities. We do not consider them to be advising on securities for a business purpose. For the most part, any advice on securities will be incidental to their professional activities. This is because they:

- do not regularly advise on securities
- are not compensated separately for advising on securities
- do not solicit clients on the basis of their securities advice, and
- do not hold themselves out as being in the business of advising on securities

Registration trigger for investment fund managers

Investment fund managers are subject to a registration trigger. This means that if a firm carries on the activities of an investment fund manager, it must register. However, investment fund managers are not subject to the business trigger.

Fitness for registration

The regulator will only register an applicant if they appear to be fit for registration. Following registration, individuals and firms must maintain their fitness in order to remain registered. If the regulator determines that a registrant has become unfit for registration, the regulator may suspend or revoke the registration. See Part 6 of this Policy Statement for guidance on suspension and revocation of individual registration. See Part 10 of this Policy Statement for guidance on suspension and revocation of firm registration.

Terms and conditions

The regulator may impose terms and conditions on a registration at the time of registration or at any time after registration. Terms and conditions imposed at the time of registration are generally permanent, for example, in the case of a restricted dealer who is limited to specific activities. Terms and conditions imposed after registration are generally temporary. For example, if a registrant does not maintain the required capital, it may have to file monthly financial statements and capital calculations until the regulator's concerns are addressed.

Opportunity to be heard

Applicants and registrants have an opportunity to be heard by the regulator before their application for registration is denied. They also have an opportunity to be heard before the regulator imposes terms and conditions on their registration if they disagree with the terms and conditions.

Assessing fitness for registration – firms

We assess whether a firm is or remains fit for registration through the information it is required to provide on registration application forms and as a registrant, and through compliance reviews. Based on this information, we consider whether the firm is able to carry out its obligations under securities legislation. For example, registered firms must be financially viable. A firm that is insolvent or has a history of bankruptcy may not be fit for registration.

In addition, when determining whether a firm whose head office is outside Canada is, and remains, fit for registration, we will consider whether the firm maintains registration or regulatory organization membership in the foreign jurisdiction that is appropriate for the securities business it carries out there.

Assessing fitness for registration – individuals

We use 3 fundamental criteria to assess whether an individual is or remains fit for registration:

- proficiency
- integrity, and
- solvency

(a) Proficiency

Individual applicants must meet the initial proficiency requirements by demonstrating that they have the applicable education, training and experience prescribed by securities legislation as well as knowledge of securities legislation.

(b) Integrity

Registered individuals must conduct themselves with integrity and have an honest character. The regulator will assess the integrity of individuals through the information they are required to provide on registration application forms and as registrants, and through compliance reviews. For example, applicants are required to disclose information about conflicts of interest, such as other employment or partnerships, service as a member of a board of directors, or relationships with affiliates, and about any regulatory or legal actions against them.

(c) Solvency

The regulator will assess the overall financial condition of an individual applicant or registrant. An individual that is insolvent or has a history of bankruptcy may not be fit for registration. Depending on the circumstances, the regulator may consider the individual's contingent liabilities. The regulator may take into account an individual's bankruptcy or insolvency when assessing their continuing fitness for registration.

PART 2 CATEGORIES OF REGISTRATION FOR INDIVIDUALS

2.1. Individual categories

Multiple individual categories

Individuals who carry on more than one activity requiring registration on behalf of a registered firm must:

- register in all applicable categories, and
- meet the proficiency requirements of each category

For example, an advising representative of a portfolio manager who is also the firm's CCO must register in the categories of advising representative and CCO. They must meet the proficiency requirements of both of these categories.

Individual registered in a firm category

An individual can be registered in both a firm and individual category. For example, a sole proprietor who is registered in the firm category of portfolio manager must also be registered in the individual category of advising representative.

2.2. Client mobility exemption – individuals

Conditions of the exemption

The mobility exemption in section 2.2 allows registered individuals to continue dealing with and advising clients who move to another jurisdiction, without registering in that other jurisdiction. Section 8.30 contains a similar exemption for registered firms.

The exemption becomes available when the client (not the registrant) moves to another jurisdiction. An individual may deal with up to 5 "eligible" clients in each other jurisdiction. Each of the client, their spouse and any children are an eligible client.

An individual may only rely on the exemption if:

- they and their sponsoring firm are registered in their principal jurisdiction

- they and their sponsoring firm only act as a dealer, underwriter or adviser in the other jurisdiction as permitted under their registration in their principal jurisdiction

- they comply with Part 13

- they act fairly, honestly and in good faith in their dealings with the eligible client, and

- their sponsoring firm has disclosed to the eligible client that the individual and if applicable, their sponsoring firm, are exempt from registration in the other jurisdiction and are not subject to the requirements of securities legislation in that jurisdiction

As soon as possible after an individual first relies on this exemption, their sponsoring firm must complete and file Form 31-103F3 *Use of mobility exemption* (Form 31-103F3) with the other jurisdiction.

Limits on the number of clients

Sections 2.2 and 8.30 are independent of each other: individuals may rely on the exemption from registration in section 2.2 even though their sponsoring firm is registered in the local jurisdiction (and is not relying on the exemption from registration in section 8.30). The limits in sections 2.2 and 8.30 are per jurisdiction.

For example a firm using the exemption in section 8.30 could have 10 clients in each of several local jurisdictions where it is not registered. An individual may also use the exemption in section 2.2 to have 5 clients in each of several jurisdictions where the individual is not registered.

The individual limits are per individual. For example several individuals working for the same firm could each have 5 clients in the same local jurisdiction and each individual could still rely on the exemption in section 2.2. However, the firm may not exceed its 10 client limit if it wants to rely on the exemption in section 8.30. If the firm exceeds the 10 client limit, the firm must be registered in the local jurisdiction.

PART 3 REGISTRATION REQUIREMENTS – INDIVIDUALS

Division 1 General proficiency requirements

Application of proficiency requirements

Part 3 sets out the initial and ongoing proficiency requirements for

- dealing representatives and chief compliance officers of mutual fund dealers, scholarship plan dealers and exempt-market dealers respectively

- advising representatives, associate advising representatives and chief compliance officers of portfolio managers

- chief compliance officers of investment fund managers

The regulator is required to determine the individual's fitness for registration and may exercise discretion in doing so.

Section 3.3 does not provide proficiency requirements for dealing representatives of investment dealers since the IIROC Rules provide those requirements for the individuals who are approved persons of IIROC member firms.

Exam based requirements

Individuals must pass exams – not courses – to meet the education requirements in Part 3. For example, an individual must pass the Canadian Securities Course Exam, but does not have to complete the Canadian Securities Course. Individuals are responsible for completing the necessary preparation to pass an exam and for proficiency in all areas covered by the exam.

3.3. Time limits on examination requirements

Under section 3.3, there is a time limit on the validity of exams prescribed in Part 3. Individuals must pass an exam within 36 months before they apply for registration. However, this time limit does not apply if the individual:

- was registered in an active capacity (i.e., not suspended), in the same category in a jurisdiction of Canada at any time during the 36-month period before the date of their application; or

- has gained relevant securities industry experience for a total of 12 months during the 36-month period before the date of their application: these months do not have to be consecutive, or with the same firm or organization

These time limits do not apply to the CFA Charter or the CIM designation, since we do not expect the holders of these designations to have to retake the courses forming part of the requirements applicable to these designations. However, if the individual no longer has the right to use the CFA Charter or the CIM designation, by reason of revocation of the designation or otherwise, we may consider the reasons for such a revocation to be relevant in determining an individual’s fitness for registration. Registered individuals are required to notify the regulator of any change in the status of their CFA Charter or the CIM designation within 10 days of the change, by submitting Form 33-109F5 *Change of Registration Information* in accordance with Regulation 31-102.

When assessing an individual’s fitness for registration, the regulator may consider

- the date on which the relevant examination was passed, and

- the length of time between any suspension and reinstatement of registration during the 36-month period

See Part 6 of this Policy Statement for guidance on the meaning of “suspension” and “reinstatement”.

Relevant securities industry experience

The securities industry experience under paragraph 3.3(2)(b) should be relevant to the category applied for. It may include experience acquired:

- during employment at a registered dealer, a registered adviser or an investment fund manager

- in related investment fields, such as investment banking, securities trading on behalf of a financial institution, securities research, portfolio management, investment advisory services or supervision of those activities

- in legal, accounting or consulting practices related to the securities industry

- in other professional service fields that relate to the securities industry, or

- in a securities-related business in a foreign jurisdiction

In limited circumstances, relevant securities industry experience may include experience obtained during employment at a firm that has relied on a registration exemption. For example, experience obtained at a registered or licensed mortgage broker, mortgage brokerage, mortgage agency or mortgage dealer under applicable legislation may be considered relevant if the experience can be demonstrated to be relevant to the category applied for. In these circumstances, the regulator may also impose terms and conditions on the individual or the registered firm sponsoring the individual in order to limit their specific activities.

Division 2 Education and experience requirements

See Appendix C for a chart that sets out the proficiency requirements for each individual category of registration.

Granting exemptions

The regulator may grant an exemption from any of the education and experience requirements in Division 2 if it is satisfied that an individual has qualifications or relevant experience that is equivalent to, or more appropriate in the circumstances than, the prescribed requirements.

Proficiency for representatives of restricted dealers and restricted portfolio managers

The regulator will decide on a case-by-case basis what education and experience are required for registration as:

- a dealing representative or CCO of a restricted dealer, and
- an advising representative or CCO of a restricted portfolio manager

The regulator will determine these requirements when it assesses the individual's fitness for registration.

3.4. Proficiency – initial and ongoing

Proficiency principle

Under section 3.4, registered individuals must not perform an activity that requires registration unless they have the education, training and experience that a reasonable person would consider necessary to perform the activity competently the knowledge and ability to design and implement an effective compliance system.

Registered individuals should update their knowledge and training to keep pace with new securities, services and developments in the industry that are relevant to their business. Firms are required to provide training on compliance with securities legislation to their registered individuals.

Responsibility of the firm

The responsibility of registered firms to oversee the compliance of registered individuals acting on their behalf extends to ensuring that they are proficient at all times. A registered firm must not permit an individual it sponsors to perform an activity if the proficiency requirements are not met.

3.11. Portfolio manager – advising representative

3.12. Portfolio manager – associate advising representative

The 12 months of relevant investment management experience referred to in section 3.11 and 24 months of relevant investment management experience referred to in section 3.12 do not have to be consecutive, or with the same firm or organization.

For individuals with a CFA charter, the regulator will decide on a case-by-case basis whether the experience they gained to earn the charter qualifies as relevant investment management experience.

Relevant investment management experience

The relevant investment management experience requirement is in addition to the specific course or designation requirements for each category of registration. We will assess whether an individual has acquired relevant investment management experience on a case-by-case basis. This section describes factors we may consider in assessing certain types of experience.

Relevant investment management experience under sections 3.11 and 3.12 may vary according to the level of specialization of the individual. It may include:

- securities research and analysis experience, demonstrating an ability in, and understanding of, portfolio analysis or portfolio security selection, or

- management of investment portfolios on a discretionary basis, including investment decision making, rebalancing and evaluating performance

Advising representatives

An advising representative may have discretionary authority over investments of others. Accordingly, this category of registration involves the most onerous proficiency requirements. We expect an individual who seeks registration as an advising representative to demonstrate a high quality of experience that is clearly relevant to discretionary portfolio management. This section sets out specific examples of experience that may satisfy the relevant investment management experience requirement for advising representatives.

(a) Discretionary portfolio management

We may consider experience performing discretionary portfolio management in a professional capacity to be sufficient to meet the relevant investment management experience requirement for registration as an advising representative. Such experience may include working at:

- an adviser registered or operating under an exemption from registration in a foreign jurisdiction

- an insurance company
- a pension fund
- a government, corporate, bank or trust company treasury
- an IIROC member firm

(b) Assistant or associate portfolio management

We may consider experience supporting registered portfolio managers or other professional discretionary asset managers to be sufficient to meet the relevant investment management experience requirement for registration as an advising representative. This may include:

- working with portfolio managers to formulate, draft and implement written investment policy statements for clients, and
- researching and analysing individual securities for potential inclusion in investment portfolios

(c) Research analyst with an IIROC member firm or registered adviser

We may consider experience performing research and analysis of individual securities with recommendations for the purpose of determining their suitability for inclusion in client investment portfolios to be sufficient to meet the relevant investment management experience requirement for registration as an advising representative.

Associate advising representatives

This category may be appropriate for individuals who meet the minimum education and experience requirements in section 3.12 but do not meet the more onerous requirements for registration as an advising representative under section 3.11. In evaluating the experience required to obtain registration as an associate advising representative, we take into account that the advice provided by an associate advising representative must be approved by an advising representative in accordance with section 4.2. Experience gained as an associate advising representative does not automatically qualify an individual to be registered as an advising representative.

We will assess on a case-by-case basis whether such experience meets the more stringent quality of experience required for registration as an advising representative. This section sets out specific examples of experience that may satisfy the relevant investment management experience requirement for associate advising representatives.

(a) Client relationship management

We may consider client relationship management experience with a registered portfolio manager firm to be sufficient to meet the relevant investment management experience requirement for registration as an associate advising representative where the applicant has assisted portfolio managers in tailoring strategies for specific clients. This may include experience assisting the portfolio managers in assessing suitability, creating investment policy statements, determining asset allocation, monitoring client portfolios and performing research and analysis on the economy or asset classes generally.

We recognize that many individuals who perform client relationship management services may not provide specific advice and therefore may not trigger the registration requirement. For example, some client services representatives conduct activities such as marketing the services of the firm by providing general information about the registrant firm and its services that do not include a strategy tailored to any specific client. While some client service representatives may accompany advising representatives or associate advising representatives to meetings with clients and provide assistance with marketing and client development activities, without registration they may not themselves develop an investment policy statement for the client, provide specific information such as recommending a particular model portfolio for the client or explain the implications of discretionary portfolio decisions that were made by the client's advising representative.

(b) Corporate finance

We may consider corporate finance experience involving valuing and analysing securities for initial public offerings, debt and equity financings, takeover bids and mergers to be sufficient to meet the relevant investment management experience requirement for registration as an associate advising representative where this experience demonstrates an ability in, and understanding of, portfolio analysis or portfolio securities selection.

Some types of experience remain highly case-specific

While the quality and nature of the experience discussed above may differ from individual to individual and we assess experience on a case-by-case basis, there are some types of experience that are even more highly case-specific. This section sets out specific examples of case specific experience that may satisfy the relevant investment management experience requirement for advising representatives and associate advising representatives.

(a) IIROC registered representatives

Some registered representatives may offer a broad range of products involving security-specific research and analysis of their own, in addition to meeting with clients to review and discuss know-your-client and investment suitability. We may consider this to be sufficient experience to meet the relevant investment management experience requirement for registration as an advising representative. Other registered representatives may sell mostly or exclusively a limited number of model portfolios or “portfolio solutions” to clients based on their investment objectives, risk profile or other factors unique to the individual client. We may consider this sufficient experience to meet the relevant investment management experience requirement for registration as an associate advising representative.

However, where an individual is restricted to the sale of mutual funds, we may not consider such experience to be sufficient to meet the relevant investment management experience requirement for registration as an advising representative or associate advising representative.

(b) Consultants

Consulting services relating to portfolio manager selection and monitoring may be highly specific to the individual or firm providing the services and may vary greatly among consultants in the sophistication of research and analysis and specificity of advice. Some may be responsible for hiring and ongoing monitoring of advisers or sub-advisers, while others may simply provide a desired asset allocation and list of recommended advisers based on the investment objectives of the client. We would generally expect to see a very high degree of sophistication and specificity in the analysis provided by the consultant and a high degree of investor reliance on the consultant in order for the individual to meet the relevant investment management experience requirement for registration as an advising representative.

Research and analysis to review and monitor the performance of registered portfolio managers, and referring clients for discretionary money management based on that review and monitoring, may meet the relevant investment management experience requirement for registration as an associate advising representative. We would not expect that general financial planning advice and referrals to portfolio managers alone would meet the threshold for relevant investment management experience required for registration as an advising representative or associate advising representative.

In some situations, the activities submitted as relevant investment management experience involve or may involve providing specific advice to clients and therefore may require registration. We also recognize that many individuals who provide portfolio manager selection and monitoring do not provide specific advice and therefore may not trigger the registration requirement. We may consider the following factors in determining whether a consultant is required to register:

- the client contracts directly with the consultant, rather than with the portfolio managers

- the consultant manages the hiring and evaluation of the portfolio managers

- there is reliance by the client on the consultant

- there are client expectations about the services to be provided by the consultant

Division 3 Membership in a self-regulatory organization

3.16. Exemptions from certain requirements for SRO-approved persons

Section 3.16 exempts registered individuals who are dealing representatives of IIROC or MFDA members from the requirements in Regulation 31-103 for suitability and disclosure when recommending the use of borrowed money. This is because IIROC and the MFDA have their own rules for these matters.

In Québec, these requirements do not apply to dealing representatives of a mutual fund dealer to the extent that equivalent requirements are applicable to those dealing representatives under regulations in Québec.

This section also exempts registered individuals who are dealing representatives of IIROC from the know your client obligations in section 13.2.

We expect registered individuals who are dealing representatives of IIROC or MFDA members to comply with the by-laws, rules, regulations and policies of IIROC or the MFDA, as applicable (SRO provisions), except for registered individuals who are dealing representatives of a mutual fund dealer, for their activities in Québec. These individuals cannot rely on the exemptions in section 3.16 unless they are complying with the corresponding SRO provisions specified in Regulation 31-103. We regard compliance with IIROC or MFDA procedures, interpretations, notices, bulletins and practices as relevant to compliance with the applicable SRO provisions.

For these purposes, an individual that has an exemption from an SRO provision and complies with the terms of that exemption would be considered to have complied with that SRO provision.

PART 4 RESTRICTIONS ON REGISTERED INDIVIDUALS

4.1. Restriction on acting for another registered firm

We will consider exemption applications on a case-by-case basis. When reviewing a registered firm’s application for relief from this restriction, we will consider if:

- there are valid business reasons for the individual to be registered with both firms

- the individual will have sufficient time to adequately serve both firms

- the applicant’s sponsoring firms have demonstrated that they have policies and procedures addressing any conflicts of interest that may arise as a result of the dual registration, and

- the sponsoring firms will be able to deal with these conflicts, including supervising how the individual will deal with these conflicts.

In the case of paragraph 4.1(1)(b), namely a dealing, advising or associate advising representative acting for another registered firm, affiliation of the firms may be one of the factors that we would consider in respect of an exemption application.

We note that the prohibitions in section 4.1 are in addition to the conflicts of interest provisions set out in section 13.4. See section 13.4 for further guidance on individuals who serve on boards of directors.

4.2. Associate advising representatives – pre-approval of advice

The associate advising representative category allows an individual to work at a registered adviser while completing the proficiency requirements for an advising representative. For example, a previously registered advising representative could work in an advising capacity while acquiring the relevant work experience required for an advising representative under section 3.11.

Associate advising representatives are not required to subsequently register as a full advising representative since this category also accommodates individuals who provide specific advice to clients, but do not manage client portfolios without supervision.

As required by section 4.2, registered firms must designate an advising representative to approve the advice provided by an associate advising representative. The designated advising representative must approve the advice before the associate advising representative gives the advice. The appropriate processes for approving the advice will depend on the circumstances, including the associate advising representative's level of experience.

Registered firms that have associate advising representatives must:

- document their policies and procedures for meeting the supervision and approval obligations as required under subsection 11.1(1)

- implement controls as required under subsection 11.1(1)

- maintain records as required under section 11.5, and

- notify the regulator of the names of the advising representative and the associate advising representative whose advice they are approving no later than the 7th day after the advising representative is designated

PART 5 ULTIMATE DESIGNATED PERSON AND CHIEF COMPLIANCE OFFICER

Sections 11.2 and 11.3 require registered firms to designate a UDP and a CCO. The UDP and CCO must be registered and perform the compliance functions set out in sections 5.1 and 5.2. While the UDP and CCO have specific compliance functions, they are not solely responsible for compliance – it is the responsibility of the firm as a whole.

The same person as UDP and CCO

The UDP and the CCO can be the same person if they meet the requirements for both registration categories. We prefer firms to separate these functions, but we recognize that it might not be practical for some registered firms.

UDP or CCO as advising or dealing representative

The UDP or CCO may also be registered in trading or advising categories. For example, a small registered firm might conclude that one individual can adequately function as UDP and CCO, while also carrying on advising and trading activities. We may have concerns about the ability of a UDP or CCO of a large firm to conduct these additional activities and carry out their UDP, CCO and advising responsibilities at the same time.

5.1. Responsibilities of the ultimate designated person

The UDP is responsible for promoting a culture of compliance and overseeing the effectiveness of the firm's compliance system. They do not have to be involved in the day to day management of the compliance group. There are no specific education or experience requirements for the UDP. However, they are subject to the proficiency principle in section 3.4.

5.2. Responsibilities of the chief compliance officer

The CCO is an operating officer who is responsible for the monitoring and oversight of the firm's compliance system. This includes:

- establishing or updating policies and procedures for the firm's compliance system, and

- managing the firm's compliance monitoring and reporting according to the policies and procedures

At the firm's discretion, the CCO may also have authority to take supervisory or other action to resolve compliance issues.

The CCO must meet the proficiency requirements set out in Part 3. No other compliance staff have to be registered unless they are also advising or trading. The

CCO may set the knowledge and skills necessary or desirable for individuals who report to them.

If a firm is registered in multiple categories, the CCO must meet the most stringent of the proficiency requirements of the firm's categories of registration.

Firms must designate one CCO. However, in large firms, the scale and kind of activities carried out by different operating divisions may warrant the designation of more than one CCO. We will consider applications, on a case-by-case basis, for different individuals to act as the CCO of a firm's operating divisions.

We will not usually register the same person as CCO of more than one firm unless the firms are affiliated, and the scale and kind of activities carried out make it reasonable for the same person to act as CCO of more than one firm. We will consider applications, on a case-by-case basis, for the CCO of one registered firm to act as the CCO of another registered firm.

Paragraph 5.2(c) requires the CCO to report to the UDP any instances of non-compliance with securities legislation that:

- create a reasonable risk of harm to a client or to the market, or
- are part of a pattern of non-compliance

The CCO should report non-compliance to the UDP even if it has been corrected.

Paragraph 5.2(d) requires the CCO to submit an annual report to the board of directors.

PART 6 SUSPENSION AND REVOCATION OF REGISTRATION – INDIVIDUALS

The requirements for surrendering registration and additional requirements for suspending and revoking registration are found in the securities legislation of each jurisdiction. The guidance for Part 6 relates to requirements under both securities legislation and Regulation 31-103.

There is no renewal requirement for registration. A registered individual may carry on the activities for which they are registered until their registration is:

- suspended automatically under Regulation 31-103
- suspended by the regulator under certain circumstances, or
- surrendered by the individual

6.1. If individual ceases to have authority to act for firm

Under section 6.1, if a registered individual ceases to have authority to act on behalf of their sponsoring firm because their working relationship with the firm ends or changes, the individual's registration with the registered firm is suspended until reinstated or revoked under securities legislation. This applies whether the individual or the firm ends the relationship.

If a registered firm terminates its working relationship with a registered individual for any reason, the firm must complete and file a notice of termination on Form 33-109F1 *Notice of Termination of Registered Individuals and Permitted Individuals* (Form 33-109F1) no later than 10 days after the effective date of the individual's termination. This includes when an individual resigns, is dismissed or retires.

The firm must file additional information about the individual's termination prescribed in Part 5 of Form 33-109F1 (except where the individual is deceased), no later than 30 days after the date of termination. The regulator uses this information to determine if there are any concerns about the individual's conduct that may be relevant to their ongoing fitness for registration. Under Regulation 33-109, the firm must provide this information to the individual on request.

Suspension

An individual whose registration is suspended must not carry on the activity they are registered for. The individual otherwise remains a registrant and is subject to the jurisdiction of the regulator. A suspension remains in effect until the regulator reinstates or revokes the individual's registration.

If an individual who is registered in more than one category is suspended in one of the categories, the regulator will consider whether to suspend the individual's registration in other categories or to impose terms and conditions, subject to an opportunity to be heard.

Automatic suspension

An individual's registration will automatically be suspended if:

- they cease to have a working relationship with their sponsoring firm
- the registration of their sponsoring firm is suspended or revoked, or
- they cease to be an approved person of an SRO.

An individual must have a sponsoring firm to be registered. If an individual leaves their sponsoring firm for any reason, their registration is automatically suspended. Automatic suspension is effective on the day that an individual no longer has authority to act on behalf of their sponsoring firm.

Individuals do not have an opportunity to be heard by the regulator in the case of any automatic suspension.

Suspension in the public interest

An individual's registration may be suspended if the regulator exercises its power under securities legislation and determines that it is no longer in the public interest for the individual to be registered. The regulator may do this if it has serious concerns about the ongoing fitness of the individual. For example, this may be the case if an individual is charged with a crime, in particular fraud or theft.

Reinstatement

"Reinstatement" means that a suspension on a registration has been lifted. Once reinstated, an individual may resume carrying on the activity they are registered for. If a suspended individual joins a new sponsoring firm, they will have to apply for reinstatement under the process set out in Regulation 33-109. In certain cases, the reinstatement or transfer to the new firm will be automatic.

Automatic transfers

Subject to certain conditions set out in Regulation 33-109, an individual's registration may be automatically reinstated if they:

- transfer directly from one sponsoring firm to another registered firm in the same jurisdiction

- join the new sponsoring firm within 90 days of leaving their former sponsoring firm

- seek registration in the same category as the one previously held, and

- complete and file Form 33-109F7 *Reinstatement of Registered Individuals and Permitted Individuals* (Form 33-109F7)

This allows individuals to engage in activities requiring registration from their first day with the new sponsoring firm.

Individuals are not eligible for an automatic reinstatement if they:

- have new information to disclose regarding regulatory, criminal, civil or financial matters as described in Item 9 of Form 33-109F7, or

- as a result of allegations of criminal activity, breach of securities legislation or breach of SRO rules:

    - were dismissed by their former sponsoring firm, or

- were asked by their former sponsoring firm to resign

In these cases, the individual must apply to have their registration reinstated under Regulation 33-109 using Form 33-109F4.

6.2. If IIROC approval is revoked or suspended

6.3. If MFDA approval is revoked or suspended

Registered individuals acting on behalf of member firms of an SRO are required to be an approved person of the SRO.

If an SRO suspends or revokes its approval of an individual, the individual's registration in the category requiring SRO approval will be automatically suspended. This automatic suspension of individuals does not apply to mutual fund dealers registered only in Québec.

If an SRO suspends an individual for reasons that do not involve significant regulatory concerns and subsequently reinstates the individual's approval, the individual's registration will usually be reinstated by the regulator as soon as possible.

Revocation

6.6. Revocation of a suspended registration – individual

If an individual's registration has been suspended under Part 6 but not reinstated, it will be automatically revoked on the second anniversary of the suspension.

"Revocation" means that the regulator has terminated the individual's registration. An individual whose registration has been revoked must submit a new application if they want to be registered again.

Surrender or termination of registration

If an individual wants to terminate their registration in one or more of the non-principal jurisdictions where the individual is registered, the individual may apply to surrender their registration at any time by completing Form 33-109F2 *Change or Surrender of Individual Categories* (Form 33-109F2) and having their sponsoring firm file it.

If an individual wants to terminate their registration in their principal jurisdiction, Form 33-109F1 must be filed by the individual's sponsoring firm. Once Form 33-109F1 is filed, the individual's termination of registration will be reflected in all jurisdictions.

PART 7 CATEGORIES OF REGISTRATION FOR FIRMS

The categories of registration for firms have 2 main purposes:

- to specify the type of business that the firm may conduct, and

- to provide a framework for the requirements the registrant must meet

Firms registered in more than one category

A firm may be required to register in more than one category. For example, a portfolio manager that manages an investment fund must register both as a portfolio manager and as an investment fund manager.

Individual registered in a firm category

An individual can be registered in both a firm and individual category. For example, a sole proprietor who is registered in the firm category of portfolio manager must also be registered in the individual category of advising representative.

7.1. Dealer categories

Section 7.1 of Regulation 31-103 sets out the dealer registration categories and permitted activities for each category. For example, investment dealers may act as a dealer or an underwriter in respect of any security or transaction. All other dealer categories are limited:

- a mutual fund dealer may only act as a dealer in respect of mutual funds and certain other investment funds

- a scholarship plan dealer may only act as a dealer in respect of scholarship plans, educational plans and educational trusts

- a restricted dealer may only act as a dealer or an underwriter in accordance with the terms and conditions of its registration.

Exempt market dealer

Under paragraph 7.1(2)(d), an exempt market dealer may only act as a dealer or an underwriter in the "exempt market". The permitted activities of an exempt market dealer are determined by reference to the prospectus exemptions in securities legislation (e.g., the accredited investor, minimum amount investment and offering memorandum exemptions in Regulation 45-106). In short, an exempt market dealer may act as a dealer or underwriter in a distribution by an issuer, including a reporting issuer, if the distribution is being made under an exemption from the prospectus requirement. An exempt market dealer may not act as a dealer or underwriter in a distribution that is being made under a prospectus (a prospectus distribution). The investment dealer category or, in the case of a mutual fund prospectus distribution, the mutual fund dealer category, are the appropriate dealer registration categories for prospectus distributions.

This distinction is explained further below.

Trades that are distributions

Under subparagraph 7.1(2)(d)(i), exempt market dealers are permitted to trade in securities if the trade is a distribution made under a prospectus exemption. This includes trading in securities of investment funds and reporting issuers provided the securities are distributed under an exemption from the prospectus requirement. For example, where a reporting issuer is making a prospectus offering through an investment dealer, an exempt market dealer may participate in a private placement of securities of the same class, if those securities are actually distributed by the reporting issuer under a prospectus exemption. Certain form and fee requirements may apply to the private placement of securities under exemptions from the prospectus requirement.

Permitted activities under subparagraph 7.1(2)(d)(i) also include participating in a resale of securities, where the resale is *deemed* to be a distribution under *Regulation 45-102 respecting Resale of Securities* (chapter V-1.1, r. 20) (Regulation 45-102). For example, if a reporting issuer makes a private placement of common shares to an accredited investor in reliance on the accredited investor exemption in Regulation 45-106, the shares will generally be subject to a 4-month restricted period. If the accredited investor wishes to resell the shares to another accredited investor within the 4-month restricted period, the resale will be deemed to be a distribution under Regulation 45-102. An exempt market dealer may participate in this resale if made in reliance on a prospectus exemption. However, once the 4-month restricted period has expired, and the shares become freely trading, an exempt market dealer may not participate in the resale if common shares of the issuer are listed, quoted or traded on a marketplace, whether the transaction is on-exchange or off-exchange, due to the restriction in subparagraph 7.1(2)(d)(ii). Secondary trading in listed securities should be conducted through an investment dealer in accordance with the rules and requirements applicable to investment dealers.

Trades that are not distributions

Exempt market dealers are permitted to participate in a resale of securities, if all the conditions in subparagraph 7.1(2)(d)(ii) are met. These include that a prospectus exemption would have been available to the seller if the trade were a distribution and the class of securities is not listed, quoted or traded on a domestic or foreign marketplace. In determining whether a prospectus exemption is available for the purposes of subparagraph 7.1(2)(d)(ii), it is necessary to consider the terms of the prospectus exemption. For example, if the terms of the exemption provide that the exemption is only available to an issuer, it is not available for the resale of securities (e.g., offering memorandum exemption).

In short, exempt market dealers are permitted to:

- trade or underwrite securities if the trade is a distribution made under a prospectus exemption

- participate in the resale of securities that are subject to resale restrictions

- participate in the resale of securities, if a prospectus exemption would be available to the seller if the trade were a distribution and the class of securities is not listed, quoted or traded on a marketplace.

Exempt market dealers are not permitted to

- establish an omnibus account with an investment dealer and trade listed securities through the investment dealer on behalf of their clients, since this activity is trading in listed securities contrary to subparagraph 7.1(2)(d)(ii)

- participate in a distribution of securities offered under a prospectus in any capacity, including as a dealer (agent, finder, selling group member) or underwriter. This includes participating in the sale of special warrants convertible into prospectus qualified securities, since this activity is an "act in furtherance" of the trade of a prospectus qualified security contrary to subparagraph 7.1(2)(d)(i).

Restricted dealer

The restricted dealer category in paragraph 7.1(2)(e) permits specialized dealers that may not qualify under another dealer category, to carry on a limited trading business. It is intended to be used only if there is a compelling case for the proposed trading to take place outside the other registration categories.

The regulator will impose terms and conditions that restrict the dealer's activities. The CSA will co-ordinate terms and conditions for restricted dealers.

7.2. Adviser categories

The registration requirement in section 7.2 applies to advisers who give "specific advice". Advice is specific when it is tailored to the needs and circumstances of a client or potential client. For example, an adviser who recommends a security to a client is giving specific advice.

Restricted portfolio manager

The restricted portfolio manager category in paragraph 7.2(2)(b) permits individuals or firms to advise in specific securities, classes of securities or securities of a class of issuers.

The regulator will impose terms and conditions on a restricted portfolio manager's registration that limit the manager's activities. For example, a restricted portfolio manager might be limited to advising in respect of a specific sector, such as securities of oil and gas issuers.

7.3. Investment fund manager category

Investment fund managers direct the business, operations or affairs of an investment fund. They organize the fund and are responsible for its management and administration. If an entity is uncertain about whether it must register as an investment fund manager, it should consider whether the fund is an "investment fund" for the purposes of securities legislation. See section 1.2 of the Policy Statement to Regulation 81-106 for guidance on the general nature of investment funds.

For additional guidance on the investment fund manager registration requirement in Alberta, British Columbia, Manitoba, Nova Scotia, New Brunswick, Northwest Territories, Nunavut, Prince Edward Island, Saskatchewan and Yukon see Multilateral Policy 31-202 *Registration Requirement for Investment Fund Managers.* Newfoundland and Labrador, Ontario and Québec have adopted *Regulation 32-102 respecting Registration Exemptions for Non-Resident Investment Fund Managers* (chapter V-1.1, r. 10.1) and *Policy Statement to Regulation 32-102 respecting Registration Exemptions for Non-Resident Investment Fund Managers* (Decision 2012-PDG-0160, 2012-08-08), which provide limited exemptions from, and guidance on, the investment fund manager registration requirement for non-resident investment fund managers.

An investment fund manager may:

- advertise to the general public a fund it manages without being registered as an adviser, and

- promote the fund to registered dealers without being registered as a dealer

If an investment fund manager acts as portfolio manager for a fund it manages, it should consider whether it may have to be registered as an adviser. If it distributes units of the fund directly to investors, it should consider whether it may have to be registered as a dealer.

In most fund structures, the investment fund manager is a separate legal entity from the fund itself. However, in situations where the board of directors or the trustee(s) of an investment fund direct the business, operations or affairs of the investment fund, the fund itself may be required to register in the investment fund manager category. To address the investor protection concerns that may arise from the investment fund manager and the fund being the same legal entity, and the practical issues of applying the ongoing requirements of a registrant on the fund, terms and conditions may be imposed.

An investment fund manager may delegate or outsource certain functions to service providers. However, the investment fund manager is responsible for these functions and must supervise the service provider. See Part 11 of this Policy Statement for more guidance on outsourcing.

Investment fund complexes or groups with more than one investment fund manager

Determining whether investment fund registration is necessary involves applying a functional test that examines the activities being carried out to determine whether an entity is directing the business, operations or affairs of an investment fund. Typically an investment fund has only one investment fund manager. However, there may be limited circumstances where investment fund complexes or groups may have more than one entity within the fund complex that is acting as an investment fund manager. Although the investment fund manager functions are often delegated to one entity within the fund complex, there may be more than one entity in the group subject to investment fund manager registration, absent an exemption from registration. We will consider exemption applications on a case-by-case basis to allow only one investment fund manager within the fund complex to be registered in appropriate circumstances.

PART 8 EXEMPTIONS FROM THE REQUIREMENT TO REGISTER

Regulation 31-103 provides several exemptions from the registration requirement. There may be additional exemptions in securities legislation. If a firm is exempt from registration, the individuals acting on its behalf are also exempt from registration. A person cannot rely on the exemptions in Divisions 1, 2 and 3 of this Part in a local jurisdiction if the person is registered to conduct the activities covered by the exemption in that jurisdiction. We expect registrants to conduct activities within a jurisdiction under their category of registration, in full compliance with securities legislation, including the requirements of Regulation 31-103.

Division 1 Exemptions from dealer and underwriter registration

We provide no specific guidance for the following exemptions because there is guidance on them in the Policy Statement to Regulation 45-106:

- 8.12
- 8.17

8.5. Trades through or to a registered dealer

No solicitation or contact

Section 8.5 provides an exemption from the dealer registration requirement for trades made

- through an appropriately registered dealer, or
- to an appropriately registered dealer that is purchasing for that dealer's account.

The exemption in paragraph 8.5(1)(a) for trades made through a registered dealer is not available if the person relying on it solicits or contacts purchasers of the securities directly. For example, if an individual acts in furtherance of a trade by soliciting or contacting potential purchasers of securities (sometimes referred to as a finder) and then the sale to the purchaser is executed through a registered dealer, the individual would not qualify for this exemption.

A person may utilize the exemption for acts in furtherance of a trade in relation to working with issuers or appropriately registered dealers, provided they do not directly solicit or contact purchasers.

Cross-border trades (jitneys)

Section 8.5 provides an exemption from the dealer registration requirement if the trade is made through a registered dealer, provided the person relying on the exemption has no direct contact with the purchaser of the security. On that basis, the execution of a trade through or to an appropriately registered dealer by a dealer located in another jurisdiction would qualify under this exemption.

However, if for example a dealer in the United States that is not registered in Alberta contacts a potential purchaser in Alberta to solicit the purchase of securities, this trade does not qualify for this exemption. The dealer in the United States must instead contact a dealer registered in Alberta, and have that dealer contact potential purchasers in Alberta.

Plan administrators

A plan administrator can rely on this exemption to place sell orders with dealers in respect of shares of issuers held by plan participants. Section 8.16 covers the activity of the plan administrator receiving sell orders from plan participants.

8.5.1. Trades through a registered dealer by registered adviser

Section 8.5.1 provides that the dealer registration requirement does not apply to a registered adviser for incidental trading activities. The exemption is only available if the trade is made through a registered dealer or a dealer exempt from registration. For example, a portfolio manager may not use the exemption to trade units of a pooled fund it manages, without involving a registered dealer or having another exemption available, including the exemption in section 8.6.

8.6. Investment fund trades by adviser to managed account

Registered advisers often use investment funds which they or their affiliates have created as a way to efficiently invest their clients' money. In issuing units of those funds to managed account clients, they are in the business of trading in securities. Under the exemption in section 8.6, a registered adviser does not have to register as a dealer for a trade in a security of an investment fund if:

- the adviser or an affiliate of the adviser acts as the fund's adviser,

- the adviser or an affiliate of the adviser acts as the fund's investment fund manager, and

- the distribution of units of the fund is made only into the adviser's clients' managed accounts.

Subsection 8.6(2) limits the availability of this exemption to legitimate managed accounts. The exemption is not available in respect of accounts that are in substance non-discretionary accounts and that have been created primarily for the purpose of distributing investment funds of the adviser to an investor without the involvement of a registered dealer.

An adviser relying on this exemption is required to provide written notice of its reliance on the exemption.

The exemption in section 8.6 is also available to those who qualify for the international adviser exemption under section 8.26.

8.18. International dealer

General principle

This exemption allows international dealers to provide limited services to permitted clients without having to register in Canada. The term "permitted client" is defined in section 1.1. International dealers that seek wider access to Canadian investors must register in an appropriate category.

Notice requirement

If a firm is relying on the exemption in more than one jurisdiction, it must provide an initial notice by filing a Form 31-103F2 *Submission to Jurisdiction and Appointment of Agent for Service* (Form 31-103F2) with the regulator in each jurisdiction where it relies on the exemption. If there is any change to the information in the firm's Form 31-103F2, it must update it by filing a replacement Form 31-103F2 with them.

So long as the firm continues to rely on the exemption, it must file an annual notice with each regulator. Subsection 8.18(5) does not prescribe a form of annual notice. An email or letter will therefore be acceptable.

In Ontario, compliance with the filing and fee payment requirements applicable to an unregistered exempt international dealer under Ontario Securities Commission Rule 13-502 *Fees* satisfies the annual notification requirement in subsection (5).

8.19. Self-directed registered education savings plan

We consider the creation of a self-directed registered education savings plan, as defined in section 8.19, to be a trade in a security, whether or not the assets held in the plan are securities. This is because the definition of "security" in securities legislation of most jurisdictions includes "any document constituting evidence of an interest in a scholarship or educational plan or trust".

Section 8.19 provides an exemption from the dealer registration requirement for the trade when the plan is created but only under the conditions described in subsection 8.19(2).

8.22.1. Short-term debt

This exemption allows specified financial institutions to trade short-term debt instruments with permitted clients, without having to register. The exemption is available in all jurisdictions of Canada, except Ontario. In Ontario, there are alternate exemptions that may be available for trading in short-term debt instruments, including the exemptions in section 35.1 of the *Securities Act* (R.S.O. 1990, c. S. 5) and section 4.1 of the Ontario Securities Commission Rule 45-501 *Ontario Prospectus and Registration Exemptions*.

Division 2 Exemptions from adviser registration

8.24. IIROC members with discretionary authority

Section 8.24 contains an exemption from the requirement to register as an adviser for registered dealers that are members of IIROC and their dealing representatives. The exemption is available when they act as an adviser in respect of a client's managed account. The term "managed account" is defined in section 1.1 of Regulation 31-103. This exemption is available for all managed accounts, including where the client is a pooled fund or investment fund.

8.25. Advising generally

Section 8.25 contains an exemption from the requirement to register as an adviser if the advice is not tailored to the needs of the recipient.

In general, we would not consider advice about specific securities to be tailored to the needs of the recipient if it:

- is a general discussion of the merits and risks of the security

- is delivered through investment newsletters, articles in general circulation newspapers or magazines, websites, e-mail, Internet chat rooms, bulletin boards, television or radio, and

- does not claim to be tailored to the needs and circumstances of any recipient

This type of general advice can also be given at conferences. However, if a purpose of the conference is to solicit the audience and generate specific trades in specific securities, we may consider the advice to be tailored or we may consider the individual or firm giving the advice to be engaged in trading activity.

Under subsection 8.25(3), if an individual or firm relying on the exemption has a financial or other interest in the securities they recommend, they must disclose the interest to the recipient when they make the recommendation.

8.26. International adviser

This exemption allows international advisers to provide limited services to certain permitted clients without having to register in Canada. International advisers that seek wider access to Canadian investors must register in an appropriate category.

Incidental advice on Canadian securities

An international adviser relying on the exemption in section 8.26 may advise in Canada on foreign securities without having to register. It may also advise in Canada on securities of Canadian issuers, but only to the extent that the advice is incidental to its acting as an adviser for foreign securities.

However, this is not an exception or a "carve-out" that allows some portion of a permitted client's portfolio to be made up of Canadian securities chosen by the international adviser without restriction. Any advice with respect to Canadian securities must be directly related to the activity of advising on foreign securities. Permissible incidental advice would include, for example:

- an international adviser, when advising on a portfolio with a particular investment objective, such as gold mining companies, could advise on securities of a Canadian gold mining company within that portfolio, provided that the portfolio is otherwise made up of foreign securities

- an international adviser, having a mandate to advise on equities traded on European exchanges could advise with respect to the securities of a Canadian corporation traded on a European exchange, to the extent the Canadian corporation forms part of the mandate

Revenue derived in Canada

An international adviser is only permitted to undertake a prescribed amount of business in Canada. In making the calculation required under paragraph 8.26(4)(d), it is necessary to include all revenues derived from portfolio management activities in Canada, which would include any sub-adviser arrangements. However, the calculation of aggregate consolidated gross revenue derived in Canada does not include the gross revenue of affiliates that are registered in a jurisdiction of Canada.

An international adviser is not required to monitor Canadian revenue on an ongoing basis. Eligibility for the exemption is assessed with reference to revenues as of the end of the adviser's last financial year. The 10% threshold in paragraph 8.26(4)(d) is determined by looking back at the revenue of the firm and its affiliates "during its most recently completed financial year".

Notice requirement

If a firm is relying on the exemption in more than one jurisdiction, it must provide an initial notice by filing a Form 31-103F2 with the regulator in each jurisdiction where it relies on the exemption. If there is any change to the information in the firm's Form 31-103F2, it must update it by filing a replacement Form 31-103F2 with them.

So long as the firm continues to rely on the exemption, it must file an annual notice with each regulator. Subsection 8.26(5) does not prescribe a form of annual notice. An email or letter will therefore be acceptable.

In Ontario, compliance with the filing and fee payment requirements applicable to an unregistered exempt international firm under Ontario Securities Commission Rule 13-502 *Fees* satisfies the annual notification requirement in subsection (5).

8.26.1. International sub-adviser

This exemption permits a foreign sub-adviser to provide advice to certain registrants, without having to register as an adviser in Canada. In these arrangements, the registrant is the foreign sub-adviser's client, and it receives the advice, either for its own benefit or for the benefit of its clients. One of the conditions of this exemption is that the registrant has entered into an agreement with its client that it is responsible for losses that arise out of certain failures by the sub-adviser.

We expect that a registrant taking on this liability will conduct appropriate initial and ongoing due diligence on the sub-adviser and ensure the investments are suitable for the registrant's client. We also expect that the registrant will maintain records of the due diligence conducted. See Part 11 of this Policy Statement for more guidance.

Division 4 Mobility exemption – firms

8.30. Client mobility exemption – firms

The mobility exemption in section 8.30 allows registered firms to continue dealing with and advising clients who move to another jurisdiction, without registering in that other jurisdiction. Section 2.2 contains a similar exemption for registered individuals.

The exemption becomes available when the client (not the registrant) moves to another jurisdiction. A registered firm may deal with up to 10 "eligible" clients in each other jurisdiction. Each of the client, their spouse and any children are an eligible client.

A firm may only rely on the exemption if:

- it is registered in its principal jurisdiction
- it only acts as a dealer, underwriter or adviser in the other jurisdiction as permitted under its registration in its principal jurisdiction
- the individual acting on its behalf is eligible for the exemption in section 2.2
- it complies with Parts 13 and 14, and

- it acts fairly, honestly and in good faith in its dealings with the eligible client

Firm's responsibilities for individuals relying on the exemption

In order for a registered individual to rely on the exemption in section 2.2, their sponsoring firm must disclose to the eligible client that the individual and if applicable, the firm, are exempt from registration in the other jurisdiction and are not subject to the requirements of securities legislation in that jurisdiction.

As soon as possible after an individual first relies on the exemption in section 2.2, their sponsoring firm must complete and file Form 31-103F3 in the other jurisdiction.

The registered firm must have appropriate policies and procedures for supervising individuals who rely on a mobility exemption. Registered firms must also keep appropriate records to demonstrate they are complying with the conditions of the mobility exemption.

See the guidance in section 2.2 of this Policy Statement on the client mobility exemption available to individuals.

PART 9 MEMBERSHIP IN AN SELF-REGULATORY ORGANIZATION

9.3. Exemptions from certain requirements for IIROC members

9.4. Exemptions from certain requirements for MFDA members

Regulation 31-103 has 2 distinct sections, sections 9.3 and 9.4, which distinguish the exemptions which are available on the basis of whether or not the member of IIROC or the MFDA is registered in another category. This clarifies our intent with respect to the exemptions for SRO members and recognizes that IIROC and the MFDA have rules in these areas.

Sections 9.3 and 9.4 contain exemptions from certain requirements for investment dealers that are IIROC members, for mutual fund dealers that are MFDA members (except in Québec) and in Québec, for mutual fund dealers to the extent equivalent requirements are applicable under the regulations in Québec.

However, if an SRO member is registered in another category, these sections do not exempt them from their obligations as a registrant in that category. For example, if a firm is registered as an investment fund manager and as an investment dealer with IIROC, section 9.3 does not exempt them from their obligations as an investment fund manager under Regulation 31-103.

However SRO members that are registered in multiple categories may use the forms prescribed by the SROs, on certain conditions. See sections 12.1, 12.12 and 12.14 for requirements on calculating working capital and the delivery of working capital calculations for SRO members that are registered in multiple categories.

We expect registered firms that are members of IIROC or the MFDA to comply with the by-laws, rules, regulations and policies of IIROC or the MFDA, as applicable (SRO provisions). These firms cannot rely on the exemptions in Part 9 unless they are complying with the corresponding SRO provisions specified in Regulation 31-103. We wish to clarify that we expect firms registered as mutual fund dealers, for their activities in Québec, to comply only with the provisions of the by-laws, rules, regulations and policies that are applicable to them. We regard compliance with IIROC or MFDA procedures, interpretations, notices, bulletins and practices as relevant to compliance with the applicable SRO provisions.

For these purposes, a firm that has an exemption from an SRO provision and complies with the terms of that exemption would be considered to have complied with that SRO provision.

Subsection 9.4(4) provides that mutual fund dealers registered in that category in Québec that are also registered in that category in another jurisdiction are exempt from sections 14.5.2 to 14.6.2 relating to the custody of assets, to the extent the registered firm complies with relevant MFDA requirements, as applicable.

PART 10 SUSPENSION AND REVOCATION OF REGISTRATION – FIRMS

The requirements for surrendering registration and additional requirements for suspending and revoking registration are found in the securities legislation of each jurisdiction. The guidance for Part 10 relates to requirements under both securities legislation and Regulation 31-103.

There is no renewal requirement for registration but firms must pay fees every year to maintain their registration and the registration of individuals acting on their behalf. A registered firm may carry on the activities for which it is registered until its registration is:

- suspended automatically under Regulation 31-103
- suspended by the regulator under certain circumstances, or
- surrendered by the firm

Division 1 When a firm's registration is suspended

Suspension

A firm whose registration has been suspended must not carry on the activity it is registered for. The firm otherwise remains a registrant and is subject to the jurisdiction of the regulator. A suspension remains in effect until the regulator reinstates or revokes the firm's registration.

If a firm that is registered in more than one category is suspended in one of the categories, the regulator will consider whether to suspend the firm's registration in other categories or to impose terms and conditions, subject to an opportunity to be heard.

Automatic suspension

A firm's registration will automatically be suspended if:

- it fails to pay its annual fees within 30 days of the due date
- it ceases to be a member of IIROC, or
- except in Québec, it ceases to be a member of the MFDA

Firms do not have an opportunity to be heard by the regulator in the case of any automatic suspension.

10.1. Failure to pay fees

Under section 10.1, a firm's registration will be automatically suspended if it has not paid its annual fees within 30 days of the due date.

10.2. If IIROC membership is revoked or suspended

Under section 10.2, if IIROC suspends or revokes a firm's membership, the firm's registration as an investment dealer is suspended until reinstated or revoked.

10.3. If MFDA membership is revoked or suspended

Under section 10.3, if the MFDA suspends or revokes a firm's membership, the firm's registration as a mutual fund dealer is suspended until reinstated or revoked. Section 10.3 does not apply in Québec.

Suspension in the public interest

A firm's registration may be suspended if the regulator exercises its power under securities legislation and determines that it is no longer in the public interest for the firm to be registered. The regulator may do this if it has serious concerns about the ongoing fitness of the firm or any of its registered individuals. For example, this may be the case if a firm or one or more of its registered or permitted individuals is charged with a crime, in particular fraud or theft.

Reinstatement

"Reinstatement" means that a suspension on a registration has been lifted. Once reinstated, a firm may resume carrying on the activity it is registered for.

Division 2 Revoking a firm's registration

Revocation

10.5. Revocation of a suspended registration – firm

10.6. Exception for firms involved in a hearing or proceeding

Under sections 10.5 and 10.6, if a firm's registration has been suspended under Part 10 and has not been reinstated, it is revoked on the second anniversary of the suspension, except if a hearing or proceeding concerning the suspended registrant has commenced. In this case the registration remains suspended.

"Revocation" means that the regulator has terminated the firm's registration. A firm whose registration has been revoked must submit a new application if it wants to be registered again.

Surrender

A firm may apply to surrender its registration in one or more categories at any time. There is no prescribed form for an application to surrender. A firm should file an application to surrender registration with its principal regulator. If Ontario is a non-principal jurisdiction, it should also file the application with the regulator in Ontario. See the *Policy Statement to Regulation 11-102 respecting Passport System* (Decision 2012-PDG-0038, 2012-03-01) for more details on filing an application to surrender.

Before the regulator accepts a firm's application to surrender registration, the firm must provide the regulator with evidence that the firm's clients have been dealt with appropriately. This evidence does not have to be provided when a registered individual applies to surrender registration. This is because the sponsoring firm will continue to be responsible for meeting obligations to clients who may have been served by the individual.

The regulator does not have to accept a firm's application to surrender its registration. Instead, the regulator can act in the public interest by suspending, or imposing terms and conditions on, the firm's registration.

When considering a registered firm's application to surrender its registration, the regulator typically considers the firm's actions, the completeness of the application and the supporting documentation.

The firm's actions

The regulator may consider whether the firm:

- has stopped carrying on activity requiring registration

- proposes an effective date to stop carrying on activity requiring registration that is within 6 months of the date of the application to surrender, and

- has paid any outstanding fees and submitted any outstanding filings at the time of filing the application to surrender

Completeness of the application

Among other things, the regulator may look for:

- the firm's reasons for ceasing to carry on activity requiring registration

- satisfactory evidence that the firm has given all of its clients reasonable notice of its intention to stop carrying on activity requiring registration, including an explanation of how it will affect them in practical terms, and

- satisfactory evidence that the firm has given appropriate notice to the SRO, if applicable

Supporting documentation

The regulator may look for:

- evidence that the firm has resolved all outstanding client complaints, settled all litigation, satisfied all judgments or made reasonable arrangements to deal with and fund any payments relating to them, and any subsequent client complaints, settlements or liabilities

- confirmation that all money or securities owed to clients has been returned or transferred to another registrant, where possible, according to client instructions

- up-to-date audited financial statements with an auditor's comfort letter

- evidence that the firm has satisfied any SRO requirements for withdrawing membership, and

- an officer's or partner's certificate supporting these documents

PART 11 INTERNAL CONTROLS AND SYSTEMS

General business practices – outsourcing

Registered firms are responsible and accountable for all functions that they outsource to a service provider. Firms should have a written, legally binding contract that includes the expectations of the parties to the outsourcing arrangement.

Registered firms should follow prudent business practices and conduct a due diligence analysis of prospective third-party service providers. This includes third-party service providers that are affiliates of the firm. Due diligence should include an assessment of the service provider’s reputation, financial stability, relevant internal controls and ability to deliver the services.

Firms should also:

- ensure that third-party service providers have adequate safeguards for keeping information confidential and, where appropriate, disaster recovery capabilities

- conduct ongoing reviews of the quality of outsourced services

- develop and test a business continuity plan to minimize disruption to the firm’s business and its clients if the third-party service provider does not deliver its services satisfactorily, and

- note that other legal requirements, such as privacy laws, may apply when entering into outsourcing arrangements

The regulator, the registered firm and the firm’s auditors should have the same access to the work product of a third-party service provider as they would if the firm itself performed the activities. Firms should ensure this access is provided and include a provision requiring it in the contract with the service provider, if necessary.

Division 1 Compliance

11.1. Compliance system and training

General principles

Subsection 11.1(1) requires registered firms to establish, maintain and apply policies and procedures that establish a system of controls and supervision (a compliance system) that:

- provides assurance that the firm and individuals acting on its behalf comply with securities legislation, and

- manages the risks associated with the firm’s business in accordance with prudent business practices

Operating an effective compliance system is essential to a registered firm’s continuing fitness for registration. It provides reasonable assurance that the firm is meeting, and will continue to meet, all requirements of applicable securities laws and SRO rules and is managing risk in accordance with prudent business practices. A compliance system should include internal controls and monitoring systems that are reasonably likely to identify non-compliance at an early stage and supervisory systems that allow the firm to correct non-compliant conduct in a timely manner.

The responsibilities of the UDP are set out in section 5.1 and those of the CCO in section 5.2. However, compliance is not only a responsibility of a specific individual or a compliance department of the firm, but rather is a firm-wide responsibility and an integral part of the firm's activities. Everyone at the firm should understand the standards of conduct for their role. This includes the board of directors, partners, management, employees and agents, whether or not they are registered.

Having a UDP and CCO, and in larger firms, a compliance group and other supervisory staff, does not relieve anyone else in the firm of the obligation to report and act on compliance issues. A compliance system should identify those who will act as alternates in the absence of the UDP or CCO.

Elements of an effective compliance system

While policies and procedures are essential, they do not make an acceptable compliance system on their own. An effective compliance system also includes internal controls, day to day and systemic monitoring, and supervision elements.

Internal controls

Internal controls are an important part of a firm's compliance system. They should mitigate risk and protect firm and client assets. They should be designed to assist firms in monitoring compliance with securities legislation and managing the risks that affect their business, including risks that may relate to:

- safeguarding of client and firm assets
- accuracy of books and records
- trading, including personal and proprietary trading
- conflicts of interest
- referral arrangements
- money laundering
- business interruption
- hedging strategies
- marketing and sales practices, including the use of titles and designations by the firm's registered individuals, and
- the firm's overall financial viability

Internal controls should also be specifically designed to assist firms in monitoring compliance with the know your client, know your product and suitability determination obligations.

Monitoring and supervision

Monitoring and supervision are essential elements of a firm's compliance system. They consist of day to day monitoring and supervision, and overall systemic monitoring.

(a) Day to day monitoring and supervision

In our view, an effective monitoring and supervision system includes:

- monitoring to identify specific cases of non-compliance or internal control weaknesses that might lead to non-compliance
- referring non-compliance or internal control weaknesses to management or other individuals with authority to take supervisory action to correct them
- taking supervisory action to correct them, and
- minimizing the compliance risk in key areas of a firm's operations

In our view, effective day to day monitoring should include, among other things

- approving new account documents
- reviewing and, in some cases, approving transactions
- approving marketing materials, and
- preventing inappropriate use or disclosure of non-public information.

Firms can use a risk-based approach to monitoring, such as reviewing an appropriate sample of transactions.

The firm's management is responsible for the supervisory element of correcting non-compliance or internal control weaknesses. However, at a firm's discretion, its CCO may be given supervisory authority, but this is not a necessary component of the CCO's role.

Anyone who supervises registered individuals has a responsibility on behalf of the firm to take all reasonable measures to ensure that each of these individuals:

- deals fairly, honestly and in good faith with their clients
- addresses conflicts of interest in the best interest of their clients

- puts the client's interests first when making suitability determinations for their clients

- complies with securities legislation

- complies with the firm's policies and procedures, and

- maintains an appropriate level of proficiency

(b) Systemic monitoring

Systemic monitoring involves assessing, and advising and reporting on the effectiveness of the firm's compliance system. This includes ensuring that:

- the firm's day to day supervision is reasonably effective in identifying and promptly correcting cases of non-compliance and internal control weaknesses

- policies and procedures are enforced and kept up to date, and

- everyone at the firm generally understands and complies with the policies and procedures, and with securities legislation

Specific elements

More specific elements of an effective compliance system include:

(a) Visible commitment

Senior management and the board of directors or partners should demonstrate a visible commitment to compliance.

(b) Sufficient resources

The firm should have sufficient resources to operate an effective compliance system. Qualified individuals (including anyone acting as an alternate during absences) should have the responsibility and authority to monitor the firm's compliance, identify any instances of non-compliance and take supervisory action to correct them.

(c) Detailed policies and procedures

The firm should have detailed written policies and procedures that:

- identify the internal controls the firm will use to ensure compliance with legislation and manage risk

- set out the firm's standards of conduct for compliance with securities and other applicable legislation and the systems for monitoring and enforcing compliance with those standards

- clearly outline who is expected to do what, when and how
- are readily accessible by everyone who is expected to know and follow them
- are updated when regulatory requirements and the firm's business practices change,
- take into consideration the firm's obligation under securities legislation to deal fairly, honestly and in good faith with its clients.
- take into consideration the firm's obligation to address conflicts of interest in the best interest of its clients, and
- take into consideration the firm's obligation to put the client's interest first when making suitability determinations for its clients.

Registered firms should have compliance systems that are effective in all business locations of the firm, not just the firm's head office.

(d) Detailed records

The firm should keep records of activities conducted to identify compliance deficiencies and the action taken to correct them.

Setting up a compliance system

It is up to each registered firm to determine the most appropriate compliance system for its operations. Registered firms should consider the size and scope of their operations, including products, types of clients or counterparties, risks and compensating controls, and any other relevant factors.

For example, a large registered firm with diverse operations may require a large team of compliance professionals with several divisional heads of compliance reporting to a CCO dedicated entirely to a compliance role.

All firms must have policies, procedures and systems to demonstrate compliance. However, some of the elements noted above may be unnecessary or impractical for smaller registered firms.

We encourage firms to meet or exceed industry best practices in complying with regulatory requirements.

Firm's obligation to provide compliance training

Under subsection 11.1(2), firms must provide compliance training. We expect firms to implement, maintain and document their compliance training program to ensure that everyone at the firm understands the standards of conduct when dealing with clients, and understands their role in the compliance system.

In particular, registered individuals should be trained in relation to their conflicts of interest, know your client, know your product and suitability determination obligations. We expect the firm to provide examples of:

- how to identify existing and reasonably foreseeable material conflicts of interest between a registered individual and their client

- how to address material conflicts of interest in the best interest of their client, and

- how to put the client's interest first when making suitability determinations for their client.

We expect the firm's compliance training program to include ongoing communication and training on changes in regulatory requirements or the firm's policies and procedures.

We recognize that the scope of a firm's compliance training will depend on the nature, size and complexity of its business. We also recognize that training materials do not necessarily have to be in writing. We expect a firm to use its professional judgment when evaluating the effectiveness of its compliance training program, including the identification of any gaps.

We expect all registered firms to be able to demonstrate that they have all the required elements of an effective compliance system, regardless of their size or any other consideration. However, we recognize that formal compliance training programs may not be necessary or practical for small firms. We expect a small firm to exercise professional judgment in determining what training is appropriate to its operations, taking into consideration how many registered individuals work at the firm and how much relevant experience each of them has accumulated.

Training to support the know your product obligation

Consistent with the know your product obligation in section 13.2.1, firms should also assess whether any additional training or proficiency requirements are necessary in order for their registered individuals to understand the securities and make appropriate suitability determinations. See section 13.2.1 of this Policy Statement for additional guidance on the know your product obligation.

Outsourcing of training

Although a firm may outsource elements of its training program, the firm remains responsible for demonstrating that its registered individuals have been trained on the firm's policies and procedures.

11.2. Designating an ultimate designated person

Under subsection 11.2(1), registered firms must designate an individual to be the UDP. Firms should ensure that the individual understands and is able to perform the obligations of a UDP under section 5.1. The UDP must be:

- the chief executive officer (CEO) of the registered firm or the individual acting in a similar capacity, if the firm does not have a CEO. The person acting in a similar capacity to a CEO is the most senior decision maker in the firm, who might have the title of managing partner or president, for example

- the sole proprietor of the registered firm, or

- the officer in charge of a division of the firm that carries on all of the registerable activity if the firm also has significant other business activities, such as insurance, conducted in different divisions. This is not an option if the core business of the firm is trading or advising in securities and it only has some other minor operations conducted in other divisions. In this case, the UDP must be the CEO or equivalent.

To designate someone else as the UDP requires an exemptive relief order. Given that the intention of section 11.2 is to ensure that responsibility for its compliance system rests at the very top of a firm, we will only grant relief in rare cases.

We note that in larger organizations, the UDP is sometimes supported by an officer who has a compliance oversight role and title within the organization and who is more senior than the CCO. We have no objection to such arrangements, but it must be understood that they can in no way diminish the UDP's regulatory responsibilities.

If the person designated as the UDP no longer meets these requirements, and the registered firm is unable to designate another UDP, the firm should promptly advise the regulator of the actions it is taking to designate a new UDP who meets these requirements.

11.3. Designating a chief compliance officer

Under subsection 11.3(1), registered firms must designate an individual to be the CCO. Firms should ensure that the individual understands and is able to perform the obligations of a CCO under section 5.2.

The CCO must meet the applicable proficiency requirements in Part 3 and be:

- an officer or partner of the registered firm, or

- the sole proprietor of the registered firm

If the CCO no longer meets any of the above conditions and the registered firm is unable to designate another CCO, the firm should promptly advise the regulator of the actions it is taking to designate an appropriate CCO.

Division 2 Books and records

Under securities legislation, the regulator may access, examine and take copies of a registered firm's records. The regulator may also conduct regular and unscheduled compliance reviews of registered firms.

11.5. General requirements for records

Under subsection 11.5(1), registered firms must maintain records to accurately record their business activities, financial affairs and client transactions, and demonstrate compliance with securities legislation.

The following discussion provides guidance for the various elements of the records described in subsection 11.5(2).

Financial affairs

The records required under paragraphs 11.5(2)(a), (b) and (c) are records firms must maintain to help ensure they are able to prepare and file financial information, determine their capital position, including the calculation of excess working capital, and generally demonstrate compliance with the capital and insurance requirements.

Client transactions

The records required under paragraphs 11.5(2)(g), (h), (i), (l) and (n) are records firms must maintain to accurately and fully document transactions entered into on behalf of a client. We expect firms to maintain notes of communications that could have an impact on the client's account or the client's relationship with the firm. These communications include

- oral communications
- all e-mail, regular mail, fax and other written communications

While we do not expect registered firms to save every voicemail or e-mail, or to record all telephone conversations with clients, we do expect that registered firms maintain records of all communications relating to orders received from their clients.

The records required under paragraph 11.5(2)(g) should document buy and sell transactions, referrals, margin transactions and any other activities relating to a client's account. They include records of all actions leading to trade execution, settlement and clearance, such as trades on exchanges, alternative trading systems, over-the-counter markets, debt markets, and distributions and trades in the prospectus-exempt market.

Examples of these records are:

- trade confirmation statements

- summary information about account activity

- communications between a registrant and its client about particular transactions, and

- records of transactions resulting from securities a client holds, such as dividends or interest paid, or dividend reinvestment program activity

Know your client

Paragraph 11.5(2)(l) requires firms to maintain records that demonstrate compliance with the know your client obligations in section 13.2, the know your product obligations in section 13.2.1 and the suitability determination obligations in section 13.3.

We expect firms to establish, maintain and apply policies, procedures and controls relating to the know your client process, in accordance with their category of registration, their business model, their client's type of account and the nature of the relationship with their clients. We also expect firms to maintain adequate documentation to support their supervision of the know your client process.

Among these policies, procedures and controls, firms should consider including a process for:

- determining the appropriate level of know your client information to be collected in the circumstances

- determining how the subjective elements of the client's information collected under paragraph 13.2(c), including investment time horizon, investment objectives and risk profile, are established

- determining what is a significant change to the client's information, and

- obtaining and recording the client's confirmation of the accuracy of their know your client information.

Know your product

We expect firms to establish, maintain and apply policies, procedures and controls relating to the know your product process, in accordance with the firm's business model, the types of securities offered, the proficiency of its registered individuals, and the nature of the relationships that the firm and its registered individuals have with clients. These policies, procedures and controls should include appropriate processes for assessing and approving, as well as monitoring for significant changes to, securities that are made available to clients. See section 13.2.1 of this Policy Statement for more guidance on the know your product obligation.

Suitability determinations

Registrants should document the basis upon which they make a suitability determination. We expect registrants to maintain records documenting all relevant facts, including key assumptions, the scope of data considered, and the analysis performed in making each suitability determination.

We expect registered firms to:

- establish policies and procedures for making a suitability determination (including the criteria used and when it is performed) and demonstrate that the suitability process is consistently applied across the firm

- maintain adequate documentation of each suitability determination, and

- establish a process to periodically review a sample of client files to ensure that the suitability process is consistently applied throughout the firm.

Firms must also maintain records for measures taken in respect of client instructions referred to in subsection 13.3(2.1).

In our view, a pattern of unsuitable trades that are reported as having been directed by a client may be an indication that a registrant does not comply with the obligation to make a suitability determination. We expect firms to establish, maintain and apply policies, procedures and controls to identify and respond to any pattern of unsuitable trades.

Client relationship

The records required under paragraphs 11.5(2)(k) and (m) should document information about a registered firm's relationship with its client and relationships that any representatives have with that client.

These records include:

- communication between the firm and its clients, such as disclosure provided to clients and agreements between the registrant and its clients

- account opening information

- change of status information provided by the client

- disclosure and other relationship information provided by the firm

- margin account agreements

- communications regarding a complaint made by the client

- actions taken by the firm regarding a complaint
- communications that do not relate to a particular transaction, and
- conflicts records

Each record required under paragraph 11.5(2)(k) should clearly indicate the name of the accountholder and the account the record refers to. A record should include information only about the accounts of the same accountholder or group. For example, registrants should have separate records for an individual's personal accounts and for accounts of a legal entity that the individual owns or jointly holds with another party.

Where applicable, the financial details should note whether the information is for an individual or a family. This includes spousal income and net worth. The financial details for accounts of a legal entity should note whether the information refers to the entity or to the owner(s) of the entity.

If the registered firm permits clients to complete new account forms themselves, the forms should use language that is clear and avoids terminology that may be unfamiliar to unsophisticated clients.

Conflicts of interest

General principles

The records required under paragraphs 11.5(2)(p), (q) and (r) are records that registered firms must maintain to demonstrate compliance with their obligations in Part 13, Division 2. Specifically, paragraph 11.5(2)(p) requires registered firms to demonstrate how they have complied with the obligations to identify, address, and disclose material conflicts of interest.

The level of detail expected in records relating to conflicts

We expect firms to use their professional judgement when deciding how much detail to provide when maintaining records that demonstrate compliance with conflicts obligations. As the materiality of a conflict increases, there should be greater detail in the records maintained to demonstrate compliance. For example, we expect to see more detailed records for material conflicts related to sales practices, compensation arrangements, incentive practices, referral arrangements, the use of proprietary products and services, and product-shelf development conflicts.

If the materiality of a particular conflict of interest is relatively low, the registered firm may record that conflict in a more general way, such as by category or type of conflict as opposed to recording each instance of such a conflict and how the firm has addressed this conflict in each instance. For example, subject to compliance with applicable securities legislation or SRO rules, if a firm has established a code of conduct or policy that limits the receipt of gifts or promotional items from third parties then, depending on the circumstances, it may be sufficient for that firm to record the details of its policy and the related procedures and controls, and how violations of that policy are addressed.

Referral arrangements

(a) Documenting referral arrangements

Registered firms must document all referral arrangements between the registered firm, its registered individuals, and another person, as well as all fees paid or received by the registered firm or its registered individuals pursuant to such arrangements.

We expect that the registered firm will also document its due diligence analysis of the parties to which it is referring clients in compliance with section 13.9.

(b) Monitoring and supervising all referral arrangements

As noted under Part 13, Division 3, and as part of a registered firm's responsibility under subsection 11.1(1), registered firms have a responsibility to monitor and supervise all of their referral arrangements to ensure that they comply with the requirements of Regulation 31-103 and other applicable securities laws and continue to comply for so long as the arrangement remains in place. This includes monitoring and supervising on an ongoing basis their own conduct and that of their registered representatives in connection with these referral arrangements, as well as taking reasonable steps to satisfy themselves that the other parties to the referral arrangements (from which they are receiving referral fees or to which they are paying referral fees) are also complying with their obligations under the referral arrangements. We expect this to include maintaining any necessary registrations and, where parties are not registered, complying with any limitations on their activities in connection with the referral arrangements. Registered firms must document their oversight of all such referral arrangements.

(c) Demonstrating how material conflicts of interest resulting from referral arrangements are addressed

As part of its obligations under paragraph 11.5(2)(p), the registered firm must demonstrate how it has addressed or plans to address, conflicts related to referral arrangements in the client's best interest, and why the registered firm has determined that the specific referral is in the client's best interest. Paragraph 13.8(b) also requires firms to record all referral fees. Our expectations for records of referral fees are discussed in the guidance below relating to section 13.8.

Sales practices, compensation arrangements and incentive practices

As part of a firm's obligations under paragraph 11.5(2)(q) we expect registered firms to document, where applicable:

- sales practices set by the firm, including sales targets and revenue quotas to which its registered individuals are subject, and sales targets and revenue quotas for the sale of proprietary products

- compensation arrangements set by the firm including how the firm compensates its registered individuals

- other compensation arrangements that the registered firm or its registered individuals benefit from, including how issuers, related or connected parties to those issuers, related or connected parties to the registered firm, or investment fund managers compensate the registered firm, including through embedded commissions

- incentive practices set by the firm, including monetary and non-monetary benefits provided by the registered firm to its registered individuals as incentives

- other incentive practices that the registered firm or its registered individuals benefit from, including monetary and non-monetary benefits that the registered firm or its registered individuals receive from issuers, related or connected parties to those issuers, related or connected parties to the registered firm, or investment fund managers. This includes:

    - a list of issuers, or related or connected parties to those issuers, that have provided incentives such as shelf fees, due diligence fees, shares, options, warrants, performance fees, or production bonuses, and

    - how the registered firm tracks and oversees such benefits.

Misleading business titles and designations

Registered firms are required to maintain records to demonstrate compliance with section 13.18, which prohibits registrants from using titles or designations that could reasonably be expected to deceive or mislead existing and prospective clients. We expect the registered firm to have policies and procedures relating to the use of titles and designations designed to avoid confusion or misleading existing and prospective clients, including more vulnerable and less sophisticated investors.

These policies and procedures should include guidance on what titles and designations may be used and describe any restrictions or prohibitions related to them, including the requirement for pre-approval of registered individuals' use of titles and designations. The registered firm should clearly communicate these policies and procedures to their registered individuals and enforce them accordingly.

Internal controls

The records required under paragraphs 11.5(2)(d), (e), (f), (j), and (o), (p) and (q) are records firms must maintain to support the internal controls and supervision components of their compliance system.

11.6. Form, accessibility and retention of records

Third party access to records

Paragraph 11.6(1)(b) requires registered firms to keep their records in a safe location. This includes ensuring that no one has unauthorized access to information, particularly confidential client information. Registered firms should be particularly vigilant if they maintain books and records in a location that may be accessible by a third party. In this case, the firm should have a confidentiality agreement with the third party.

Division 3 Certain business transactions

11.8. Tied selling

Section 11.8 prohibits an individual or firm from engaging in abusive sales practices such as selling a security on the condition that the client purchase another product or service from the registrant or one of its affiliates. These types of practices are known as “tied selling”. In our view, this section would be contravened if, for example, a financial institution agreed to lend money to a client only if the client acquired securities of mutual funds sponsored by the financial institution.

However, section 11.8 is not intended to prohibit relationship pricing or other beneficial selling arrangements similar to relationship pricing. Relationship pricing refers to the practice of industry participants offering financial incentives or advantages to certain clients.

11.9. Registrant acquiring a registered firm’s securities or assets

Notice requirement

Under section 11.9, registrants must give the regulator notice if they propose to acquire an ownership interest in voting securities (or securities convertible into voting securities) or assets of another registered firm or the parent of another registered firm. This notice must be delivered to the principal regulator of the registrant proposing to make the acquisition and to the principal regulator of the registered firm they propose to acquire, if that firm is registered in Canada. If the principal regulator of both firms is the same, only one notice is required.

Registrants acquiring securities or assets of another registered firm for a client in nominee name do not need to provide notice under section 11.9. For purposes of this section, a substantial part of the assets of the registered firm would include a registered firm’s book of business, a business line or a division of the firm, among other things. This notice gives the regulator an opportunity to consider ownership issues that may affect a firm’s fitness for registration.

Filing of the notice with the principal regulator

It is intended that the notice filed with the principal regulator(s) will be shared with other regulators with an interest in the proposed acquisition. Therefore, although only the principal regulator(s) will receive a notice, other jurisdictions may object to the proposed acquisition under subsections 11.9(4) and 11.9(5). The registrant will have an opportunity to be heard in any jurisdiction that has objected to the proposed acquisition. It is our intent, however, to coordinate the review of these notices and any decisions to object to these proposed acquisitions.

Subsection 11.9(4) does not apply in British Columbia. However, the regulator in British Columbia may exercise discretion under section 36 or 161 of the BC *Securities Act* (R.S.B.C. 1996, c. 418) (BCSA) to impose conditions, restrictions or requirements on the registrant's registration or to suspend or revoke the registration if it decides that an acquisition would affect the registrant's fitness for registration or be prejudicial to the public interest. In these circumstances, the registrant would be entitled to an opportunity to be heard, except if the regulator issues a temporary order under section 161 of the BCSA.

Content of the notice

When preparing the notice under section 11.9, registrants should consider including the following information to help the regulator assess the proposed transaction:

- the proposed closing date for the transaction

- the business reasons for the transaction

- the corporate structure, both before and after the closing of the proposed transaction, including all affiliated companies and subsidiaries of the acquirer and any registered firm involved in the proposed transaction whether interests in a company, partnership or trust are held directly or through a holding company, trust or other entity

- information on the operations and business plans of the acquirer and any registered firm involved in the proposed transaction, including any changes to Item 3.1 of Form 33-109F6 *Firm Registration* such as primary business activities, target market, and the products and services provided to clients of any registered firm involved in the proposed transaction

- any significant changes to the business operations of any registered firm involved in the proposed transaction, including changes to the CCO, the UDP, key management, directors, officers, permitted individuals or registered individuals

- whether the registered firms involved in the proposed transaction have written policies and procedures to address conflicts of interest that may arise following the transaction and information on how such conflicts of interest have been or will be addressed.

- whether the registered firms involved in the proposed transaction have adequate resources to ensure compliance with all applicable conditions of registration

- a confirmation that any registered firm involved in the proposed transaction will comply with section 4.1 following the transaction

- details of any client communications in connection with the transaction that have been made or are planned or an explanation of why no communications to clients are anticipated

- whether a press release will be issued in relation to the proposed transaction

11.10. Registered firm whose securities are acquired

Notice requirement

Under section 11.10, registered firms must notify their principal regulator if they know or have reason to believe that any individual or firm is about to acquire 10% or more of the voting securities (or securities convertible into voting securities) of the firm or the firm's parent. This notice gives the regulator an opportunity to consider ownership issues that may affect a firm's fitness for registration. We expect this notice to be sent as soon as the registered firm knows or has reason to believe such an acquisition is going to take place.

Filing of the notice with the principal regulator

It is intended that the notice filed with the principal regulator(s) will be shared with other regulators with an interest in the proposed acquisition. Therefore, although only the principal regulator(s) will receive a notice, other jurisdictions may object to the proposed acquisition under subsections 11.10(5) and 11.10(6). The registered firm will have an opportunity to be heard in any jurisdiction that has objected to the proposed acquisition. It is our intent, however, to coordinate the review of these notices and any decisions to object to these proposed acquisitions.

Application for registration

We expect any individual or firm that acquires assets of a registered firm and is not already a registrant will have to apply for registration. We will assess their fitness for registration when they apply.

Subsection 11.10(5) does not apply in British Columbia. However, the regulator in British Columbia may exercise discretion under section 36 or 161 of the BCSA to impose conditions, restrictions or requirements on the registrant's registration or to suspend or revoke the registration if it decides that an acquisition would affect the registrant's fitness for registration or be prejudicial to the public interest. In these circumstances, the registrant would be entitled to an opportunity to be heard, except if the regulator issues a temporary order under section 161 of the BCSA.

Content of the notice

Refer to the guidance in section 11.9.

PART 12 FINANCIAL CONDITION

Division 1 Working capital

12.1. Capital requirements

Frequency of working capital calculations

Section 12.1 requires registered firms to notify the regulator as soon as possible if their excess working capital is less than zero.

Registered firms should know their working capital position at all times. This may require a firm to calculate its working capital every day. The frequency of working capital calculations depends on many factors, including the size of the firm, the nature of its business and the stability of the components of its working capital. For example, it may be sufficient for a sole proprietor firm with a dedicated and stable source of working capital to do the calculation on a monthly basis.

Form 31-103F1 *Calculation of excess working capital*

Application of *Regulation 52-107 Acceptable Accounting Principles and Auditing Standards*

Form 31-103F1 *Calculation of Excess Working Capital* (Form 31-103F1) must be prepared using the accounting principles used to prepare financial statements in accordance with *Regulation 52-107 respecting Acceptable Accounting Principles and Auditing Standards* (chapter V-1.1, r. 25) (Regulation 52-107). Refer to section 12.10 of this Policy Statement and *Policy Statement to Regulation 52-107 respecting Acceptable Accounting Principles and Auditing Standards* (Decision 2010-PDG-0217, 2010-11-22) (Policy Statement 52-107) for further guidance on audited financial statements.

IIROC and MFDA member firms that are also registered in another category

IIROC and MFDA member firms that are also registered in a category that does not require SRO membership must still comply with the financial filing requirements in Part 12, even if they are relying on the exemptions in sections 9.3 and 9.4. Provided certain conditions are met, SRO members that are registered in other categories may be permitted to calculate their working capital in accordance with the SRO forms and file the SRO forms instead of Form 31-103F1.

For example, if the SRO firm is also an investment fund manager, it will need to report any net asset value (NAV) adjustments quarterly in order to comply with the investment fund manager requirements, notwithstanding that its SRO has no such requirements. However, they may be permitted to calculate their working capital in accordance with the SRO forms and file the SRO forms instead of Form 31-103F1. See sections 12.1, 12.12 and 12.14 for the requirements on delivery of working capital calculations for SRO members that are registered in multiple categories.

Working capital requirements are not cumulative

The working capital requirements for registered firms set out in section 12.1 are not cumulative. If a firm is registered in more than one category, it must meet the highest capital requirement of its categories of registration, except for those investment fund managers who are also registered as portfolio managers and meet the requirements of the exemption in section 8.6. These investment fund managers need only meet the lower capital requirement for portfolio managers.

If a registrant becomes insolvent or declares bankruptcy

The regulator will review the circumstances of a registrant's insolvency or bankruptcy on a case-by-case basis. If the regulator has concerns, it may impose terms and conditions on the registrant's registration, such as close supervision and delivering progress reports to the regulator, or it may suspend the registrant's registration.

12.2. Subordination agreement

Non-current related party debt must be deducted from a firm's working capital on Form 31-103F1, unless the firm and the lender have executed a subordination agreement in the form set out in Appendix B of Regulation 31-103 and delivered a copy of that agreement to the regulator. A portion of the non-current loan becoming current would not impact the original subordination agreement; the firm would have to notify the regulator if the firm repays the loan or any part of the non-current portion of the loan. However, the current portion of the originally-intended non-current subordinated loan would have to be included in Line 4 of Form 31-103F1, and could not be included in Line 5 of Form 31-103F1. This may not be the total amount of the original loan as set out in the subordination agreement, and as such the amount in the subordination agreement would not agree to Line 5 of Form 31-103F1.

Related party debt due on demand or repayable by the firm at any time, including pursuant to a revolving line of credit, is an example of a current liability. These types of liabilities are not eligible to be subordinated for the purposes of calculating excess working capital. The amount of current related party debt must be included in line 4 – *Current liabilities* of Form 31-103F1.

Firms must deliver subordination agreements to the regulator on the earlier of 10 days after the execution of the agreement or the date on which the firm excludes the amount of the related party debt from its excess working capital calculation. A firm may not exclude the amount until the subordination agreement is executed and delivered to the regulator.

The firm's obligations under section 12.2 to notify the regulator 10 days before it repays the loan or terminates the subordination agreement apply regardless of the terms of any loan agreement. Firms should ensure the terms of their loan agreements do not conflict with their regulatory requirements.

If a subordinated related party debt is being increased and the incremental increase is to be subordinated, the subordination agreement submitted to the regulator should only report the incremental increase. Firms should not report the full balance of the related party debt, as noted on the statement of financial position, on the new subordination agreement unless the previous subordination agreement is terminated and notification of this termination is made in accordance with section 12.2.

In conjunction with the submission of a new subordination agreement, the regulator may request that the firm provide a schedule detailing the total outstanding subordinated debt.

The regulator may request that additional documentation be provided in conjunction with the firm's notice of repayment of a subordinated debt in order to assess whether the firm will have sufficient excess working capital following the repayment. This may include updated interim financial information and a completed Form 31-103F1.

At the time the firm submits a notice of repayment, the firm should provide an updated schedule to the regulator, detailing the total outstanding subordinated debt following the repayment.

Division 2 Insurance

Insurance coverage limits

Registrants must maintain bonding or insurance that provides for a "double aggregate limit" or a "full reinstatement of coverage" (also known as "no aggregate limit"). The insurance provisions state that the registered firm must "maintain" bonding or insurance in the amounts specified. We do not expect that the calculation would differ materially from day to day. If there is a material change in a firm's circumstances, it should consider the potential impact on its ability to meet its insurance requirements.

Most insurers offer aggregate limit policies that contain limits based on a single loss and on the number or value of losses that occur during the coverage period.

Double aggregate limit policies have a specified limit for each claim. The total amount that may be claimed during the coverage period is twice that limit. For example, if an adviser maintains a financial institution bond of $50,000 for each clause with a double aggregate limit, the adviser's coverage is $50,000 for any one claim and $100,000 for all claims during the coverage period.

Full reinstatement of coverage policies and no aggregate limit policies have a specified limit for each claim but no limit on the number of claims or losses during the coverage period. For example, if an adviser maintains a financial institution bond of $50,000 for each clause with a full reinstatement of coverage provision, the adviser's maximum coverage is $50,000 for any one claim, but there is no limit on the total amount that can be claimed under the bond during the coverage period.

Insurance requirements are not cumulative

Insurance requirements are not cumulative. For example, a firm registered in the categories of portfolio manager and investment fund manager need only maintain insurance coverage for the higher of the amounts required for each registration category. Despite being registered as both a portfolio manager and an investment fund manager, when calculating the investment fund manager insurance requirement under subsection 12.5(2), an investment fund manager should only include the total assets under management of its own investment funds. It is only with respect to its own funds that the registrant is acting as an investment fund manager.

12.4. Insurance – adviser

The insurance requirements for advisers depend in part on whether the adviser holds or has access to client assets.

An adviser will be considered to hold or have access to client assets if they do any of the following:

- hold client securities or cash for any period
- accept funds from clients, for example, a cheque made payable to the registrant
- accept client money from a custodian, for example, client money that is deposited in the registrant's bank or trust accounts before the registrant issues a cheque to the client
- have the ability to gain access to client assets
- have, in any capacity, legal ownership of, or access to, client funds or securities
- have the authority, such as under a power of attorney, to withdraw funds or securities from client accounts
- have authority to debit client accounts to pay bills other than investment management fees
- act as a trustee for clients

- act as fund manager or general partner for investment funds, or

- use a custodian that is not functionally independent of the adviser and that, if used, allows the registered firm to access client assets

A registered firm will generally be considered to have access to client assets through the use of a custodian that is not functionally independent of the firm when any of the following apply:

- the registered firm and the custodian share the same mind and management such that the registered firm and the custodian would not reasonably be considered to be operating independently

- the custodial activities are performed by personnel that are not separate from, or are unable to act independently from, personnel of the registered firm

- there is a lack of systems and controls to ensure the functional independence of personnel performing the custodial function

12.6. Global bonding or insurance

Registered firms may be covered under a global insurance policy. Under this type of policy, the firm is insured under a parent company's policy that covers the parent and its subsidiaries or affiliates. Firms should ensure that the claims of other entities covered under a global insurance policy do not affect the limits or coverage applicable to the firm.

Division 4 Financial reporting

12.10. Annual financial statements

12.11. Interim financial information

Accounting Principles

Registrants are required to deliver annual financial statements and interim financial information that comply with Regulation 52-107. Depending on the financial year, a registrant will look to different parts of Regulation 52-107 to determine which accounting principles and auditing standards apply:

- Part 3 of Regulation 52-107 applies for financial years beginning on or after January 1, 2011;

- Part 4 of Regulation 52-107 applies to financial years beginning before January 1, 2011.

Part 3 of Regulation 52-107 refers to Canadian GAAP applicable to publicly accountable enterprises, which is IFRS as incorporated into the Handbook. Under

Part 3 of Regulation 52-107, annual financial statements and interim financial information delivered by a registrant must be prepared in accordance with Canadian GAAP applicable to publicly accountable enterprises except that any investments in subsidiaries, jointly controlled entities and associates must be accounted for as specified for separate financial statements in International Accounting Standard 27 Consolidated and Separate Financial Statements. Separate financial statements are sometimes referred to as non-consolidated financial statements.

Subsection 3.2(3) of Regulation 52-107 requires annual financial statements to include a statement and description about this required financial reporting framework. Section 2.7 of Policy Statement 52-107 provides guidance on subsection 3.2(3). We remind registrants to refer to these provisions in Regulation 52-107 and Policy Statement 52-107 in preparing their annual financial statements and interim financial information.

Part 4 of Regulation 52-107 refers to Canadian GAAP for public enterprises, which is Canadian GAAP as it existed before the mandatory effective date for the adoption of IFRS, included in the Handbook as Part V. Under Part 4 of Regulation 52-107, annual financial statements and interim financial information delivered by a registrant must be prepared in accordance with Canadian GAAP for public enterprises except that the financial statements and interim financial information must be prepared on a non-consolidated basis.

12.14. Delivering financial information – investment fund manager

NAV errors and adjustments

Section 12.14 requires investment fund managers to periodically deliver to the regulator, among other things, a completed Form 31-103F4 *Net Asset Value Adjustments* if any NAV adjustment has been made. A NAV adjustment is necessary when there has been a material error and the NAV per unit does not accurately reflect the actual NAV per unit at the time of computation.

Some examples of the causes of NAV errors are:

- mispricing of a security
- corporate action recorded incorrectly
- incorrect numbers used for issued and outstanding units
- incorrect expenses and income used or accrued
- incorrect foreign exchange rates used in the valuation, and
- human error, such as inputting an incorrect value

We expect investment fund managers to have policies that clearly define what constitutes a material error that requires an adjustment, including threshold levels, and how to correct material errors. If an investment fund manager does not have a threshold in place, it may wish to consider the threshold in IFIC Bulletin Number 22 *Correcting Portfolio NAV Errors* or adopt a more stringent policy.

PART 13 DEALING WITH CLIENTS – INDIVIDUALS AND FIRMS

Division 1 Know your client, know your product and suitability determination

13.2. Know your client

General principles

Registrants act as gatekeepers of the integrity of the capital markets. They should not, by act or omission, facilitate conduct that brings the market into disrepute. As part of their gatekeeper role, registrants are required to establish the identity of, and conduct due diligence on, their clients under the know your client (or KYC) obligation in section 13.2.

KYC information is essential for determining suitability, in order to protect the client, the registrant and the integrity of the capital markets. The KYC obligation requires registrants to take reasonable steps to obtain and periodically update information about their clients. The KYC process is an ongoing one which does not end after the initial KYC analysis is complete.

Establishing the identity and reputation of the client

Clients that are individuals

Registrants must collect information to establish the identity of the clients that are individuals. Registrants must take reasonable steps to confirm the accuracy of the information they collect in order to form a reasonable belief that they know the identity of an individual.

Verifying a client's reputation

Paragraph 13.2(2)(a) requires registrants to make inquiries if they have cause for concern about a client's reputation and to make all reasonable inquiries necessary to resolve the concern. This includes making a reasonable effort to determine, for example, the nature of the client's business or the identity of beneficial owners where the client is a corporation, partnership or trust. See subsection 13.2(3) for additional guidance on identifying clients that are corporations, partnerships or trusts.

Identifying insiders

Under paragraph 13.2(2)(b), a registrant must take reasonable steps to establish whether the client is an insider of a reporting issuer or any other issuer whose securities are publicly traded.

We consider “reasonable steps” to include explaining to the client what an insider is and what it means for securities to be publicly traded.

For purposes of this paragraph, “reporting issuer” has the meaning given to it in securities legislation and “other issuer” means any issuer whose securities are traded in any public market. This includes domestic, foreign, exchange-listed and over-the-counter markets, but does not include issuers whose securities have been distributed through a private placement and are not freely tradeable.

A registrant need not ascertain whether the client is an insider if the only securities traded for the client are mutual fund securities and scholarship plan securities referred to in paragraphs 7.1(2)(b) and (c). However, we encourage firms, when selling highly concentrated pooled funds, to enquire as to whether a client is an insider of the issuer of any securities held by the fund, notwithstanding the exemption provided in subsection 13.2(7). In addition, we remind registrants that they remain subject to the requirement in paragraph 13.2(2)(b) when they trade any other securities than those listed in paragraphs 7.1(2)(b) and (c).

This exemption does not change an insider’s reporting and conduct responsibilities.

Clients that are corporations, partnerships or trusts

Subsection 13.2(3) requires registrants to establish the identity of any person who owns or controls 25% or more of the shares of a client that is a corporation or exercises control over the affairs of a client that is a partnership or trust. We remind registrants that this is in addition to the requirement in paragraph 13.2(2)(a) which requires registrants to make inquiries if they have cause for concern about a client’s reputation. If a registrant has cause for concern about a particular client that is a corporation, partnership or trust, they may need to identify all beneficial owners of such entity.

KYC for conducting a suitability determination

We expect a registrant’s KYC process to result in it having sufficient understanding of its clients to be able to discharge its suitability obligations under section 13.3. See below for a discussion of the extent to which the depth of KYC enquiries may vary depending on the relationship with the client and the securities and services offered by the registrant. We stress that KYC information must not be made to correspond or match with a security, account or portfolio or otherwise be manipulated to lead to a pre-determined outcome.

Registrants should take the opportunity on the initial KYC collection to explain the client's role in keeping KYC information current with the registrant. Some clients may be reluctant to provide relevant KYC information or may delay responding to update requests. The refusal of a client to provide or update all of the information requested by a registrant does not automatically prevent the registrant from servicing the client. A registrant should use professional judgment to consider whether it has collected enough information and whether the information remains sufficiently current.

Meaningful interaction with the client regardless of tools or technology

The process of collecting and updating a client's KYC information must amount to a meaningful interaction between the client and the registrant. Although standardized questionnaires or other tools may be used to facilitate the collection of KYC information and to document that information, the registrant remains responsible for the KYC process. The KYC obligation does not vary depending on the medium through which a registrant interacts with its client to gather the necessary information.

KYC obligations cannot be delegated

Responsibilities arising from the KYC obligation cannot be delegated. A registrant may not rely on a third party, such as a referral agent, for KYC information.

Providing assistance to clients

While some of the information collected can be readily obtained from the client, other elements may require explanation and further discussion with the client. For example, clients may need assistance in articulating their investment needs and objectives. Clients may also provide instructions that are unclear or give inconsistent responses to KYC questions. In these situations, the registrant should make further enquiries of the client. We expect particular care to be exercised by registrants concerning less sophisticated clients and those who may be vulnerable due to considerations such as age or disability. The registrant should not simply assume that the client will understand KYC questions and technical terms used in related discussions or interactions. KYC questions and client communications should be in plain language and supported with explanations of what each question or item relates to and what relevant terms and expressions mean.

Tailoring the KYC process

Although paragraph 13.2(2)(c) sets out a prescribed list of factors that a registrant must take into consideration in order to obtain sufficient KYC information, the depth of the enquiries that a registrant must make with regard to a client will vary. A registrant should tailor its KYC process to reflect its business model, including the nature of its relationships with clients and the securities and services it offers to them. For example, extensive KYC information will be required if the registrant offers an ongoing and fully-customized service or is a portfolio manager with discretionary authority for a client with relatively complex financial circumstances. Less extensive enquiries may be sufficient where a registrant offers model portfolios made up of investment funds to clients with relatively simple financial circumstances. Where the securities being sold to a client are illiquid or highly risky, more information on a client's financial circumstances, including investments held elsewhere, may need to be gathered by the registrant to sufficiently support a suitability determination.

KYC information to support use of prospectus exemptions

Registrants should develop a KYC process that provides for the collection of sufficient information about the client to allow the registrant to determine if the client meets the requirements of a prospectus exemption that is proposed to be relied on.

Client's personal circumstances

Subparagraph 13.2(2)(c)(i) requires the registrant to ensure that it has sufficient information about the client's personal circumstances. For individuals, this includes:

- date of birth
- address and contact information
- civil status or family situation
- number of dependants
- employment status and occupation
- whether someone other than the client is authorized to provide instructions on the account, and
- whether someone other than the client has a financial interest in the account.

For non-individuals, this includes:

- legal name
- head office address and contact information
- type of legal entity, i.e. corporation, trust, or other entity
- form and details regarding the organization of the legal entity, i.e. articles of incorporation, trust deed, or other constating documents
- nature of business
- persons authorized to provide instructions on the account and details of any restrictions on their authority, and

- whether someone other than the client has a financial interest in the account.

Client's financial circumstances

Subparagraph 13.2(2)(c)(ii) requires the registrant to ensure that it has sufficient information on the client's financial circumstances. A client's financial circumstances include, where applicable:

- annual income
- liquidity needs
- financial assets
- net worth, and
- whether the client is using leverage or borrowing to finance the purchase of securities.

\- *Client's liquidity needs*

Liquidity needs are an important aspect of a client's financial circumstances. Registrants should consider ascertaining the extent to which a client wishes or needs to access all or a portion of their investments to meet their ongoing and short-term expenses and financial obligations or fund major planned expenditures. When assessing a client's liquidity needs, a registrant should also consider whether the client has any other means to cover their expenditures, whether the needs are expected or unexpected, and whether, once the need materializes, the money will be withdrawn on a regular basis, such as once a month or once a year.

\- *Client's financial assets and net worth*

Registrants should take reasonable steps to obtain a breakdown of financial assets, including deposits and type of securities such as mutual funds, listed securities and exempt securities. We also expect a registrant to take reasonable steps to determine a client's net worth, which includes all types of assets and liabilities. In some cases, a registrant may need to enquire about investments the client holds outside of the registrant to have a better understanding of a client's financial circumstances to sufficiently support its suitability determination. This information may be particularly important to a registrant's ability to assess whether an investment might lead a client to become over-concentrated in a security or sector.

\- *Leverage or borrowing to finance the purchase of securities*

Understanding a client's financial circumstances includes whether or not a client is using leverage or is borrowing to finance the purchase of securities. When a client uses leverage or borrows money to invest, or borrows against the value of their investments, we expect the registrant to gather additional details regarding the client's ability to meet debt obligations. This will help the registrant with their suitability determination for an investment funded or carried through borrowing.

Client's investment needs and objectives

Subparagraph 13.2(2)(c)(iii) requires the registrant to ensure that it has sufficient information on the client's investment needs and objectives. A client's investment needs may include liquidity, discussed above as an aspect of financial circumstances. A client's investment objectives are the results they want to achieve when investing, such as capital preservation, income generated by invested capital, capital growth or speculation. The questions used by the registrant to ascertain most clients' investment objectives should include an opportunity for the client to express them in non-technical terms that are meaningful to them, such as saving for retirement to maintain a certain lifestyle, increasing wealth by a certain percentage in a specific number of years, investing for purchase of a home, or investing for the post-secondary education of their children.

Understanding a client's overall investment needs and objectives informs a registrant's ability to make suitability determinations for a client. Depending on the nature of the relationship with the client, and the securities and services offered by the registrant, it may be appropriate to set out investment goals for a client's account or portfolio which may be done by developing an investment policy statement. Where investment goals are agreed upon with a client, they should be set out in terms that are specific and measurable. A registrant should consider setting out investment return assumptions that would be required to meet the client's investment needs and objectives. A registrant should also periodically update the client on progress towards any goals set for their account or portfolio.

Client's investment knowledge

Subparagraph 13.2(2)(c)(iv) requires the registrant to ensure that it has sufficient information about the client's investment knowledge. This includes the client's understanding of financial markets, the relative risk and limitations of various types of investments, and how the level of risk taken affects potential returns. This information also plays a role in the registrant's assessment of the client's risk profile under subparagraph 13.2(2)(c)(v).

We expect registrants to inquire about a client's level of awareness and previous experiences with finances and investments. Some registrants may use self-assessment questionnaires for this purpose. Registrants should always make further inquiries if the information provided by a client appears to be inconsistent with their apparent level of investment knowledge. For example, a client may indicate that they have limited investment knowledge and experience, while also indicating a willingness to accept a high level of risk.

Client’s risk profile

Determination of the client’s risk profile

Subparagraph 13.2(2)(c)(v) requires the registrant to have sufficient information about the client’s risk profile. Establishing a client’s risk profile involves understanding the client’s willingness to accept risk, sometimes referred to as risk tolerance, and their ability to endure potential financial loss, sometimes referred to as risk capacity. Risk tolerance and risk capacity are separate considerations that together make up the client’s overall risk profile.

Registrants should have in place a process for assessing a client’s risk profile that includes:

- assessing a client’s willingness to accept risk (risk tolerance) and a client’s ability to endure potential financial loss (risk capacity),

- appropriately interpreting client responses to questions and not attributing inappropriate weight to certain answers, and

- identifying clients that are more suited to placing their money in cash deposits or guaranteed products because they are unwilling or unable to accept the risk of loss of capital.

Assessing a client’s capacity for loss involves the registrant having an understanding of the other factors prescribed in paragraph 13.2(2)(c), particularly the client’s financial circumstances, including liquidity needs, debts, income and assets. Another consideration in determining risk capacity is how much of a client’s total investments an account or a particular securities position represents. Age and life stage can also be important considerations when assessing a client’s capacity to withstand loss. The risk profile for a client should reflect the lower of (a) the client’s willingness to accept risk and (b) the client’s ability to endure potential financial loss.

The process for developing a client’s risk profile should be supportable and reliable. Tools such as questionnaires should be designed to arrive at a meaningful risk profile for the client. The questions and answers that are used to establish the level of risk a client is willing and able to accept should be documented. The questions should be fair, clear and not misleading. A client’s risk profile should not be manipulated to justify recommending higher-risk products, for example, by only having a single category for risk tolerance. Clients should not be influenced by a representative as to the way they respond to questions related to their risk tolerance or risk capacity.

Resolving conflicts between a client’s expectations and risk profile

A client’s expectations for returns in line with their investment needs and objectives may conflict with the level of risk that they are willing and able to accept on their account. A desire to meet unrealistic expectations may lead such clients to ask the registrant to invest in higher-risk products that are unsuitable for them. A detailed discussion of the relationship between risk and return may be necessary to reconcile such conflicts and establish more realistic expectations.

Registrants should not override the risk a client is willing and able to accept on the basis that the client's expectations for returns cannot otherwise be met given the risk profile associated with their KYC responses. The registrant should identify any mismatches between the client's investment needs and objectives, risk tolerance and capacity for loss. The questions at the source of this conflict should be revisited with the client. If a client's goals or return objectives cannot be achieved without taking greater risk than they are able or willing to accept, alternatives should be clearly explained such as saving more, spending less or retiring later.

Where after discussion, it is determined that the client does not have the capacity or tolerance to sustain the potential losses and volatility associated with a higher risk portfolio, the registrant should explain to the client that their need or expectation for a higher return cannot realistically be met, and as a result, the higher risk portfolio is unsuitable. The interaction with the client and end results should be properly documented.

Client's investment time horizon

Subparagraph 13.2(2)(c)(vi) requires the registrant to ascertain the client's investment time horizon. When a client identifies their investment time horizon, the registrant has the responsibility to assess its feasibility and reasonableness relative to the client's liquidity needs, age, investment objectives, risk profile, and other particular circumstances. The length of the client's investment time horizon impacts the types of investments that may be suitable for the client. Investors with a longer investment time horizon may have a greater degree of flexibility when building a portfolio, whereas a short investment time horizon may mean that conservative investments may be the only suitable option.

Client's confirmation

Under section 13.2(3.1), the registrant must take reasonable steps to obtain the client's confirmation of the accuracy of the information collected under subsection 13.2(2), including any significant changes to the client's information. This confirmation may be evidenced by obtaining the client's signature (handwritten, electronic or digital signature) or, alternatively, by maintaining notes in the client file detailing the client's instructions to change the information. It should also be verified by providing written confirmation to the client with details of the instructions for change and providing an opportunity for the client to correct any changes that have been made. A registrant should consider implementing additional controls to evidence any change in client name, address or banking information since these changes may bring about an increased potential for fraud. Controls could include obtaining the client's handwritten, electronic or digital signature.

We expect registrants to record the date on which information is collected under subsection 13.2(2) and updated under subsections 13.2(4) or 13.2(4.1). The books and records required to be maintained under section 11.5 should include maintaining evidence of a client's confirmation of the accuracy of their KYC information.

Keeping KYC information current

Under subsection 13.2(4), registrants are required to make reasonable efforts to keep their clients' KYC information current.

We consider information to be current if it is sufficiently up-to-date to support a suitability determination. At a minimum, registrants must review KYC information collected under subsection 13.2(2)(c) at the frequency set out in subsection 13.2(4.1). If an exempt market dealer is also registered in another dealer registration category, we expect KYC information collected under subsection 13.2(2)(c) to have been reviewed within the last 12 months prior to recommending or trading in an exempt security.

Registrants should review and refresh the KYC information on record for a client after having a meaningful and documented interaction with the client. Registrants are not expected to re-collect all of the client's information, at every review, or in all circumstances of a potential change. There may be situations in which a more fulsome inquiry process (including re-collection of all of a client's KYC information) might be required, depending on how long it has been since all of the client's KYC information has been updated. We expect registrants to be proactive in determining that KYC information is current and, at a minimum, to periodically confirm with clients that the information they have on file remains current.

Significant change to client information

We expect registrants to make reasonable enquiries to determine if there has been a significant change to a client's KYC information. For purposes of section 13.2, a "significant change" to a client's information includes changes to their risk profile, investment time horizon or investment needs and objectives, as well as any other change that would reasonably be expected to have a significant impact on the net worth or income of the client. A significant change to the client's KYC information may result in the information no longer being sufficient to enable the registrant to meet its suitability determination obligations. In those circumstances, registrants should consider restricting activities in the client's account to liquidating trades, transfers or disbursements.

13.2.01. Know your client – trusted contact person

Appendix G sets out how we interpret the requirements under sections 13.2.01 and 13.19 relating to trusted contact persons and temporary holds. It also provides general commentary and guidance surrounding issues of financial exploitation of vulnerable clients, and concerns about clients' mental capacity to make decisions involving financial matters.

13.2.1 Know Your Product

General obligations of registrants

Section 13.2.1 sets out know your product (or KYP) requirements for both firms and individuals. Registrants must have an understanding of the securities that are purchased and sold for, or recommended to, their clients, obtained through a robust KYP process, in order to make the suitability determination that is required by section 13.3.

Making securities available to clients

Registered firms must ensure that KYP obligations are met in respect of securities they make available to clients. A registered firm makes a security available to clients by:

- purchasing or selling it for a client,
- recommending it to a client, or
- placing the security on the firm's shelf or product list, as applicable.

We also take the view that a registered adviser or registered dealer makes a security available to clients by advertising or promoting the security in any medium, including distributing marketing material about the security to a client.

Involvement of multiple registrants

We do not expect a duplication of the KYP review, approval and monitoring processes where multiple registrants are involved with securities, such as investment funds, fund of fund structures, model portfolios, and situations where sub-advisers have been engaged. We expect that registered firms will comply with their KYP obligations with respect to the securities involved at the level they are making those securities available to clients, or, in the case of registered individuals, understand those securities at the level they are purchasing them for or recommending them to clients.

For example, a registrant purchasing securities of an investment fund would discharge its KYP obligations on the fund itself, and it would be the responsibility of the registered adviser responsible for the fund's investments to discharge its KYP obligations on the securities held within the fund's portfolio. Where a portfolio manager has engaged a sub-adviser, it is the sub-adviser that must comply with the specific KYP obligations in respect of the securities it advises on. For registered individuals whose clients invest in model portfolios, the KYP obligation is to take reasonable steps to understand how the model portfolios are composed, their features and risks, and who they would be suitable for, while the adviser(s) responsible for selecting the securities within the model portfolios must discharge their KYP obligations in respect of those securities.

While we do not expect a duplication of the KYP process, registrants must use their professional judgement to ensure they have completed a sufficient assessment, and obtained a sufficient understanding, of the securities they are making available to clients to meet their suitability obligations in section 13.3.

Transfers in and client directed trades

Registrants must take reasonable steps to assess and understand those securities transferred into the firm from another registrant, as well as those that are a result of a client directed trade, within a reasonable time after the transfer or trade. Registered individuals are required to have an understanding of all securities held in a client's account, including those that are held as a result of a transfer in or a client directed trade, in order to make the required periodic suitability determination under section 13.3. We recognize that the depth of the understanding required may vary depending on the nature of the securities, the client's circumstances and investment objectives, and the relationship between the client and the registrant. Firms are not required to approve securities that are transferred in or those that are held as a result of a client directed trade if they do not otherwise make those securities available to clients.

Securities of related and connected issuers

Registrants are not relieved of their KYP obligations in respect of securities of related and connected issuers. Where a firm offers securities of related and connected issuers as well as other securities, we expect that the securities of related and connected issuers will be subject to the same KYP process as those of other issuers. We remind registrants of the requirements in Part 13, Division 2 and their obligation to address conflicts in the best interest of their clients, including those that arise as a result of making securities of related and connected issuers available to clients.

KYP process for firms

To comply with subsection 13.2.1(1), firms should establish a KYP process to ensure that securities that they are considering making available to clients are assessed and approved, and that they are monitored on an ongoing basis for significant changes once they are made available to clients.

The KYP process put in place by the firm may vary depending on the business model of the firm, the types of securities offered, the proficiency of its registered individuals, and the nature of the relationships that the firm and its registered individuals have with clients. For example, in the case of portfolio managers that permit their registered advising representatives to choose from the universe of securities rather than from a shelf or product list, the process put in place by the firm may reflect that the individual advising representatives are responsible for carrying out the assessment of those securities on behalf of the firm. Where a firm maintains a shelf or product list, the firm's process may reflect that it is the responsibility of the firm to carry out the assessment of the securities included on that shelf or product list.

In addition, the extent of the assessment, approval and monitoring processes required may vary depending on the structure, features and risks of securities being considered or made available by the firm. Firms may tailor their processes to the types of securities being considered and the complexity and risks of those securities, and their policies and procedures should set out the different levels of assessment, approval and monitoring for different types of securities, as appropriate. A security by security process will not be required in all circumstances.

For example, a firm's KYP process for less complex and risky types of securities may be less extensive than the process for more complex and risky types of securities, such as those that are novel, not transparent in structure, or involve leverage, options or other derivatives. Securities sold under a prospectus exemption may require a more extensive review and approval process because of the limited disclosure available about them and the less liquid nature of the securities.

KYP requirements for registered individuals

To comply with subsection 13.2.1(2), registered individuals must take reasonable steps to understand securities purchased or sold for, or recommended to, clients, including the structure, features and risks of the securities as well as the initial and ongoing costs of the securities and the impact of those costs. Securities that are more complex or risky may require a more detailed consideration by registered individuals. An understanding of all securities that registered individuals purchase or sell for, or recommend to, clients is necessary in order for registered individuals to make the suitability determination that is required by section 13.3.

We also expect registered individuals to have, based on their proficiency, a general understanding of the types of securities that are available through the registered firm for the registered individuals to purchase or sell for, or recommend to, clients. This is required in order for the registered individuals to meet their obligations under subsection 13.3(1), including the requirement to consider a reasonable range of alternatives as part of making a suitability determination for a client.

We expect that firms will provide their registered individuals with access to the information gathered about securities that have been assessed and approved to be made available to clients, to assist the registered individuals in complying with their KYP obligations. We expect that firms will provide their registered individuals with any necessary training and tools, for example, as well as take any other steps necessary to assist their registered individuals complying with their KYP obligations.

Under subsection 13.2.1(3), registered individuals must not purchase securities for or recommend securities to clients unless those securities have been approved by the firm to be made available to clients. However, the fact that a security is "approved" by the firm is not enough to discharge a registered individual's obligation to take reasonable steps to understand the security being purchased or sold for, or recommended to, a client by the registered individual.

Elements to be considered in the assessment of securities

The following elements should be considered when assessing securities (although, as noted above, the depth of the inquiry on each element may vary depending, for example, on the types of securities and the complexity and risks of those securities):

- the general structure and features of the security, including the overall complexity, transparency and uniqueness of the security, the basis of the security's return and the likelihood of achieving its investment objectives and any expected returns, the time horizon and liquidity restrictions, and the use of leverage;

- the conflicts of interest, if any, inherent in the security, arising for example from the compensation structure, related party issues or other factors, including an assessment of how any conflicts of interest are being addressed by the issuer;

- the parties involved, for example, management of the issuer, portfolio manager, product manufacturer or sponsor, guarantors or significant counterparties;

- the risks of the security;

- the initial and ongoing costs of acquiring, owning and disposing of the security, as well as the impact of those costs on performance, client returns or otherwise, including:

    - fees paid to registrants or other parties, such as commissions, sales charges, trailer fees, management fees, incentive fees, referral fees and redemption fees;

    - embedded costs in the security, such as expenses or bid-ask spreads

Firms are expected to have the appropriate skills and experience to perform the necessary assessment of all securities to be made available to clients.

Additional due diligence may be necessary where there are reasons to question the validity of an issuer's information or where information provided about the securities is not sufficient to permit a meaningful assessment of the securities. An in-depth assessment of a security should take place where any issues are identified during the review process.

Firms should consider whether any restrictions or controls, such as concentration limits or controls on the use of the security in client portfolios, are required for any securities they are considering making available to clients.

Firms should also assess whether any modifications need to be made to their compliance or other systems to support particular securities, and whether additional training or proficiency requirements are necessary in order for their registered individuals to understand the securities and make appropriate suitability determinations.

Where securities to be sold pursuant to exemptions from the prospectus requirements under securities legislation are made available to clients, we expect that firms will consider training their registered individuals on the characteristics and concerns related to exempt securities to ensure that their registered individuals understand those securities and recommend them only in appropriate circumstances.

Approving securities to be made available to clients

Firms are required to establish appropriate approval processes for securities they make available to clients. As noted above, what constitutes an appropriate process for a firm may vary depending on the business model of the firm, the types of securities offered, the proficiency of its registered individuals, and the nature of the relationships that the firm and its registered individuals have with clients.

The approval process may also vary based on the complexity and risks of the securities. Less complex and risky types of securities may only require a high level or less detailed or extensive approval process, while the approval process for more complex securities may be more detailed and extensive and may, for example, involve individuals from a firm's senior management, compliance or risk management areas, as appropriate.

It is up to the firm to determine the appropriate approval process for the types of securities that it makes available to clients and the appropriate controls to have on its registered individuals to ensure that those individuals purchase or recommend only securities that have been approved to be made available to clients.

Any necessary restrictions or controls, compliance or other system modification, or training programs should be put in place before the security is made available to clients.

Monitoring securities made available to clients

A firm's KYP process should include an appropriate process for monitoring for significant changes to securities that have been approved by the firm and continue to be made available to clients. As noted above, what constitutes an appropriate monitoring process may vary depending on the type or complexity of the security, as well as on the business model of the firm, the proficiency of its registered individuals, and the nature of the relationships that the firm and its registered individuals have with clients. It is the responsibility of the firm to determine how and at what frequency the monitoring will take place.

Where there are significant changes to securities that the firm has approved and continues to make available to clients, firms should consider revisiting their approval of or restrictions or controls on the securities as appropriate, and firms and their registered individuals should also consider whether or not the change would require new suitability determinations for clients holding that security where appropriate, as required under subsection 13.3(2)(b).

We remind registrants of the requirement under section 13.3 for periodic suitability determinations in connection with clients' accounts and the securities within those accounts. At these times, we expect that registrants will also consider whether there have been any changes to the securities, or any significant changes to the business environment or market conditions that would affect the risks or other aspects of the securities.

A firm should also consider whether its process in respect of specific securities requires monitoring for significant changes to the business environment or market conditions that would affect the risks or other aspects of the securities.

13.3. Suitability determination

Scope of the suitability determination

General principles

(a) Meaning of "suitability determination"

"Suitability determination" refers to a determination made by a registrant that satisfies the criteria in paragraphs 13.3(1)(a) and (b). The obligation to make a suitability determination is a fundamental obligation owed by registered firms and registered individuals to their clients and is critical to ensuring investor protection. It is a cornerstone of the registration regime and an extension of the duty to deal fairly, honestly and in good faith which registered firms and their registered individuals owe to their clients. However, meeting the criteria for a suitability determination does not imply a guarantee of any particular client outcome.

(b) Meeting prior KYC and KYP obligations

Suitability cannot be determined without having first complied with the KYC and KYP obligations. We expect registrants to gather sufficient information through the KYC process to support a suitability determination. For example, while a client's risk profile is an essential element of the client's KYC information, using the risk rating of a security as the only input in determining its suitability for a client is not in itself sufficient to meet the requirements in subsection 13.3(1). Registrants must also understand all securities that are purchased and sold for, or recommended to, their clients to support a suitability determination.

(c) Meaning of "investment action"

An "investment action" includes opening an account for a client, purchasing, selling, depositing, exchanging or transferring securities for a client's account, and taking any other investment action for a client, or making a recommendation or decision to take any such action. An investment action for a client also includes a recommendation or decision to continue to hold securities, which may be the case, for example, upon a review of a client's account and the securities in the client's account under subsection 13.3(2).

(d) Transfers in and other circumstances

We recognize that in some cases, such as when securities are transferred in from another registrant, it may not be possible for registrants to complete the suitability determination required in advance of opening an account for the client. In these circumstances, we expect the registrant to:

- complete the suitability determination within a reasonable time period after the account is opened, and

- have a process in place to restrict investment actions that can be taken by or on behalf of a client until the suitability determination has been completed (for example, by restricting the accounts to liquidating trades, transfers or disbursement).

Interests of the client come first

(a) General principle

The client's interests, as distinguished from those of the registrant or any other party, are at the core of the obligations under section 13.3. The fact that a recommendation or decision is determined by the registrant, on a reasonable basis, to be suitable for a client pursuant to paragraph 13.3(1)(a) will therefore not be considered to be enough to meet this obligation; the registrant must also determine that the action puts the client's interest first pursuant to paragraph 13.3(1)(b).

(b) Range of possible suitable recommendations

We recognize that there may be several options or courses of action for a registrant to take when recommending securities or services to clients, or when making decisions for clients, that can meet the criteria for a suitability determination. An assessment by a registrant of the specific suitability factors outlined in paragraph 13.3(1)(a) may result in a range of possible suitable recommendations or decisions for the client. However, when making a suitability determination, registrants must put the client's interest first, ahead of their own interests and any other competing considerations, such as a higher level of remuneration or other incentives, and must exercise their professional judgement when opting for one recommendation or decision among other suitable options.

(c) Account type suitability

The suitability determination criteria set out in paragraphs 13.3(1)(a) and (b) apply broadly to all investment actions taken by or recommended to a client by a registrant, including opening an account for a client. When opening an account, we expect registrants to:

- ensure that the type of account recommended, the dealer or adviser compensation option and the nature of the service offered to the client, including the use of investment strategies such as leveraging, are both suitable for the client and put the client's interest first, and

- explain the features and associated costs of different types of accounts that are available to the client at the registered firm, such as, for example, fee-based and commission-based accounts, and recommend the type of account that puts the client's interest first.

The suitability determination of the account type should be made prior to the opening of the account, subject to the exception noted above where securities are transferred in from another registrant and it is not possible to complete the suitability determination of the account type in advance of opening an account for the client. In this case, we expect the registrant to complete the suitability determination of the account type within a reasonable time period after the account is opened.

(d) Periodic reviews of client's account

The suitability determination criteria set out in paragraphs 13.3(1)(a) and (b) also apply to:

- all periodic reviews of a client's account and the securities within the account that a registrant completes under subsection 13.3(2), including decisions or recommendations to continue to hold securities, and

- determinations about how much cash to leave uninvested in a client's account.

(e) Client instructions and liquidating securities

The suitability determination criteria also apply upon receiving a client instruction, as well as to liquidating securities for clients, such as those transferred in from another registrant. Registrants must use their professional judgement when liquidating such securities for clients, and must do so in a way that puts the client's interest first, being mindful of any tax or other consequences to the client.

(f) Circumstances where appropriate accounts, securities and services are not available

If the registrant cannot recommend an account, services or securities to the client that meet the criteria set out in paragraphs 13.3(1)(a) and (b) because these are not available at the firm, the registrant should decline to open an account or provide the securities or the services to the client.

Portfolio approach to suitability

To meet the criteria in paragraph 13.3(1)(b) to put the client's interest first, suitability cannot be determined only on a trade by trade basis, but must be determined on the basis of the client's overall circumstances, given the relationship between the client and the registrant, and the securities and services offered by the registrant. Where a client has multiple investment accounts with the registrant, the registrant must take into consideration whether a recommendation or decision for one account would materially affect the concentration and liquidity of the client's investments across all their accounts held with the firm. As noted below, we expect registrants to determine appropriate concentration thresholds for their clients.

Suitability determination cannot be delegated

Registrants may not delegate their obligations under section 13.3 to an unregistered individual, such as an administrative assistant or a referral agent or a registrant at another firm.

Factors for determining suitability

Specific factors are indicated

Paragraph 13.3(1)(a) indicates specific factors upon which a registrant must base its suitability determination. However, we recognize that, depending on the circumstances, such as the securities and services offered by the firm and the client's particular circumstances, the factors in paragraph 13.3(1)(a) may not be equally applicable to every suitability determination. In these situations, we expect registrants to use their professional judgement to determine the weight to put on each of the specific factors in paragraph 13.3(1)(a) and, overall, to put the client's interest first when making a suitability determination.

Concentration and liquidity in a client's account

Over-concentration in any one security, sector or industry can have a significant impact on the risk and liquidity in a client's account. Depending on the circumstances, such as the securities and services offered by the firm and the client's particular circumstances, we expect registrants to determine appropriate concentration and liquidity thresholds for their clients and to have processes in place to calculate, monitor and manage concentration in a client's account. Registrants should consider a number of factors when determining the appropriate concentration and liquidity, for example, the type of security, market conditions, and redemption or other liquidity restrictions. Generally, the higher the concentration in a particular type of security, sector or industry, the more steps the registrant should take, and appropriately document, to demonstrate that the investment was suitable for the client.

For example, registrants should assess whether the client's investments are over-concentrated in:

- illiquid exempt market securities as compared to more liquid publicly traded securities,

- securities of a single issuer, or group of related issuers, as compared to a broadly-based portfolio of issuers, or

- securities of an issuer, or group of related issuers, that provides exposure to a single industry or asset class, for example, real estate, as compared with a broadly-based portfolio of issuers that provide exposure to diversified industries or asset classes.

Potential and actual impact of costs

Cost as referred to in subparagraph 13.3(1)(a)(iv) is interpreted broadly and includes all direct and indirect costs, fees, commissions and charges, including trailing commissions and any other kind of direct and indirect registrant compensation which may be associated with a client purchasing, selling, holding or exchanging a security, or a registrant making a decision for a client's managed account.

Costs can have a significant impact on a client's return over time. Registrants must assess the relative costs of the options available to clients at the firm when making a suitability determination, as well as the impact of those costs. This includes assessing the impact on the client's overall return of any compensation paid, directly or indirectly, to the registrant, whether by the client, a registered individual's sponsoring firm, or a third party. Registered individuals must put their client's interest first when selecting from multiple suitable options available to the client, and must document the reasonable basis for their suitability determinations.

Consideration of a reasonable range of alternatives

Registrants have an obligation to consider a reasonable range of alternative recommendations or decisions available to the registered individual through the registered firm when making a suitability determination. What constitutes a reasonable range of alternative recommendations or decisions for a client will depend upon the circumstances, including the securities and services offered to the client, the degree of skill and proficiency of the registered individual, and the client's particular circumstances. For example, where a firm offers only a limited range of model portfolios, we would not expect the representative to conduct an in-depth consideration of alternatives if it is clear that only a limited number of options, or a single option, would be suitable for the client.

Reassessing suitability

A suitability determination is required upon the occurrence of an event in subsection 13.3(2), including upon the required periodic review of client's information in accordance with subsections 13.2(4) or (4.1), when the registrant becomes aware of the change. We expect the suitability determination to take place in a timely manner, and the determination of a reasonable time period will depend on the nature of the event itself and the circumstances surrounding the event.

The extent of the requirement to make a new suitability determination in respect of the client's account and the securities within the account is dependent on the particular circumstances, such as what type of event triggered the obligation to reassess suitability, the relationship between the client and the registrant and the services and securities offered, and the types of the securities within the account. For example:

- pre-authorized purchases or systematic withdrawals pursuant to established plans do not require a suitability determination prior to each purchase or withdrawal; however, a suitability determination must be made prior to establishing a systematic plan as well as upon the occurrence of a triggering event;

- when a client's account contains illiquid securities that have no redemption features, such as many of the exempt market securities distributed by exempt market dealers, we recognize that the extent of the reassessment of the suitability determination may be limited due to the illiquid nature of the securities. However, we expect that the registrant will take this fact into account when making future recommendations for the client, including any additional investments;

- when there is a change to a registered individual designated as responsible for a client's account, the extent of the suitability determination required will depend on the circumstances, and may be limited depending on the relationship between the client and the registrant and the securities held by the client. For example, where the client invests in a model portfolio managed by an online adviser, we would not expect a change to the registered individual responsible for the account, if any, to necessarily result in an in-depth reassessment of suitability or any changes to the composition of the client's account;

- we do not expect that registrants will necessarily undertake a reassessment of the client's account type on each periodic review. Rather, we expect that registrants will reflect on the nature of the particular change or event triggering the suitability determination and will use their professional judgement in determining whether the client's account type needs to be reassessed to ensure that it continues to be suitable for the client and puts the client's interest first. For example, it may be appropriate to consider a new account type for a client if there have been significant changes to a client's circumstances, or, if on a periodic review under paragraph 13.3(2)(d), there have been changes to a registrant's offerings such that a new account type may be more appropriate for the client.

Dealing with client instructions (unsolicited orders)

A registrant has no obligation to accept a client order or instruction that does not, in the registrant's view, meet the criteria for a suitability determination. In our view, marking the order as unsolicited is not sufficient. The registrant must take the measures set out in subsection 13.3(2.1) and advise the client in a timely manner against proceeding.

Should the client choose to keep an investment that does not meet or no longer meets the criteria for a suitability determination, it may be appropriate to recommend changes to other investments held by the client at the firm in order to maintain the suitability of the overall account. Any advice given should be documented if the client declines to follow the registrant's recommendation.

Exemptions for certain types of clients

There are exemptions from the requirement to make suitability determinations:

- in subsection 13.3(3), for clients that are registered firms, Canadian financial institutions or Schedule III banks

- in subsection 13.3.1(1) for permitted clients that are not individuals and that have waived, in writing, the suitability determination requirement for all trades, and

- in subsection 13.3.1(2) for permitted clients with non managed accounts that are individuals and that have waived, in writing, the suitability determination requirement for all trades.

SRO rules may also provide conditional exemptions from the obligations under section 13.3, for example, for dealers who offer order execution only services.

Review by the regulator of the suitability determination

Registrants should make their suitability determinations based on the information reasonably available to them at the time. If we review a suitability determination, we will do so based on what a reasonable registrant with a similar business model would have done under the same circumstances. We will not review whether the suitability determination has been met based on events subsequent to the determination by the registrant, nor do we expect that there is only one best decision, recommendation or course of action: there could be several decisions or recommendations that the registrant has a reasonable basis for concluding are equally suitable and that puts the interest of the client first.

Division 2 Conflicts of interest

13.4 Identifying, addressing and disclosing material conflicts of interest - registered firm

13.4.1 Identifying, reporting and addressing material conflicts of interest - registered individual

Responsibility to identify material conflicts of interest

What is a conflict of interest?

A conflict of interest includes any circumstance where:

- the interests of different parties, such as the interests of a client and those of a registrant, are inconsistent or divergent

- a registrant may be influenced to put their interests ahead of their client's interests, or

- monetary or non-monetary benefits available to a registrant, or potential detriments to which a registrant may be subject, may compromise the trust that a reasonable client has in their registrant.

When is a conflict of interest "material"?

Registrants must determine whether a conflict is material. The materiality of a conflict will depend on the circumstances. When determining whether a conflict is material, registrants should consider whether the conflict may be reasonably expected to affect either of the following or both:

- the decisions of the client in the circumstances,

- the recommendations or decisions of the registrant in the circumstances.

Identifying material conflicts of interest

A registered firm cannot properly address a material conflict in the best interest of its clients unless it has adopted robust policies and procedures to, among other things, accurately identify the conflict in a timely way. Pursuant to sections 13.4 and 13.4.1, both a registered firm and its registered individuals must take reasonable steps to identify existing and reasonably foreseeable material conflicts of interest. Reasonable steps to identify such conflicts could include:

- taking proactive measures to anticipate reasonably foreseeable conflicts;

- implementing policies and procedures to identify existing conflicts; and

- assessing the materiality of those conflicts to distinguish between those conflicts that are material and those that are not.

Addressing material conflicts in the best interest of the client

When addressing material conflicts of interest in the best interest of clients, a registered firm and its registered individuals must put the interests of their clients first, ahead of their own interests and any other competing considerations. Registrants must address material conflicts of interest by either avoiding those conflicts or by using controls to mitigate those conflicts sufficiently so that the conflict has been addressed in the client's best interest. We provide guidance below on examples of controls that registrants could consider when addressing various conflicts in the best interest of clients.

To comply with subsections 13.4(2) and 13.4.1(2), registrants must avoid a material conflict of interest if there are no appropriate controls available in the circumstances that would be sufficient to otherwise address the conflict in the best interest of the client. Similarly, if a particular conflict is capable of being addressed by using controls, but the specific controls being used by a registered firm are not sufficiently mitigating the effect of the conflict, the firm must avoid that conflict until it has implemented controls sufficient to address the conflict in the best interest of the client.

Registered firms must avoid a conflict if that is the only reasonable response in the circumstances that is consistent with the obligation to address conflicts in the best interest of clients. Registered firms must avoid such conflicts even if this means foregoing an otherwise attractive business opportunity or type of compensation for the firm or its registered individuals.

Examples of conflicts of interest and controls

The first step for registered firms to address material conflicts in the best interest of clients is to promote a tone from the top, set by the firm's board of directors (or equivalent), UDP and senior management, that emphasizes the importance of integrity when dealing with clients.

Registered firms could consider the following practices when determining how to address material conflicts in the best interest of clients:

- policies and procedures to identify and address material conflicts of interest that include:

  - a broad definition of "conflicts of interest" that enables the registered firm, and each individual acting on its behalf, to understand and identify conflicts of interest that may arise

  - a defined escalation procedure for handling potential conflict situations, for example, an internal requirement that when individuals acting on a registered firm's behalf become aware of an existing or reasonably foreseeable conflict of interest, the individual should promptly report the conflict to the CCO of the firm

- a clear delineation of firm and representatives' responsibilities with respect to identifying and addressing material conflicts of interest

- appropriate resources, independence, and authority to the CCO and other internal control functions

- regular reporting of material conflicts of interest by the CCO to the firm's UDP, executive management, and board of directors (or equivalent), including how the firm is addressing such conflicts in the best interest of clients

- periodic testing of the firm's conflicts management framework, and

- a system for confirming that effective disclosure of material conflicts of interest is provided to clients.

Conflicts arising from proprietary products

It is an inherent conflict of interest for a registered firm to trade in, or recommend, proprietary products and this conflict is, in our experience, almost always a material conflict of interest. Firms that do so must be able to demonstrate that they are addressing this conflict in the best interest of their clients.

Registered firms who trade in, or recommend, proprietary products in addition to non-proprietary products could consider the following examples of controls when determining how to address such conflicts in the best interest of their clients:

- prohibiting monetary or non-monetary benefits at the firm that could bias individual recommendations towards proprietary products over non-proprietary products

- demonstrating that proprietary products are subject to the same know your product processes and selection criteria, as well as ongoing performance and other monitoring, as non-proprietary products

- clearly documenting how proprietary products fit within the firm's business model and strategy, and how they are aligned with client interests

- monitoring the use and level of proprietary products in client portfolios to assist in evaluating whether the conflict is being addressed in the best interests of clients

- making non-proprietary products offered by the firm as easy to access for its registered individuals and its clients as proprietary products offered by the firm

- clearly disclosing to clients the nature of the firm's product and service offerings and the extent to which proprietary products may be included in client portfolios, and

- obtaining independent advice on, or an independent evaluation of, the effectiveness of the firm's policies, procedures, and controls to address this conflict.

Registered firms who only trade in, or recommend, proprietary products could consider the following examples of controls when determining how to address this conflict in the best interest of their clients:

- clearly documenting how the proprietary products fit within the firm's business model and strategy, and how they are aligned with client's interests

- providing clear disclosure to clients about the nature of the firm's product and service offerings and that only proprietary products will be included in client portfolios

- developing client profiles setting out the types of investors for whom the proprietary products may be suitable, including concentration or other limits for such securities where appropriate, and turning away any potential clients who do not fit the profile for that product

- establishing a robust oversight process for compliance with Part 13 Division 1 in respect of proprietary products

- establishing a robust know your product process for the proprietary products, including subsequent performance and other monitoring of the securities, and an ongoing evaluation of the suitability of the securities for client portfolios

- conducting periodic due diligence on comparable non-proprietary products available in the market and evaluating whether the proprietary products are competitive with the alternatives available in the market, and

- obtaining independent advice on, or an independent evaluation of, the effectiveness of the firm's policies, procedures, and controls to address this conflict.

Conflicts arising from third-party compensation

It is an inherent conflict of interest for a registrant to receive third-party compensation. We also consider circumstances where registrants receive greater third-party compensation for the sale or recommendation of certain securities relative to others to be an inherent conflict of interest. In our experience, these are almost always material conflicts of interest.

Registered firms should be able to demonstrate that both product shelf development and client recommendations are based on the quality of the security without influence from any third-party compensation associated with the security. Registered firms could consider the following examples of controls when considering how to address these conflicts in the best interest of their clients:

- confirming that securities which provide lower levels of third-party compensation or no third-party compensation are included in the evaluation process, and that such process is free from bias towards securities that provide third-party compensation or higher third-party compensation. For example, by evaluating securities before the application of third-party compensation, or by ensuring that securities providing third-party compensation or higher third-party compensation are subject to the same know your product processes and selection criteria as other similar securities providing lower levels of third-party compensation or no third-party compensation

- as part of the firm's product shelf development, conducting periodic due diligence on securities on the firm's shelf that provide third-party compensation to determine whether such securities are competitive with comparable alternatives available in the market (including those that do not provide third-party compensation)

- clearly documenting how securities that provide third-party compensation fit within the firm's business model and strategy, and how they are aligned with client interests and the services provided to clients. Registrants should in particular take the following factors into account:

  - the range of ongoing investment and financial services provided to clients

  - the extent of such services, and

  - controls to confirm that the services are provided;

- developing client profiles setting out the types of investors for whom securities that provide third-party compensation may be suitable

- maintaining internal compensation arrangements for registered individuals that do not solely tie the registered individual's compensation, either directly or indirectly, to commission revenue that is based on securities recommended or sold

- monitoring registered individuals' recommendations to determine whether predominance is given to securities that provide third-party compensation or higher third-party compensation, and to assist in evaluating whether the conflict is being addressed in the best interest of clients, and

- imposing consequences on registered individuals for breaches of the firm's conflict of interest policies and procedures that are sufficiently robust to counteract the potential incentives that registered individuals might have to put their own interests ahead of their clients' interests.

Conflicts arising from internal compensation arrangements and incentive practices

It is an inherent conflict of interest for registered firms to create incentives to sell or recommend certain products or services over others. It is also an inherent conflict of interest for registered individuals to receive greater compensation from their sponsoring firm for the sale or recommendation of certain products or services over others. In our experience these are almost always material conflicts of interest.

In our experience, sales and revenue targets almost always create material conflicts of interest between registered individuals and their clients because such targets may cause some registered individuals to put their interests ahead of their clients' interests. Also, as the negative consequences for failing to meet a sales or revenue target become more severe, the risk increases that registered individuals will put their interests ahead of their clients' interests.

Registered firms must be able to demonstrate that they are addressing these conflicts in the best interest of their clients. If a registrant is not controlling these conflicts in the best interest of its clients, the registrant must avoid these conflicts. Registered firms could consider the following examples of controls when considering how to address such conflicts in the best interest of their clients:

- applying consequences for conflicts violations that are proportionate to the potential benefit that could be achieved for reaching the sales or revenue target or the compensation or incentive threshold. For example:

    - prohibiting the registered individual from future participation in the compensation arrangement or incentive practice

    - requiring that the registered individual be compensated in a way that does not vary depending on the amount of revenue that they generate for the firm or the product or service that they recommend

    - requiring that a portion of the benefits or bonus be repaid to the registered firm, and

    - demotion or termination of employment;

- tying a portion of the registered individual's variable compensation to the absence of valid client complaints against the registrant, or to the registered individual's compliance with the registered firm's policies and procedures

- limiting the registered individual's variable compensation to a lower portion of their total compensation

- deferring payment of a portion of the compensation or incentive for a reasonable amount of time, and

- maintaining internal compensation arrangements that do not differ by product or service sold to the client, or by account or client type.

In addition to controlling these conflicts in the best interest of clients, registrants must comply with the suitability determination obligation under section 13.3. If certain products or services available at a firm compensate its registered individuals better than others, in addition to determining that the recommendation is suitable, registered individuals must put their clients' interest first when deciding which product or service to recommend. As a result, the client's interests, not the registrant's interests, must guide the recommendations made by a registrant to its clients. Registrants must not recommend a product or service just because it pays them better than the alternatives. This is also consistent with a registrant's obligation to deal fairly, honestly and in good faith with its clients.

Conflicts of interest at supervisory level

If a registered firm's compliance or supervisory staff's compensation is tied to the sales or revenue generation of the firm overall or the registered individuals that they supervise, there is an inherent conflict of interest that may cause them to put their interests ahead of clients' interests. In our experience, it is almost always a material conflict of interest as compliance and supervisory staff may not be able to properly oversee these registered individuals when compensated in this manner.

In firms where dealing or advising representatives also take on compliance roles, this conflict may be practically unavoidable. In such circumstances, we expect registered firms to address this conflict in the best interest of clients by implementing policies and procedures sufficient to mitigate the risk to clients' interests and to closely monitor for compliance with these policies and procedures.

Conflicts in fee-based accounts

In our experience, there is almost always a material conflict of interest if a client is in a fee-based account and that account holds securities with embedded commissions. In all cases where there is a material conflict of interest, it must be addressed in the best interests of the client.

Registrants should also evaluate on an ongoing basis whether a fee-based compensation arrangement is in the best interest of the client, given the client's circumstances, investment needs and objectives, and the level of account activity. Registrants offering fee-based accounts should have controls in place to confirm that clients are receiving services consistent with the terms of the account or agreement with their clients.

Addressing conflicts between clients

We recognize that there can be competing interests among clients, and that a registrant may have difficulty trying to address these conflicts in the best interest of all their clients simultaneously. Addressing such conflicts in the best interest of clients means that the conflict must be addressed fairly and transparently between the clients. Firms should have internal systems to evaluate and document the balancing of competing client interests.

Conflicts related to referral arrangements

Paid referral arrangements are inherent conflicts of interest which, in our experience, are almost always material conflicts of interest, and must be addressed in the best interest of the client. Before a registrant refers a client, in exchange for a referral fee, to another party, the registrant must determine that making the referral is in the client's best interest. In making that determination, we expect registrants to consider the benefits to the client of making the particular referral over alternatives or at all.

In making a referral, registered firms and individuals must be guided only by the client's interests. We therefore expect that a registrant will not make a client referral to a party solely because of the referral fee that they will receive from that party, or because the amount or duration of the referral fee that they will receive from that party may be greater than the amount or duration of the referral fee that they would receive from a competitor to that party. If a client pays more for the same, or substantially similar, products or services as a result of a referral arrangement, we would not consider the inherent conflict of interest to have been addressed in the best interest of the client. This is also consistent with a registrant's obligation to deal fairly, honestly and in good faith with its clients.

See sections 11.5 and 13.8 of this Policy Statement for guidance on books and records obligations relating to referral arrangements and the specific obligations relating to these arrangements.

Purchasing assets from a client outside the normal course of business

The purchase of an asset from a client outside the normal course of a registrant's business may create a material conflict of interest that we expect registrants to avoid unless the registrant can clearly demonstrate that the purchase is in the client's best interest.

Full control or authority over the financial affairs of a client

Having full control or authority over the financial affairs of a client who is an individual (for example, through a power of attorney), or acting as an executor for a client's estate, is an inherent conflict of interest for a registered individual. In our experience, this is almost always a material conflict of interest. We expect registered firms to have policies and procedures in place to ensure that these conflicts are identified and are either avoided or otherwise addressed in the client's best interest.

Individuals who serve on a board of directors

(a) Board of directors of another registered firm

Under section 4.1, a registered individual must not act as a director of another registered firm that is not an affiliate of the individual's sponsoring firm.

(b) Board of directors of non-registered persons

Section 4.1 does not apply to registered individuals who act as directors of unregistered firms. However, material conflicts of interest can arise when a registered individual serves on a board of directors. Examples include conflicting fiduciary duties owed to the company and to a registered firm or client, possible receipt of inside information and conflicting demands on the representative's time.

Conflicts of interest are further exacerbated when a registered individual acts as a director, officer, shareholder, owner or partner of an issuer whose securities the registered individual also recommends to clients. In such situations the responsibility to the firm and the registered individual to address the conflicts of interest is heightened due to the severity of the risk to the client.

The regulator will take into account the potential conflicts of interest that may arise when an individual serves on a board of directors when assessing that individual's application for registration or continuing fitness for registration.

(c) Board of directors of reporting issuers

A representative of a registrant acting as a director of or adviser to a reporting issuer raises concerns with respect to conflicts of interest, particularly in relation to issues of insider information, trading and timely disclosure. All registrants should be conscious of their responsibilities in these situations and weigh the burden of dealing in an ethical manner with the conflicts of interest against the advantages of acting as a director of a reporting issuer.

Directors of a reporting issuer have an obligation not to reveal any confidential information about the issuer until there is full public disclosure of the information, particularly when the information might have a bearing on the market price or value of the securities of the issuer.

Any director of a reporting issuer who is a partner, director, officer, employee or agent of a registrant should recognize that the director's first responsibility with respect to confidential information is to the reporting issuer. A director should meticulously avoid any disclosure of inside information to partners, directors, officers, employees or agents of the registrant or to its clients.

If a partner, director, officer, employee or agent of a registrant is not a director but is acting in an advisory capacity to a reporting issuer and discussing confidential matters, the same care should be taken as if that person were a director. Should the matter require consultation with other personnel of the registrant, adequate measures should be taken to guard the confidential nature.

Individuals who have activities outside of the sponsoring firm

(a) Firm oversight of outside activity and reportable outside activity

The regulator will take into account and require reporting of certain outside activities of a registered individual when assessing that individual's application for registration or continuing fitness for registration, as well as the firm's fitness for registration. Please see the *Policy Statement to Regulation 33-109 respecting Registration Information* for more information.

Registered firms, on the other hand, are required to have policies and procedures to identify and address material conflicts of interest and risks arising from all outside activities that their registered individuals may participate in. This assessment by registrants should not be limited to only the outside activities reportable by registered firms to regulators. In particular, registered firms and registered individuals must determine whether an outside activity is a conflict of interest and determine whether the conflict of interest is material in the circumstances. Please refer to other areas in section 13.4 of this Policy Statement for more information.

(b) Conflicts and other risks arising from outside activities

Registered individuals' activities outside of their sponsoring firm may impact a registered individual's and a registered firm's ability to deal fairly, honestly and in good faith with their clients and to meet their obligations as a registrant, and may give rise to risks in the following areas:

- Outside activities may create material existing or potential conflicts of interest between a registered individual and the registered individual's clients, for example, because the compensation they receive for these activities, or the nature of the relationship between the individual and the outside entity, may cause some registered individuals to put their interests ahead of their clients' interests.

- Outside activities could interfere with the registered individual's ability to properly carry out the registrable activities. For example, if the outside activity requires the registered individual to work full-time during day-time hours, this could lead to insufficient time to properly service clients or to properly carry out the registrable activities, including remaining current on securities law and product knowledge.

- Outside activities could lead to client confusion, particularly where the outside activity relates to financial services (such as financial and estate planning, tax preparation, insurance, mortgage brokerage). The client may view the outside activity as part of the registered firm's activities. This may occur where the same premises, email address, business cards, mailing address, or telephone numbers are used. The outside business activity could expose the registered firm to complaints and litigation.

- When a registered individual in a position of influence deals with or advises clients or potential clients who may be susceptible to that influence, investor protection concerns arise. For example, the registered individual may use the position of influence to cause another individual to become a client or the other individual may be persuaded to purchase a security based upon their opinion of the registered individual and not upon the merits of the security or the other individual's investment needs and objectives. Such registrants must comply with additional requirements set out in section 13.4.3.

- The outside activity may be prohibited by law or regulation. For example, section 4.1 prohibits a registered individual from acting for another registered firm in certain circumstances and section 11.8 prohibits tied selling.

- Where a registered individual has outside activities, the individual may improperly use information obtained from the registered firm in the outside activity. Clients may have only provided confidential information for the purposes of dealing with the registered individual at the registered firm and not for use in the outside activity. If this information is privileged, confidential or insider information, the registered individual's use of this information in the outside activities may impact the registered firm's ability to comply with securities laws.

- Outside activities may reveal registrable activities being carried on by the registered individual outside of the registered individual's firm or with other unregistered persons. They may also reveal non-compliance with securities laws or otherwise objectionable conduct.

In order to be able to assess the conflicts and other risks, we expect registered firms to establish a reporting mechanism that requires their registered individuals to report their outside activities. Before approving any outside activities, registered firms are required to consider existing or potential material conflicts of interest and other risks that arise from outside activities. If the firm cannot properly address a material conflict of interest in the best interest of the client and manage the risks in accordance with prudent business practices, it should not permit the outside activity.

In addition, registered individuals are required to promptly report to their sponsoring firm any material conflict which arises between a registered individual and the registered individual's client in accordance with subsection 13.4.1(2). The registered individual must avoid carrying out the outside activities if controls are not enough to address the conflict in the best interest of clients and must not engage in the outside activity until the registered firm has given its approval for the outside activity.

(c) Monitoring and supervising individuals' outside activities

A registered firm is responsible for monitoring and supervising their registered individuals. This includes the activities outside of their sponsoring firm that the registered individuals participate in.

Monitoring and supervising registered individuals' outside activities helps registered firms meet their regulatory obligations, including:

- compliance with the requirement to operate an effective compliance system under section 11.1;

- the conflicts of interest provisions set out in section 13.4; and

- the restrictions on clients set out in section 13.4.3.

When the regulator reviews how a registered firm monitors and supervises their registered individuals' outside activities, we expect firms to:

- have appropriate policies and procedures to identify material conflicts of interest arising from outside activities and address these conflicts of interest in the best interest of clients, and that include a broad definition of "outside activities";

- require registered individuals to disclose to their firm, and require the firm to review and approve all outside activities prior to the activities commencing;

- have policies and procedures to determine that outside activities do not:

  - involve activities that are inconsistent with securities legislation, IIROC requirements or MFDA requirements, as applicable;

  - interfere with the registered individual's ability to perform their regulatory obligations and to update the registered individual's knowledge and training to keep pace with new securities, services and developments in the industry that are relevant to the registered individual's business, and

  - interfere with the registered individual's ability to properly service clients.

- provide training or education on outside activities, including the need to report on changes in outside activities and the restrictions on a registered individual who is in a position of influence as to the clients the registered individual can deal with or advise;

- require registered individuals to disclose to any new sponsoring firm, and require that new sponsoring firm to review and approve, all outside activities prior to the registered individual joining the new sponsoring firm;

- assess whether the registered firm has the necessary information and is able to properly supervise and monitor the outside activities;

- maintain records documenting its supervision of its individuals' outside activities and store these records so that they are available for review by regulators;

- take appropriate supervisory actions when the registered firm identifies non-compliance with its policies on outside activities, such as no or late reporting of an outside activity;

- identify existing and reasonably foreseeable material conflicts of interest and take appropriate steps to address such conflicts in the best interest of clients;

- permit only outside activities that do not impair the ability to provide adequate client service, including, where necessary, having an alternate representative available for the client;

- make a determination that the outside activity is consistent with the registrant's duty to deal fairly, honestly and in good faith with its clients;

- implement risk management, including proper separation of the outside activity and the registerable activity;

- assess the exposure of the registered firm to complaints and litigation arising from the outside activities;

- assess whether the registered firm's knowledge of its registered individual's lifestyle is commensurate with its knowledge of the registered individual's activities and stay alert to other indicators of possible fraudulent activity. For example, if information comes to the registered firm's knowledge (including through a client complaint) that a registered individual's lifestyle is not commensurate with the registered individual's compensation by the firm, we would expect the registered firm to make further inquiries to assess the situation.

Failure to fulfil these responsibilities may be taken into consideration in assessing the firm's continued fitness for registration.

Registered firms should consider the following additional practices in relation to the monitoring and supervision of their registered individuals' outside activities:

- using standard forms and/or questionnaires to collect and assess their registered individuals' outside activities;

- having an intake method for registered individuals to disclose these outside activities to the firm;

- providing guidelines that describe what an outside activity is and the types of outside activities that are restricted or prohibited by securities laws or by the registered firm;

- having active involvement of the appropriate staff of the registered firm in the oversight of outside activities;

- performing internet searches or branch reviews to identify non-disclosed outside activities;

- having their registered individuals provide annual certifications for attesting compliance with policies relating to outside activities;

- providing monthly or quarterly reminders to their registered individuals to report changes to their outside activities;

- disclosing outside activities to clients using a standard form that is tailored for each outside activity;

- obtaining acknowledgement from clients that they do not fall within the class of individuals that a registered individual who is in a position of influence may not trade for or advise.

Because the nature of outside activities as well as the individual's registered activities may evolve over time, the registered firm is responsible to monitor and supervise outside activities in such a way that material conflicts are continually addressed in the best interest of clients and the risks are managed in accordance with prudent business practices.

Registered individual's responsibility to report and address material conflicts of interest

Under subsection 13.4.1(2), the registered individual must promptly report to his or her sponsoring firm any material conflict which arises between a registered individual and their client. The registered individual must not proceed with the activity in question until their sponsoring firm has given its consent to proceed. A firm can provide that consent in a number of ways.

For example, if a registered individual's activity is done in accordance with their sponsoring firm's policies and procedures related to that conflict then that may be sufficient consent for the purposes of paragraph 13.4.1(5)(b), unless the firm chooses to require its representatives to obtain express consent before proceeding with the particular activity. However, if the registered firm considers that the conflict must be avoided, the registered individual is prohibited from proceeding with the activity in question. Prior to a firm giving its consent to an individual to proceed with an activity, the firm should put necessary controls in place.

However, the registered firm’s consent does not automatically mean that the registered individual has satisfied their obligation to address the conflict in the best interest of their client. Registered individuals and their sponsoring firms each have a distinct obligation to address material conflicts in the best interest of the client.

Conflicts disclosure

Disclosing conflicts of interest

Under subsections 13.4(4), (5) and (6), a registered firm must provide disclosure about conflicts in all cases where prescribed by securities legislation or SRO rules applicable to it. We stress however that disclosure alone is not sufficient to address a material conflict of interest in the best interest of clients. Not only does disclosure sometimes fail to mitigate the risks related to conflicts of interest, but in some instances disclosure of conflicts may aggravate the potential risks to a client’s interests.

We expect that clients will use disclosure about material conflicts of interest to help inform their decision when evaluating the registrant’s business practices, conflicts management and overall performance on an ongoing basis. As a result, the disclosure that clients receive is critical to their ability to make an informed decision about how to manage and evaluate their relationship with the registrant. Disclosure regarding material conflicts of interest must therefore be fulsome in content as set out in Regulation 31-103, must be prominent, specific and written in plain language, and must be disclosed at the appropriate time in order to be meaningful to the client.

See section 13.10 for guidance on the specific disclosure requirements relating to referral arrangements.

When disclosure is appropriate

Registered firms should ensure that their clients are adequately informed about material conflicts of interest that may affect the products and services provided to them.

Timing of disclosure

If a reasonable client would expect to be informed of a material conflict of interest, a registered firm must disclose that conflict during the account opening process. If a conflict was not identified prior to account opening, that conflict must be disclosed, in a timely manner, after it has been identified. These timing requirements are designed to give clients a reasonable amount of time to assess the conflict before making an investment decision.

If a conflict has been identified and it has not yet been disclosed to clients, we would not consider the disclosure “timely” if that disclosure only occurs after a related trade has been completed. Similarly, if there has been a significant change in respect of conflicts disclosure previously provided to a client, the registered firm must notify the client of that significant change, in compliance with subsection 14.2(4).

Although subsection 13.4(7) does not require registered firms to remind clients of conflicts disclosure that has already been provided to them, registrants should consider their obligation to deal fairly, honestly and in good faith with clients in the case of a transaction that presents a conflict which was disclosed a long time ago.

For example, if the registrant provided disclosure of the conflict of interest to the client with the client's account opening documentation months or years earlier, we expect that a registered representative would also disclose the transaction-related conflict to the client shortly before the transaction or at the time the transaction is recommended. However, there is no requirement in subsection 13.4(7) that such reminders be provided to the client in writing.

When disclosure is not appropriate

Disclosure may not be appropriate if a conflict of interest involves confidential or commercially sensitive information, or the information amounts to "inside information" under insider trading provisions in securities legislation.

In these situations, registered firms will need to assess whether there are other methods to adequately address the conflict of interest. If not, the firm may have to decline to provide the service to avoid the conflict of interest.

Registered firms should also have specific procedures for responding to conflicts of interest that involve inside information and for complying with insider trading provisions.

How to disclose a conflict of interest

Disclosure about a material conflict of interest should not:

- be generic disclosure;
- give partial disclosure that could mislead their clients; or
- obscure the conflicts of interest in overly detailed disclosure or buried in the middle of a large disclosure document.

In order to help make conflicts disclosure more prominent, firms should consider using a stand-alone, and succinct, conflicts disclosure document.

Examples of conflicts of interest disclosure

(a) Proprietary product disclosure

If a registrant is trading in, or recommending, proprietary products, it is an inherent conflict of interest. In our experience, it is almost always a material conflict that a reasonable client would expect to be informed of. The registrant should disclose if they only offer proprietary products or whether they offer a mix of proprietary products and non-proprietary products on their shelf and recommended product list.

With respect to the potential impact of this conflict and the risk it could pose to clients' interests, if the registrant is only offering proprietary products then the registrant should consider making the following disclosure prior to opening an account for the client:

"The suitability determination conducted by the firm and its representatives will not consider the larger market of non-proprietary products or whether those non-proprietary products would be better, worse, or equal in meeting the client's investment needs and objectives.".

The firm must also disclose how they are addressing this conflict in the best interest of their clients.

When providing disclosure about proprietary products, a registered firm may also choose to maintain a list of the related or connected issuers for which it acts as a dealer or adviser. It may make the list available to clients by

- posting the list on its website and keeping it updated

- providing the list to the client at the time of account opening, or

- explaining to the client at the time of account opening how to contact the firm to request a copy of the list free of charge.

The list may include examples of the types of issuers that are related or connected and the nature of the firm's relationship with those issuers. For example, a firm could describe the nature of its relationship with an investment fund within a family of investment funds. This would mean that the firm may not have to update the list when a new fund is added to that fund family.

As noted above, information regarding proprietary product conflicts should be made available to clients before the advice or trade giving rise to the conflict so that clients have a reasonable amount of time to assess it. Registrants should use their professional judgement for the best way and time to inform clients about these conflicts. Previous disclosure may no longer be relevant to, or remembered by, a client, while disclosure of the same conflict more than once in a short time may be unnecessary and confusing.

Firms do not have to disclose to clients their relationship with a related or connected issuer that is a mutual fund managed by an affiliate of the firm if the names of the firm and the fund are similar enough that a reasonable person would conclude they are affiliated.

(b) Relationships with other issuers

Firms should assess whether conflicts of interest may arise in relationships with issuers that do not fall within the definitions of related or connected issuers. Examples include non-corporate issuers such as a trust, partnership or special purpose entity or conduit issuing asset-backed commercial paper. This is especially important if a registered firm or its affiliates are involved in sponsoring, manufacturing, underwriting or distributing these securities.

The registered firm should disclose the relationship with these types of issuers if those relationships give rise to a material conflict of interest.

(c) Compensation conflicts

Prior to entering into a transaction with a client, a registrant must disclose any commissions or other compensation that they will be receiving in respect of the transaction.

If a representative's compensation differs depending on the products or services provided, then this is a material conflict that must be disclosed to clients. With respect to the nature and extent of the conflict, the registrant should disclose a summary of the compensation conflict in plain language. For example, if particular products pay a larger percentage-commission than other products available to the client, the extent of the compensation difference should be explained.

Registrants must explain the potential impact of this conflict and the risk it could pose to clients' interests, including an explanation of the increased risk that the firm's representatives may be influenced to recommend a product that provides them better compensation, even though another product available at the firm may be just as good, or better, at meeting the client's investment needs and objectives. The firm must also disclose how it is addressing this conflict in the best interest of its clients.

13.4.3. Individuals in a position of influence

When considering the approval of a registered individual's outside activity, registered firms are expected to understand the nature of the activity and determine if the activity puts the registered individual in a position of influence. Additional regulatory requirements apply where the activity of a registered individual is a position of influence. These requirements do not apply where the individual is solely a permitted individual (*i.e.*, the individual is not registered).

A registered firm is expected to have appropriate policies and procedures in place

- to identify all registered individuals who are in a position of influence,

- to provide reasonable assurance that the registered individual does not trade or advise in securities or derivatives with clients who are subject to that influence, and

- to report the position of influence as a reportable activity to regulators.

Where a registered firm has assessed that a position is not a position of influence, we expect registered firms to have documented their assessment at the time the assessment is made and have this documentation available to regulators upon request. Additionally, the conflicts of interest requirements set out in section 13.4 and 13.4.1 continue to apply to these activities. Only the requirements in section 13.4.3 would not apply.

Under section 13.4.3, certain specific roles are considered positions of influence. For example, a leader in a religious organization or other similar organization is a person who provides leadership or guidance on the faith in a recognized capacity in the organizational structure of the faith, such as a priest, deacon, rabbi, cantor or imam. It may be a position appointed by the faith's organization or selected by the congregation. It does not include any person who is responsible for only clerical or administrative duties, or any person who is only a member of the congregation. Other roles within the faith's organization that extend beyond clerical and administrative duties should be assessed on a case-by-case basis as to whether they are positions of influence. If a registered individual is known to the client or potential client through the registered individual's role as a religious authority figure, it could influence the client's perceptions of the risks of the security or investment strategy, or of the duty of care owed by the registered individual.

An assessment of other positions is required. Registered firms could consider the following non-exhaustive factors to determine whether the outside activity puts the registered individual in a position of influence:

- the degree of influence that the registered individual has through that position due to the functions of the position, the prestige of the position or the training or specialized knowledge required for the position;

- the degree to which a person may be confused as to whether the registered individual is acting in the capacity as a registrant or in another capacity; and

- the degree of susceptibility another person has to the registered individual in that position due to the other person's reliance on or perception of the registered individual's specialized knowledge, expertise, or trustworthiness associated with the role.

If both the degree of influence by the registered individual in the position of influence and the confusion or susceptibility of a person subject to that influence are considered significant, a registered firm is expected to consider the outside activity to be a position of influence.

The determination of whether the registered individual is in a position of influence will be based on the specific facts and will be determined in light of all relevant considerations and the surrounding circumstances. A position that would not normally be a position of influence could be in certain circumstances. We expect firms to be sufficiently aware of their sponsored individual's activities to determine whether a particular activity may rise to the level of a position of influence.

For example, an individual who is a primary care physician would be viewed as being in a position of influence. The physician has specialized medical knowledge and training that patients would not have. Patients see the physician when they are unwell, are reliant on the physician for their health, and may view the physician favourably based on the medical treatment they received, which may make them susceptible to influence. In this scenario, the physician would not be permitted to trade or advise in securities or derivatives with current or ongoing patients of the physician.

However, an assessment of other health care roles is required to determine if it is a position of influence. For example, dentists, optometrists, and technical workers at a medical facility, such as X-ray technicians and data health management coordinators, are not considered to be positions of influence because the degree of susceptibility is not significant.

A caregiver in an assisted living facility may be a position of influence. The caregiver's primary role is to provide care to residents in the assisted living facility, which includes making care decisions. The residents and their family members would be reliant on the caregiver for the quality of care received and would not easily be able to change facilities.

Below are other examples of activities that registered firms may consider as positions of influence due to the influence they carry in their specialized role, coupled with the susceptibility of the persons who receive the services:

- a correctional officer working in the criminal justice system;

- a youth mentor in an organized program;

- social workers who serve a vulnerable client base (e.g., substance abuse programs, mental health care);

- an immigration consultant.

An example of an activity that may not be a position of influence is an instructor for a hobby or recreational course, such as learning to paint or dance, as opposed to a university or college course in finance required for a degree or diploma. While the instructor of a hobby or recreational course may grade students' work, the instructor does not have influence because the course is being taken for recreational or hobby purposes. The students are also not susceptible since the instructor is not grading the students for the purposes of granting a degree or diploma and the students do not rely on the grades for future education and employment opportunities.

Some elected officials, such as school trustees, would also not be considered positions of influence. While they may be influential, generally, they serve a broad base of people and may not use their position unilaterally. Therefore, the degree of susceptibility of their constituents does not rise to the level present in the examples above and in the expressly identified positions set out in paragraphs 13.4.3(2)(a) to (f) of the definition of position of influence.

However, there may be circumstances where an elected official may be in a position of influence. More prominent elected officials might be in a position of influence, as a potential client might be under the impression that specific securities or portfolio advice are being endorsed or approved by a governmental body. In particular, potential clients might view products offered by a prominent elected official to be of lower risk by virtue of the identity of the registered individual. Similarly, the perceived risk of an investment might be influenced if the registered individual is known to the client through the registered individual's role as a caregiver or, as noted above, as a religious authority figure.

A landlord would not be considered to be in a position of influence. While the landlord has power over their tenant in relation to the tenant's ability to continue to rent the accommodation, we would not view the degree of power of the landlord and the degree of susceptibility of the tenant to meet the level of a position of influence.

Individuals who are a liquidator, an executor or trustee of an estate or hold a power of attorney over another person would not, in our view, be in a position of influence. In these cases, the individual has been appointed to act on behalf of an estate or another person. The registered individual's influence is limited only to that estate or person and the individual has a fiduciary duty to act in the best interest of the estate or person. However, there is an inherent conflict of interest for a registrant to have full control or authority over the financial affairs of a client. In our experience, this is almost always a material conflict of interest. SRO rules only permit an individual to act as a liquidator, an executor, trustee, or power of attorney in certain circumstances. Registrants that are members of an SRO must comply with their SRO requirements. Where the individual is not subject to SRO rules, we expect registered firms to have policies and procedures in place such that these conflicts are identified and are either avoided or otherwise addressed in the client's best interest.

13.5. Restrictions on certain managed account transactions

Section 13.5 prohibits a registered adviser from engaging in certain transactions in investment portfolios it manages for clients on a discretionary basis where the relationship may give rise to a conflict of interest or a perceived conflict of interest. The prohibited transactions include trades in securities in which a responsible person or an associate of a responsible person may have an interest or over which they may have influence or control.

Disclosure when responsible person is partner, director or officer of issuer

Paragraph 13.5(2)(a) prohibits a registered adviser from purchasing securities of an issuer in which a responsible person or an associate of a responsible person is a partner, officer or director for a client's managed account. The prohibition applies unless the conflict is disclosed to the client and the client's written consent is obtained prior to the purchase.

If the client is an investment fund, the disclosure should be provided to, and the consent obtained from, each security holder of the investment fund in order for it to be meaningful. This disclosure may be provided in the offering memorandum that is provided to security holders. Like all disclosure about conflicts, it should be prominent, specific, clear and meaningful to the client. Consent may be obtained in the investment management agreement signed by the clients of the adviser that are also security holders of the investment fund.

This approach may not be practical for prospectus qualified mutual funds. Investment fund managers and advisers of these funds should also consider the specific exemption from the prohibition under section 6.2 of *Regulation 81-107 respecting Independent Review Committee for Investment Funds* (chapter V-1.1, r. 43) (Regulation 81-107) for prospectus-qualified investment funds.

Restrictions on trades with certain investment portfolios

Paragraph 13.5(2)(b) prohibits certain trades, including, for example, those between the managed account of a client and the managed account of:

- a spouse of the adviser
- a trust for which a responsible person is the trustee, or
- a corporation in which a responsible person beneficially owns 10% or more of the voting securities

It also prohibits inter-fund trades. An inter-fund trade occurs when the adviser for an investment fund knowingly directs a trade in portfolio securities to another investment fund that it acts for or instructs the dealer to execute the trade with the other investment fund. Investment fund managers and their advisers should also consider the exemption from the prohibition that exists for inter-fund trades by public investment funds under section 6.1 of Regulation 81-107.

Paragraph 13.5(2)(b) is not intended to prohibit a responsible person from purchasing units in the investment fund itself, nor is it intended to prohibit one investment fund from purchasing units of another fund in situations where they have the same adviser.

In instances where an IIROC dealer, who is also an adviser to a managed account, trades between its inventory account and the managed account, the dealer is expected to have policies and procedures that sufficiently mitigate the conflicts of interest inherent in such transactions. Generally, we expect these policies and procedures to ensure that:

- the trades achieve best execution as referenced in *Regulation 23-101 respecting Trading Rules* (chapter V-1.1, r. 6), while ensuring that the trades are consistent with the objectives of the managed account

- reasonable steps are taken to access information, including marketplace quotations or quotes provided by arms-length parties, to ensure that the trade is executed at a fair price

- there is appropriate oversight and a compliance mechanism to monitor this trading activity in order to ensure that it complies with applicable regulatory requirements, including the requirements referred to above.

13.6. Disclosure when recommending related or connected securities

Section 13.6 restricts the ability of a registered firm to recommend a trade in a security of a related or connected issuer. The restrictions apply to recommendations made in any medium of communication. This includes recommendations in newsletters, articles in general circulation, newspapers or magazines, websites, e-mail, Internet chat rooms, bulletin boards, television and radio.

It does not apply to oral recommendations made by registered individuals to their clients. These recommendations are subject to the requirements of Part 13 Division 2.

Division 3 Referral arrangements

Division 3 sets out the requirements for permitted referral arrangements. The purpose of these requirements is to ensure that under any referral arrangements:

- individuals and firms that engage in registerable activities are appropriately registered,

- the roles and responsibilities of the parties to the written agreement are clear, including responsibility for compliance with securities legislation, and

- clients are provided with disclosure about the referral arrangement to help them evaluate the referral arrangement and the extent of any conflicts of interest

As discussed above in Examples of conflicts of interest and controls - Conflicts related to referral arrangements, paid referral arrangements are inherent conflicts of interest which are, in our experience, almost always material conflicts of interest. We expect registered firms to have policies and procedures in place to ensure that these conflicts are identified and are either avoided or otherwise addressed in the best interest of the client.

Registered firms have a responsibility to monitor and supervise all of their referral arrangements to ensure that they comply with the requirements of Regulation 31-103 and other applicable securities laws and continue to comply for so long as the arrangement remains in place. We expect firms to have in place effective policies and procedures for monitoring and supervising all referral arrangements the firm has entered into.

Obligations to clients

A client who is referred to an individual or firm becomes the client of that individual or firm for the purposes of the services provided under the referral arrangement. The registrant receiving a referral must meet all of its obligations as a registrant toward its referred clients, including know your client, know your product, and suitability determinations. The registrant cannot rely on the referring party to discharge any part of these obligations, nor should a registrant knowingly participate in a referral arrangement where the other party is engaged in registerable activity without being appropriately registered or exempt from registration.

13.7. Definitions – referral arrangements

Section 13.7 defines "referral arrangement" in broad terms. Referral arrangement means an arrangement in which a registrant agrees to provide or receive a referral fee. The definition is not limited to referrals for providing investment products, financial services or services requiring registration. It also includes receiving a referral fee for providing a client name and contact information to an individual or firm.

Section 13.7 also defines "referral fee" in board terms. It includes sharing or splitting any commission resulting from the purchase or sale of a security.

We will examine, on a case-by-case basis, whether a given payment is a referral fee or not.

13.8. Permitted referral arrangements

Under section 13.8, parties to a referral arrangement are required to set out the terms of the arrangement in a written agreement. This is intended to ensure that each party's roles and responsibilities are made clear. This includes obligations for registered firms involved in referral arrangements to keep records of referral fees. Payments do not necessarily have to go through a registered firm, but a record of all payments related to a referral arrangement must be kept. This record should include:

- the name(s) of the client(s) referred
- the amount of the fee
- the person paying the fee, and
- who provides the disclosure to referred clients.

We expect referral agreements to include:

- the roles and responsibilities of each party

- limitations on any party that is not a registrant (to ensure that it is not engaging in any activities requiring registration)

- the disclosure to be provided to referred clients, and

- who provides the disclosure to referred clients

Registrants receiving referrals are responsible for:

- carrying out all activity requiring registration that results from the referral arrangement, and

- communicating with referred clients

Registered firms are required to be parties to referral agreements. This ensures that they are aware of these arrangements so they can adequately supervise their representatives and monitor compliance with the agreements. This does not preclude the individual registrant from also being a party to the agreement. Registered individuals cannot enter into referral arrangements independently of their sponsoring firms or without their knowledge.

A party to a referral arrangement may need to be registered depending on the activities that the party carries out. Registrants cannot use a referral arrangement to assign, contract out of or otherwise avoid their regulatory obligations.

Registrants may wish to refer their clients to other registrants for services that they are not authorized to perform under their category of registration. In making referrals, registrants should ensure that the referral does not itself constitute an activity that the registrant is not authorized to engage in under its category of registration.

We would consider the referral of a client by a registrant to a registered dealer to constitute trading in securities by the referring registrant for a business purpose if, in the referral:

- the referring registrant makes any statement to the client about the merits of a specific security or trade,

- the referring registrant makes any recommendation or otherwise represents to the client that a specific trade is suitable for that client or another person, and

- the referring registrant accepts any instructions from the client in respect of trades to be made by the registered dealer.

13.9. Verifying the qualifications of the person receiving the referral

Section 13.9 requires a registrant making a referral to take reasonable steps to satisfy itself that the other party to the referral arrangement is appropriately qualified to perform the contemplated services, and if applicable, is appropriately registered. The registrant is responsible for determining the due diligence steps that are necessary in the particular circumstances. We expect that, at a minimum, they will include

- an assessment of the types of clients that the referred services would be appropriate for, and

- an assessment by the registrant of the qualifications of the referral party, including taking reasonable steps to determine whether the referral party has been the subject of any civil actions, regulatory or professional disciplinary matters conducted under any legislation, or client complaints, relating to his, her or its professional activities..

13.10. Disclosing referral arrangements to clients

The disclosure of information to clients required under section 13.10 is intended to help clients make an informed decision about the referral arrangement and to assess any conflicts of interest. The disclosure must be provided to clients before or at the time the referred services are provided. A registered firm, and any registered individuals who are directly participating in the referral arrangement, should take reasonable steps to ensure that clients understand:

- with which entity they are dealing

- what they can expect that entity to provide to them

- the registrant's key responsibilities to them

- the limitations of the registrant's registration category

- any relevant terms and conditions imposed on the registrant's registration

- the extent of the referrer's financial interest in the referral arrangement, and

- the nature of any existing or reasonably foreseeable conflict of interest that may arise from the referral arrangement

Division 4 Borrowing and lending

13.12. Restriction on borrowing from, or lending to clients

Subsection 13.12(1) is intended to limit the financial exposure of a registered firm. To the extent that products sold to clients are structured in a way that would result in the registrant becoming a lender to the clients, including the registrant extending margin to the client, we would consider the registrant to not be in compliance with subsection 13.12(1).

Subsection 13.12(1) prohibits registrants from lending money, extending credit or providing margin to clients as we consider that this activity creates a conflict of interest which cannot be easily managed.

We note that SROs are exempt from section 13.12 as they have their own rules or prohibitions on lending, extending credit and providing margin to clients. Direct lending to clients (margin) is reserved for IIROC members. The MFDA has its own rules prohibiting margining and, except in specific limited circumstances, lending.

Division 5 Complaints

13.14. Application of this Division

Investment fund managers are only subject to Division 5 if they also operate under a dealer or adviser registration, in which case the requirements in this Division apply in respect of the activities conducted under their dealer or adviser registration.

In Québec, a registered firm is deemed to comply with this Division if it complies with sections 168.1.1 to 168.1.3 of the Québec *Securities Act* (chapter V-1.1), which provides a substantially similar regime for complaint handling.

The guidance in Division 5 of this Policy Statement applies to firms registered in any jurisdiction including Québec.

However, section 168.1.3 of the Québec *Securities Act*, includes requirements with respect to dispute resolution or mediation services that are different than those set out in section 13.16 of Regulation 31-103. In Québec, registrants must inform each complainant, in writing and without delay, that if the complainant is dissatisfied with how the complaint is handled or with the outcome, they may request the registrant to forward a copy of the complaint file to the Autorité des marchés financiers. The registrant must forward a copy of the complaint file to the Autorité des marchés financiers, which will examine the complaint. The Autorité des marchés financiers may act as a mediator if it considers it appropriate to do so and the parties agree.

13.15. Handling complaints

General duty to document and respond to complaints

Section 13.15 requires registered firms to document complaints, and to effectively and fairly respond to them. We are of the view that registered firms should document and respond to all complaints received from a client, a former client or a prospective client who has dealt with the registered firm (complainant).

Firms are reminded that they are required to maintain records which demonstrate compliance with complaint handling requirements under paragraph 11.5(2)(m).

Complaint handling policies

An effective complaint system should deal with all formal and informal complaints or disputes in a timely and fair manner. To achieve the objective of handling complaints fairly, the firm's complaint system should include standards allowing for objective factual investigation and analysis of the matters specific to the complaint.

We take the view that registered firms should take a balanced approach to the gathering of facts that objectively considers the interests of

- the complainant
- the registered representative, and
- the firm

Registered firms should not limit their consideration and handling of complaints to those relating to possible violations of securities legislation.

Complaint monitoring

The firm's complaint handling policy should provide for specific procedures for reporting the complaints to superiors, in order to allow the detection of frequent and repetitive complaints made with respect to the same matter which may, on a cumulative basis, indicate a serious problem. Firms should take appropriate measures to deal with such problems as they arise.

Responding to complaints

Types of complaints

All complaints relating to one of the following matters should be responded to by the firm by providing an initial and substantive response, both in writing and within a reasonable time:

- a trading or advising activity
- a breach of client confidentiality
- theft, fraud, misappropriation or forgery
- misrepresentation
- an undisclosed or prohibited conflict of interest, or

- personal financial dealings with a client

Firms may determine that a complaint relating to matters other than the matters listed above is nevertheless of a sufficiently serious nature to be responded to in the manner described below. This determination should be made, in all cases, by considering if an investor, acting reasonably, would expect a written response to their complaint.

When complaints are not made in writing

We would not expect that complaints relating to matters other than those listed above, when made verbally and when not otherwise considered serious based on an investor's reasonable expectations, would need to be responded to in writing. However, we do expect that verbal complaints be given as much attention as written complaints. If a complaint is made verbally and is not clearly expressed, the firm may request the complainant to put the complaint in writing and we expect firms to offer reasonable assistance to do so.

Firms are entitled to expect the complainant to put unclear verbal issues into written format in order to try to resolve confusion about the nature of the issue. If the verbal complaint is clearly frivolous, we do not expect firms to offer assistance to put the complaint in writing. The firm may nonetheless ask the complainant to put the complaint in writing on his or her own.

Timeline for responding to complaints

Firms should

- promptly send an initial written response to a complainant: we consider that an initial response should be provided to the complainant within 5 business days of receipt of the complaint

- provide a substantive response to all complaints relating to the matters listed under "Types of complaints" above, indicating the firm's decision on the complaint

A firm may also wish to use its initial response to seek clarification or additional information from the client.

Requirements for providing information about the availability of dispute resolution or mediation services paid for by the firm are discussed below.

We encourage firms to resolve complaints relating to the matters listed above within 90 days.

13.16. Dispute resolution service

Section 13.15 requires a registered firm to document and respond to each complaint made to it about any product or service that is offered by the firm or one of its representatives. Section 13.16 provides for recourse to an independent dispute resolution or mediation service at a registered firm's expense for specified complaints where the firm's internal complaint handling process has not produced a timely decision that is satisfactory to the client.

Registered firms may be required to make an independent dispute resolution or mediation service paid for by the firm available to a client in respect of a complaint that

- relates to a trading or advising activity of the firm or its representatives, and

- is raised within 6 years of the date when the client knew or reasonably ought to have known of the act or omission that is a cause of or contributed to the complaint

As soon as possible after a client makes a complaint (for example, when sending its acknowledgment or initial response to the complaint), and again when the firm informs the client of its decision in respect of the complaint, a registered firm must provide a client with information about

- the firm's obligations under section 13.16,

- the steps the client must take for an independent dispute resolution or mediation service to be made available to the client at the firm's expense, and

- the name of the independent service that will be made available to the client (outside of Québec, this will normally be the Ombudsman for Banking Services and Investments (OBSI), as discussed below) and how to contact it

A client may escalate an eligible complaint to the independent dispute resolution or mediation service made available by the registered firm in 2 circumstances:

- If the firm fails to give the client notice of its decision within 90 days of receiving the complaint (telling the client that the firm plans to take more than 90 days to make its decision does not 'stop the clock'). The client is then entitled to escalate the complaint to the independent service immediately or at any later date until the firm has notified the client of its decision.

- If the firm has given the client notice of its decision about the complaint (whether it does so within 90 days or after a longer period) and the client is not satisfied with the decision, the client then has 180 days in which to escalate the complaint to the independent service.

In either instance, the client may escalate the complaint by directly contacting the independent service.

We think that it may sometimes be appropriate for the independent service, the firm and the client involved in a complaint to agree to longer notice periods than the prescribed 90 and 180 day periods as a matter of fairness. We recognize that where a client does not cooperate with reasonable requests for information relating to a complaint, a firm may have difficulty making a timely decision in respect of the complaint. We expect that this would be relevant to any subsequent determination or recommendation made by an independent service about that complaint.

The client must agree that the amount of any recommendation by the independent service for monetary compensation will not exceed $350,000. This limit applies only to the amount that can be recommended. Until it is escalated to the independent service, a complaint made to a registered firm may include a claim for a larger amount.

Except in Québec, a registered firm must take reasonable steps to ensure that the dispute resolution and mediation service that is made available to its clients for these purposes will be OBSI. The reasonable steps we expect a firm to take include maintaining ongoing membership in OBSI as a “Participating Firm” and, with respect to each complaint, participating in the dispute resolution process in a manner consistent with the firm's obligation to deal fairly, honestly and in good faith with its client. This would include entering into consent agreements with clients contemplated under OBSI's procedures.

Since section 13.16 does not apply in respect of a complaint made by a permitted client that is not an individual, we would not expect a firm that only has clients of that kind to maintain membership in OBSI.

A registered firm should not make an alternative independent dispute resolution or mediation service available to a client at the same time as it makes OBSI available. Such a parallel offering would not be consistent with the requirement to take reasonable steps to ensure that OBSI will be the independent service that is made available to the client. Except in Québec, we expect that alternative service providers will only be used for purposes of section 13.16 in exceptional circumstances.

We would regard it as a serious compliance issue if a firm misrepresented OBSI's services or exerted pressure on a client to refuse OBSI's services.

If a client declines to make use of OBSI in respect of a complaint, or if a client abandons a complaint that is under consideration by OBSI, the registered firm is not obligated to provide another service at the firm's expense. A firm is only required to make one dispute resolution or mediation service available at its expense for each complaint.

Nothing in section 13.16 affects a client's right to choose to seek other recourse, including through the courts.

Registrants that are members of an SRO, including those that are registered in Québec, must also comply with their SRO's requirements with respect to the provision of independent dispute resolution or mediation services.

Registrants who do business in other sectors

Some registrants are also registered or licensed to do business in other sectors, such as insurance. These registrants should inform their clients of the complaint mechanisms for each sector in which they do business and how to use them.

Division 6 Registered sub-advisers

13.17. Exemption from certain requirements for registered sub-advisers

Section 13.17 contains an exemption from certain client related requirements for registered sub-advisers. These requirements are not necessary because in a sub-adviser arrangement the sub-adviser's client is another registrant. We remind registrants that these exemptions do not apply if the client is not a registrant. One of the conditions of this exemption is that the other registrant has entered into an agreement with its client that it is responsible for losses that arise out of certain failures by the sub-adviser. We expect that a registrant taking on this liability will conduct appropriate initial and ongoing due diligence on the sub-adviser and before making recommendations or investment decisions based on the sub-adviser's advice, ensure the investment is suitable for the registrant's client.

We also expect that the other registrant and the sub-adviser will maintain records of their transactions and that the other registrant will maintain records of the due diligence conducted on the sub-adviser. See Part 11 of this Policy Statement for more guidance.

Division 7 Misleading communications

13.18 Misleading communications

Misleading business titles and designations

Section 13.18 prohibits registrants in their client-facing relationships from, among other things, using titles or designations that could reasonably be expected to deceive or mislead existing and prospective clients. Certain titles can be confusing to the average investor or imply that a registered individual performs a particular function at a firm or has particular expertise. Similarly, titles can give rise to certain client expectations or help to create an unfounded feeling of trust, reassurance or prestige. Registered firms should keep these considerations in mind before authorizing their registered individuals to use specific titles in their client-facing relationships. Particular scrutiny should be given to the use of titles that convey an expertise in seniors' issues or retirement planning to confirm that any registered individual using such a title is appropriately qualified and competent in that area.

When considering whether a designation is misleading, registered firms should consider whether the designation has:

- a rigorous curriculum and examination process

- experience requirements, and

- been issued by a reputable organization.

Registered firms should recognize that some types of clients, such as seniors, may tend to be vulnerable to misleading designations. If a registered firm permits their registered individuals to use designations of any kind, including those that suggest an expertise in retirement planning, registered firms must have procedures in place to confirm that those designations are not misleading.

The nature of the relationship with clients and the products and services provided

If a registered firm uses advertising that exaggerates the products and services available to clients, this could reasonably be expected to mislead a client as to the products and services to be provided as well as to the nature of the relationship that may exist between the registrant and the client.

If a registered firm primarily or exclusively offers proprietary products, or products manufactured by an affiliate of the firm, and holds itself out as a firm that offers a wide range of products, this could reasonably be expected to mislead a client as to the products to be provided and as to the nature of the relationship.

If a registered firm or its registered individuals hold themselves out as being in a fiduciary-like relationship with their clients but the registrants do not actually conduct themselves to the standard of a fiduciary, this could reasonably be expected to deceive or mislead a client as to the nature of the relationship between themselves and their registrant.

Titles, designations, awards, or recognitions based on sales activity or revenue generation

A registered individual's sales activity or revenue generation are distinct from their proficiency, experience, and qualifications. If a prestigious sounding title, designation, award, or recognition is tied to a registered individual's sales activity or revenue generation, this could reasonably be expected to deceive or mislead a client as to the proficiency, experience, or qualifications of that registered individual.

For example, if membership in a registered firm's "President's Club" is based partly or entirely on a registered individual's sales activity or revenue generation, the registered individual must not use that recognition or award.

Corporate officer titles

A registered individual in a client-facing relationship must not use a corporate officer title, such as president or vice-president, unless their sponsoring firm has duly appointed that registered individual to that corporate office pursuant to the corporate law applicable to their sponsoring firm. The use of a corporate officer title is also still subject to the general rule set out under subsection 13.18(1) and firms must consider whether the use of a corporate officer title would be misleading prior to approving their use.

Division 8 Temporary holds

13.19. Conditions for temporary hold

Appendix G sets out how we interpret the requirements under sections 13.2.01 and 13.19 relating to trusted contact persons and temporary holds. It also provides general commentary and guidance surrounding issues of financial exploitation of vulnerable clients, and concerns about clients' mental capacity to make decisions involving financial matters.

PART 14 HANDLING CLIENT ACCOUNTS – FIRMS

If a client consents, documents required in this Part can be delivered in electronic form. For further guidance, see Policy Statement 11-201.

Division 1 Investment fund managers

Section 14.1 sets out the limited application of Part 14 to investment fund managers. The sections of Part 14 that apply to investment fund managers when performing their investment fund manager activities include section 14.1.1, section 14.55.2, section 14.5.3, section 14.6, section 14.6.1, section 14.6.2, subsection 14.12(5) and section 14.15. An investment fund manager that is also registered as a dealer or adviser (or both) is subject to all relevant sections of Part 14 in respect of that firm's dealer or adviser activities.

Section 14.1.1 requires investment fund managers to provide information that is known to them concerning position cost, deferred sales charges and any other charges deducted from the net asset value of the securities, and trailing commissions to dealers and advisers who have clients that own the investment fund manager's funds. This information must be provided within a reasonable period of time, in order that the dealers and advisers may comply with their client reporting obligations. This is a principles-based requirement. An investment fund manager must work with the dealers and advisers who distribute fund products to determine what information they need from the investment fund manager in order to satisfy their client reporting obligations. The information and arrangements for its delivery may vary, reflecting different operating models and information systems.

Division 2 Disclosure to clients

14.2. Relationship disclosure information

Registrants should ensure that clients understand who they are dealing with. They should carry on all registerable activities in their full legal or registered trade name. Contracts, confirmation and account statements, among other documents, should contain the registrant's full legal name.

Content of relationship disclosure information

Subsection 14.2(1) sets out a general principle that a registered firm must deliver to a client all information that a reasonable investor would consider important about the client's relationship with the registrant. Firms should bear in mind that although it will very often be sufficient to provide a client with the information prescribed in subsection 14.2(2), that is not an exhaustive list and the over-arching general principle will always apply to a client-registrant relationship.

There is no prescribed form for the relationship disclosure information required under section 14.2. A registered firm may provide this information in a single document, or in separate documents, which together give the client the prescribed information.

The relationship disclosure information required to be delivered under subsection 14.2(1) is intended to shape and confirm clients' expectations of the services and products they will receive through the registrant. It is therefore of the greatest importance that it should be should be communicated in a manner consistent with the guidance on client communications under section 1.1 of this Policy Statement. We encourage registrants to avoid the use of technical terms and acronyms when communicating with clients. To satisfy their obligations under section 14.2, registered individuals must spend sufficient time with clients as part of an in-person or telephone meeting, or other method that is consistent with their operations, to adequately explain the information that is delivered to them. We expect a firm to have policies and procedures requiring its registered individuals to demonstrate they have done so. What is considered "sufficient" will depend on the circumstances, including a client's understanding of the delivered documents.

Evidence of compliance with client disclosure requirements at account opening, prior to trades and at other times, can include detailed notes of meetings or discussions with clients, signed client acknowledgements and tape-recorded phone conversations.

Promoting client participation

Registered firms should help their clients understand the registrant-client relationship. They should encourage clients to actively participate in the relationship and provide them with clear, relevant and timely information and communications.

In particular, registered firms should help and encourage clients to:

- **Keep the firm up to date.** Clients should be encouraged to

    - provide full and accurate information to the firm and the registered individuals acting for the firm

    - promptly inform the firm of any change to their information that could result in a change to the types of investments appropriate for them, such as a change to their income, investment objectives, risk profile, investment time horizon or net worth

- **Be informed.** Clients should be
  - helped to understand the potential risks and returns on investments
  - encouraged to carefully review sales literature provided by the firm
  - encouraged to consult professionals, such as a lawyer or an accountant, for legal or tax advice where appropriate
- **Ask questions.** Clients should be encouraged to
  - request information from the firm to resolve concerns about their account, transactions or investments, or their relationship with the firm or a registered individual acting for the firm
- **Stay on top of their investments.** Clients should be encouraged to
  - review all account documentation provided by the firm
  - regularly review portfolio holdings and performance

Account type

Paragraph 14.2(2)(a) requires a firm to provide a description of the nature or type of a client's account. In order that a client will understand their relationship with the firm, a client will need to know how their account will operate. Examples of relevant information include whether

- there is a minimum account size
- it is a fee-based account or commissions will be payable, and
- there are limits on what products or services are made available for accounts of that type.

Further requirements in this section are intended to expand on this foundation.

Disclosure of where and the manner in which client's assets are held or accessed, including the relevant associated risks and benefits

Under paragraphs 14.2(2)(a.1) and (a.2), registered firms must disclose to clients the location where, and the manner in which client assets are held or accessed, including the relevant associated risks and benefits to the client. The risks to a client will vary depending on the type of custodial arrangement that is in place. At a minimum, we would generally expect the disclosure to include the following:

- the way(s) that the registered firm holds client's assets, and the associated risks

- the way(s) that the registered firm has access to the client's assets, and the associated risks

- whether a qualified custodian holds any or all of the client's assets

- if a custodian uses any sub-custodians to hold the client's assets in cases where the registered firm directs or arranges which custodian to use to hold client cash and securities

- if the registered firm uses a custodian that is not independent of the registered firm, and whether the registered firm has access to the client's assets through this relationship

- if a foreign custodian or a foreign dealer holds the client's cash and securities in accordance with subsection 14.5.2(3) or 14.6(2) or section 14.6.1 or 14.6.2, the rationale for using the foreign custodian or dealer and a description of the risks of using that foreign custodian or dealer, including the potential difficulty associated with the client's ability to enforce their legal rights and the potential difficulty that the client may face in respect of repatriating their assets on the bankruptcy or insolvency of the foreign custodian or dealer

Description of products and services

Under paragraph 14.2(2)(b), a firm must provide a general description of the products and services it will offer to a client, including certain prescribed information. The re-sale restrictions referred to in subparagraph 14.2(2)(b)(i) would include, for example, requirements that securities must be redeemed back to their issuer, and liquidity restrictions would include such things as hold periods and the absence of a market place for typical exempt market securities and some proprietary products.

Under paragraph 14.2(2)(b.1), a registered firm must provide a general description of any limits on the selection of the products and services the firm will offer to the client, including whether the firm will primarily or exclusively provide proprietary products to the client; whether there are other restrictions on the selection of products or services. A firm may be restricted to specialized offerings because of its registration category (mutual fund dealers and exempt market dealers, for example), or by terms and conditions placed on its registration, as well as by business decisions to limit what it offers to clients based on account type or other considerations. The products or services that a firm offers to a client might also be restricted as a result of regulatory or business restrictions on a registered representative assigned to their account.

A registrant's duty to deal with the client fairly, honestly and in good faith, and its obligation to make suitability determinations that put the client's interests first, require a firm to tell a client if it does not have products or services that are suitable for them. This determination may depend on the investment goals designated for the client's account. For example, it may make a difference if the account is the primary retirement savings vehicle for a retail investor, or is a secondary account set up by an accredited investor for speculating in exempt market products.

Disclosure of conflicts of interest

Under paragraph 14.2(2)(e), a firm must disclose conflicts of interest. Firms should also take note of subsections 13.4(5), (6) and (7) with respect to conflicts of interest disclosure.

Disclosure of charges and other compensation

Under paragraphs 14.2(2)(f), (g) and (h), registered firms must provide a client with information on the operating and transaction charges they might pay investments and any third-party compensation, such as trailing commissions and issuer commissions including options or warrants, that may be paid to the firm in relation to the client. These requirements have been drafted in broad terms and we expect firms to be careful not to omit or obscure any of the required information.

A registered firm's charges to a client and the compensation it may receive from third parties in respect of the client will vary depending on the type of relationship with the client and the nature of the services and investment products offered. A firm is not expected to provide information on all the types of accounts that it offers and the fees related to these accounts if it is not relevant to the client's situation.

"Operating charge" is defined broadly in section 1.1 and examples include (but are not exclusive to) service charges, administration fees, safekeeping fees, management fees, transfer fees, account closing fees, annual registered plan fees and any other charges associated with maintaining and using an account that are paid to the registrant. For registered firms that charge an all-in fee for the operation of the account, such as a percentage of assets under management, that fee is the operating charge. We do not expect firms with an all-in operating charge to provide a breakdown of the items covered by the fee.

"Transaction charges" is also defined broadly in section 1.1 and examples include (but are not exclusive to) commissions, transaction fees, switch or change fees, performance fees, short-term trading fees, and sales charges or redemption fees that are paid to the registrant. Although we do not consider "foreign exchange spreads" to be a transaction charge, we encourage firms to include a general notification in trade confirmations and reports on charges and other compensation that the firm may have incurred a gain or loss from a foreign exchange transaction as a best practice.

Operating charges and transaction charges include only charges paid to the registered firm by the client. Third-party charges, such as custodian fees that are not paid to the registered firm, are not included in operating charges or transaction charges. Operating and transaction charges include any sales taxes that are paid on the amounts charged to the client. Registrants may wish to inform clients where a charge includes sales tax, or separately disclose the components of the charge. Withholding taxes would not be considered a charge.

Registrants should advise clients with managed accounts whether the registrant will receive third-party compensation and, if so, whether the fee paid by the client to the registrant will be affected by this. For example, the management fee paid by a client on the portion of a managed account related to mutual fund holdings may be lower than the overall fee on the rest of the portfolio.

Description of content and frequency of client reporting

Under paragraph 14.2(2)(i), a registered firm is required to provide a description of the content and frequency of reporting to the client. Reporting to clients includes, as applicable:

- trade confirmations under section 14.12
- account statements under section 14.14
- additional statements under section 14.14.1
- security position cost information under section 14.14.2
- annual report on charges and other compensation under section 14.17
- investment performance reports under section 14.18

Guidance about registered firm's client reporting obligations is provided in Division 5 of this Part.

Suitability determinations and KYC information

Paragraph 14.2(2)(k) requires registered firms to inform their clients of their obligation to make suitability determinations (subject to the exception in subsection 14.2(7)). Paragraph 14.2(2)(l) requires firms to provide clients with a copy of their KYC information. Since firms have an ongoing obligation under subsection 13.2(4.1) to update KYC information, this means that a firm must provide a client with the KYC information it has collected at the time of account opening, and also whenever it has collected updated information. In order that this information will help a client to understand their relationship with the registrant, consistent with the principle in subsection 14.2(1), we expect this disclosure to include a description of the various terms (such as "risk profile" and "investment time horizon") which make up the KYC information, and explain that it will be used in making suitability determinations for the client. The obligation in subsection 14.2(1) is ongoing, so if KYC information is updated, it must also be provided to the client.

Benchmarks

Paragraph 14.2(2)(m) requires registered firms to provide clients with a general explanation of how investment performance benchmarks might be used to assess the performance of a client's investments and any options available to the client to obtain information about benchmarks from the registered firm. Other than this general discussion, there is no requirement for registered firms to provide benchmark information to clients. Nonetheless, we encourage firms to do so as a best practice. Guidance on the provision of benchmarks is set out in this Policy Statement at the end of the discussion of the content of investment performance reports under section 14.19.

Scholarship plan dealers

Paragraph 14.2(2)(n) requires an explanation of the important aspects of the scholarship plan that, if not fulfilled, would cause loss to the client. To be complete, this prescribed disclosure could include any options that would allow the investor to retain notional earnings in the event that they do not maintain prescribed payments under the plan and any fees associated with those options.

Investment impact of costs and restrictions

Paragraph 14.2(2)(o) requires a general explanation of the potential impact of ongoing fees the client may incur and any charges they may pay to the firm, including an explanation of their compounding effect over time. Note that this requirement is with reference to the client's investment returns, rather than returns specific to any one security. A registrant must therefore explain the potential impacts with reference to a client's accounts at the firm.

Order execution trading

Subsections 14.2(7) and (8) provide that only limited relationship disclosure information must be delivered by a dealer whose relationship with a client is limited to executing trades as directed by a registered adviser acting for the client. In a relationship of this kind, each registrant must explain to the client its role and responsibility to the client, and what services and reporting the client can expect of it.

14.2.1. Pre-trade disclosure of charges

For non-managed accounts, section 14.2.1 requires disclosure to a client of charges and fees specific to a transaction prior to the acceptance of a client's instruction. This disclosure is not required to be in writing. Oral disclosure of charges is sufficient for the purposes of disclosing charges at the time of a transaction. In the case of a client who is a frequent trader, if the firm has good reason to believe applicable "standard" charges or fees are well understood, a brief confirmation that the usual charges will apply would be an acceptable alternative to specifying the actual amount of the charges. Specific charges must be reported in writing on the trade confirmation as required in section 14.12.

For a redemption of a security on a deferred sales charge basis, disclosure that a deferred sales charge might be triggered, and the schedule that would apply if it is sold within the time period that a deferred sales charge would be applicable, must be presented. The actual amount of the deferred sales charge, if any, would need to be disclosed once the security is redeemed. For the purposes of disclosing trailing commissions and investment fund management fees, the dealing representative may draw attention to the information in the prospectus or the fund facts document if that document is provided at the point of sale.

With respect to a transaction involving a debt security, pre-trade disclosure should include a discussion of any commission the registered firm will receive on the trade. This discussion should include both the number of basis points that the charge represents as well as the corresponding dollar amount, or a reasonable estimate of the amount if the actual amount of the charges is not known to the firm at the time.

If a client will be investing in securities of a mutual fund or another vehicle that includes any of the following features, a registrant must briefly explain what they are and how they may affect the investment:

- the management fee

- the sales charge options available to the client and an explanation as to how such charges work. Any redemption fees or short-term trading fees that may apply should also so be discusses

- any trailing commission, or other embedded fees

- any options regarding front end loads

- any fees related to the client changing or switching investments ("switch or change fees")

In order to help their clients to understand what trailing commissions and fund management fees are, we encourage registrants to explain them in the simplest terms possible,. We think this should include explaining that trailing commissions are not additional charges paid by the client to the registrant. "Trailing commission" is defined for the purposes of Regulation 31-103 in section 1.1 in broad terms designed to ensure that payments similar to what are generally known as trailing commissions will be subject to similar reporting requirements under this regulation.

Switch or change transactions

Processing a switch or change transaction without client knowledge is contrary to a registrant's duty to act fairly, honestly and in good faith. In our view, compliance with this duty requires that clients are informed, before any switch or change transaction is processed, of charges associated with the transaction, dealers' incentives for such a transaction (including increased trailing commissions), and any tax or other implications of such a transaction. In each case, we expect dealers to explain why a proposed switch or change transaction is appropriate for the client. We consider that providing clients with clear and complete disclosure of the charges at the time of a transaction will help clients to be aware of the implications of proposed transactions and deter registrants from transacting for the purpose of generating commissions. Registrants are also reminded that their obligations in connection with suitability and conflicts of interest apply to such transactions, as well as their obligations under any applicable SRO requirements or guidance.

We expect all changes or switches to a client's investments to be accurately reported in trade confirmations by reporting each of the purchase and sale transactions making up the change or switch, as required in section 14.12, with a description of the associated charges.

14.4. When the firm has a relationship with a financial institution

As part of their duty to clients, registrants who have a relationship with a financial institution should ensure that their clients understand which legal entity they are dealing with. In particular, clients may be confused if more than one financial services firm is carrying on business in the same location. Registrants may differentiate themselves through various methods, including signage and disclosure.

Division 3 Client assets and investment fund assets

14.5.2. Restriction on self-custody and qualified custodian requirement

Section 14.5.2 specifies situations where registered firms must ensure that any custodian used to hold the cash or securities of a client or an investment fund is a Canadian custodian. If a registered firm has physical possession of the cash or securities of a client or an investment fund then we expect the registered firm to transfer those cash and securities to a Canadian custodian. If a registered firm has access to the cash or securities of a client or an investment fund then we expect the registered firm to confirm that those cash and securities are being held at a Canadian custodian. If a registered firm directs or arranges which custodian a client or an investment fund will use to hold their cash or securities then we expect the registered firm to direct that client or investment fund to, or arrange a custodial relationship with, a Canadian custodian.

For the purposes of section 14.5.2, we expect "cash and securities of an investment fund" to include the cash and securities that comprise the portfolio of an investment fund, as well as cash that may be held by an investment fund manager for investment in, or on the redemption of, securities of the investment fund.

Subsection 14.14(7) sets out when a security is considered to be held by a registered firm for a client. We consider the terms "hold" or "held" in this Division to include the situations identified in subsection 14.14(7). Section 12.4 of this Policy Statement provides examples of when holding or having access to client assets may occur. For the purposes of this Division, we expect all registered firms to consider the examples listed in section 12.4 in determining whether they hold or have access to client assets. For the purposes of section 14.5.2, we interpret the phrase "hold or have access" as not including the handling in transit of a client's cheque made payable to a third party.

We recognize that there may be good reasons for a foreign custodian to be used to hold client or investment fund cash or securities, including where:

- foreign securities comprise all or substantially all of the client's or investment fund's portfolio

- the registered firm's client or the investment fund is resident in a foreign jurisdiction

- a foreign custodian is required to facilitate portfolio transactions in a foreign jurisdiction, or

- using a foreign custodian is more beneficial to the client or investment fund than using a Canadian custodian for tax reasons

In such circumstances, we expect registered firms to assess the risks and benefits of using a foreign custodian compared to the risks and benefits of using a Canadian custodian and determine which custodian is more beneficial for the client. Considerations may include:

- the protections offered by an investor protection fund approved or recognized by the regulator in Canada compared to the comparable investor compensation scheme available in the foreign jurisdiction

- the robustness of the custodial regime in the foreign jurisdiction

- the potential difficulty a client or an investment fund may have enforcing its legal rights in the foreign jurisdiction

- the potential difficulty a client or an investment fund may have repatriating its assets if the foreign custodian declares bankruptcy or becomes insolvent

- the nature of the regulation of the foreign custodian, and

- the sufficiency of the equity of the foreign custodian in the circumstances

A registered firm has a duty to act fairly, honestly and in good faith with its client, or in the best interests of an investment fund that it manages, as applicable. In addition, in compliance with paragraph 11.1(1)(b), registered firms are expected to manage any risks associated with the use of a foreign custodian in accordance with prudent business practices. Accordingly, we expect registered firms to consider alternatives in their assessment of the use of a foreign custodian which, among other considerations, might include whether their client, or an investment fund that they manage, may be better served by:

- using a Canadian custodian who can appoint a foreign custodian to act as a sub-custodian, or

- limiting the client’s or investment fund’s exposure to a particular foreign custodian, which may include using a more diverse range of foreign custodians

Where a foreign custodian is used, we will assess this practice on a case-by-case basis.

Certain investment instruments may be both securities and derivatives. Accordingly, the custodial requirements in this Division apply to these instruments, subject to:

- the definition provision under section 14.5.1, and

- the exemption provided for customer collateral subject to the custodial requirements under *Regulation 94-102 respecting Derivatives: Customer Clearing and Protection of Customer Collateral and Positions* (chapter I-14.01, r. 0.001)

Exemptions from restriction on self-custody and qualified custodian requirement

Investment fund managers are deemed to have access to the portfolio assets of the investment funds managed by them, and must ensure that the portfolio cash and securities of the investment fund are held at a qualified custodian under section 14.5.2. The exemption under paragraph 14.5.2(7)(d) is not available to investment fund managers with respect to the investment funds managed by them.

Registered advisers often create and use investment funds as a way to invest their clients’ money. Registered advisers who also act as the investment fund manager of an investment fund should ensure that the portfolio cash and securities of the investment fund managed by them are held at a qualified custodian. Paragraph 14.5.2(7) (c) provides an exemption for registered firms from the requirement to use a qualified custodian for securities issued by investment funds so long as the securities issued by the investment funds are recorded on the books of the investment fund, or the fund’ transfer agent, only in the name of the registered advisers’ clients.

Mortgages

We recognize that mortgages may have unique custodial practices which may differ from the custodial practices of other types of securities. Mortgages are exempt from the qualified custodian requirement and restriction on self-custody in all jurisdictions of Canada provided that they meet the conditions as set out under paragraph 14.5.2(7)(f).

Prohibition on self-custody and the use of a custodian that is not functionally independent

Under subsection 14.5.2(1), the registered firm itself cannot be the custodian or sub-custodian for a client or investment fund, except in certain circumstances. Under subsections 14.5.2(5) and 14.5.2(6), the qualified custodian, or the Canadian financial institution with respect to cash, must be functionally independent of the registered firm, except in certain circumstances. For the purposes of paragraphs 14.5.2(1)(b) and 14.5.2(5)(b), we would consider a system of controls and supervision to manage the risks to the client or investment fund associated with the custody of the client's or investment fund's cash or securities to include:

- segregation of duties between the custodial function and other functions
- client asset verification examination performed by a third party

Even when a registered firm is not required to use a qualified custodian under subsections 14.5.2(2) or (3) or a Canadian financial institution under subsection 14.5.2(4), we consider it prudent for the registered firm to use a custodian that is functionally independent of the registered firm. Refer to section 12.4 of this Policy Statement for examples of having access to client assets through the use of a custodian that is not functionally independent of the registered firm. The relationship between a registered firm and a non-independent custodian can give rise to serious conflicts of interest. We remind registered firms of their obligations under section 13.4 to identify and respond to conflicts of interest. If the conflicts of interest cannot be managed fairly and effectively, the registered firm should consider using an independent custodian to hold client assets instead.

General prudent custodial practices

Assets other than cash and securities

Section 14.6 sets out the requirement that if a registered firm holds client assets or investment fund assets, which includes securities, cash and other types of assets, then that registered firm must hold the assets separate and apart from its own property, and in trust for the client or investment fund. In accordance with this Division, where a registered firm holds client assets or investment fund assets directly (for example, the assets held are not cash or securities, or the registered firm is relying on an exemption from the requirement to use a qualified custodian), we will assess those circumstances on a case-by-case basis.

We recognize that in limited cases, it may not be feasible to hold certain asset types at a qualified custodian. For example, bullion requires a custodian that is experienced in providing bullion storage and custodial services, and is familiar with the requirements relating to the physical handling and storage of bullion. Such a custodian may not meet the definition of a "qualified custodian". In those cases, we expect a registered firm that would otherwise be subject to subsection 14.5.2(2), (3) or (4), had the client assets or investment fund assets been cash or securities, to exercise due skill, care and diligence in the selection and appointment (where applicable) of the custodian. This can involve the registered firm reviewing the facilities, procedures, records, insurance coverage, and creditworthiness of the selected custodian. We would also expect registered firms to conduct a periodic review of custodial arrangements for client assets or investment fund assets.

Delivery of custodial statements

We expect registered firms to encourage clients or investment funds, as applicable, to confirm that they are receiving account statements from their custodian and, as applicable, to compare the custodial statements to the statements sent by the registered firms.

Reconciliation with custodians

Registered firms are expected to reconcile, on a regular basis, their internal records of client assets or investment fund assets and the records of the custodian where client or investment fund assets are held.

Custodial arrangements

For investment fund managers

Investment fund managers should exercise due skill, care and diligence in the selection and appointment of the custodian for the investment funds managed by them. We expect investment fund managers to conduct a periodic review of custodial arrangements for their investment funds. We also expect investment fund managers to consider whether the custodian it appoints uses all reasonable diligence, care and skill in the selection and monitoring of its sub-custodians, whether the sub-custodians would meet the definition of a "qualified custodian" and whether the appropriate segregation arrangements are observed throughout the custody chain of the portfolio assets of the investment fund.

We expect investment fund managers to put in place a written custodial agreement with the custodian on behalf of investment funds managed by them. Written custodial agreements are expected to provide for key matters such as the location of portfolio assets, any appointment of a sub-custodian, the method of holding portfolio assets, the standard of care of the custodian and the responsibility for loss. Prospectus-qualified investment funds are subject to further custodial requirements under *Regulation 81-102 respecting Investment Funds* (chapter V-1.1, r. 39) and *Regulation 41-101 respecting General Prospectus Requirements* (chapter V-1.1, r. 14).

For registered firms other than investment fund managers

Where registered firms, other than investment fund managers, have influence over a client's selection of a custodian, we consider it a prudent business practice for these registered firms to conduct similar due diligence to that of investment fund managers as outlined in the section above. Registered firms, other than investment fund managers, often direct or arrange the custodial arrangement for their clients; however, the registered firms are not typically a party to the custodial agreement between the client and the custodian used to hold client assets. Nevertheless, we expect registered firms that direct or arrange the custodial arrangement for their clients to understand the material terms of the written custodial agreement and to explain to the clients the main purpose of the agreement. If a custodial agreement allows a custodian to use a sub-custodian, the registered firm should alert the client to that fact and encourage the client to contact the custodian if they have any concerns with the custodial agreement.

14.5.3. Cash and securities held by a qualified custodian

Section 14.5.3 sets out requirements as to how cash and securities should be held by a qualified custodian or a Canadian financial institution. A registered firm can comply with the requirement under subsection 14.5.3(a) by verifying that cash and securities of a client or an investment fund are reported on the custodial account statement of that client or investment fund as issued by the qualified custodian or the Canadian financial institution.

A qualified custodian may arrange for the deposit of securities with a depository, or clearing agency, that operates a book-based system. Such depositories or clearing agencies include The Canadian Depository For Securities Limited, the Depository Trust Company or any other domestic or foreign depository or clearing agency that is incorporated or organized under the laws of a country or a political subdivision of a country and operates a book-based system in that country or political subdivision or operates a transnational book-based system.

14.6. Client and investment fund assets held by a registered firm in trust

Section 14.6 requires a registered firm to segregate client assets and investment fund assets and hold them in trust. When a registered firm is not required to use a qualified custodian, or a Canadian financial institution for cash, under subsections 14.5.2(2), (3) or (4), we consider it prudent for registered firms who are not members of an SRO to only hold client assets in client name, or portfolio assets of the investment fund in the name of the investment fund. This is because the capital requirements for non-SRO members are not designed to reflect the added risk of holding client assets in nominee name.

Investment fund managers may hold cash for investment in, or on the redemption of, securities of the investment fund. For the purposes of section 14.6, such cash-in-transit is considered to be cash and securities of an investment fund of the investment fund manager, and is subject to the requirements under section 14.6. Some investment fund managers choose to outsource certain fund administrative functions to a service provider, including the trust accounting function. Under some outsourcing arrangements, a service provider may be holding cash for investment in, or on the redemption of, securities of the investment fund. Under these arrangements, investment fund managers should ensure that, at a minimum, the cash is held in a designated trust account at a Canadian custodian, a Canadian financial institution, or a foreign custodian (if it is more beneficial to the investment fund to use the foreign custodian than a Canadian custodian or a Canadian financial institution), and ensure that the cash is held separate and apart from the property of the service provider.

Under other outsourcing arrangements, a service provider may be provided with access to cash for investment in, or on the redemption of, securities of the investment fund, or access to the portfolio assets of the investment fund. Investment fund managers are reminded that they are responsible and accountable for all functions that they outsource to a service provider. Delegating access to investors' cash-in-transit or portfolio assets of an investment fund can increase the risk of loss. Investment fund managers are expected to exercise heightened due diligence and oversight to ensure that the service provider has adequate controls in place and that investors' assets are adequately protected.

14.6.1 Custodial provisions relating to certain margin or security interests

Section 14.6.1 sets out acceptable custodial practices relating to margin posted with, and security interests held by, a foreign dealer or counterparty in respect of certain derivatives transactions. We expect that the assessment of the use of a foreign custodian in section 14.5.2 of this Policy Statement will apply equally to the foreign dealer referenced in this section.

In addition to these custodial practices relating to certain derivatives, a registered firm may also ensure that cash or securities of a client or investment fund are delivered to a person in satisfaction of its obligations under a securities lending, repurchase or reverse repurchase agreement if the collateral, cash proceeds or purchased securities that are delivered to the client or investment fund in connection with the transaction are held under the custodianship of a qualified custodian or a sub-custodian of the client or investment fund in compliance with Division 3 of Part 14.

14.6.2 Custodial provisions relating to short sales

Section 14.6.2 sets out acceptable custodial practices relating to cash or securities of a client or investment fund that are deposited with a foreign dealer as security in connection with a short sale of securities. We expect that the assessment of the use of a foreign custodian in section 14.5.2 of this Policy Statement will apply equally to the foreign dealer referenced in this section.

Division 4 Client accounts

14.10. Allocating investment opportunities fairly

If the adviser allocates investment opportunities among its clients, the firm's fairness policy should, at a minimum, indicate the method used to allocate the following:

- price and commission among client orders when trades are bunched or blocked

- block trades and initial public offerings among client accounts

- block trades and initial public offerings among client orders that are partially filled, such as on a pro-rata basis

The fairness policy should also address any other situation where investment opportunities must be allocated.

Division 5 Reporting to clients

Reporting to clients is on an account basis, except that

- securities that are not held in an account (i.e., securities reported under an additional statement) must be included in a report for the account through which they were traded, and

- subsection 14.18(4) permits performance reports for more than one account of a client and also securities not held in an account to be combined with the client's written consent.

Registered firms may choose how they meet their client reporting obligations within the framework set out in the Regulation. We encourage firms to combine client statements, position cost information and client reports into comprehensive documents or send them together. For example, an account statement and an additional statement for securities traded through (but not held) in an account might be combined, perhaps along with position cost information, each quarter. Once a year, an integrated statement such as this could be further combined with the report on charges and other compensation and the performance report, or delivered along with a separate document that combines the 2 reports.

We believe that integrating client reporting as much as possible within the limitations of firms' systems capabilities will better enable clients to make use of the information and that it is in the interests of registrants to have clients that are well informed about the services they provide. When client reporting information is combined or delivered together, we expect registered firms will give each element sufficient prominence among the others that a reasonable investor can readily locate it.

Consistent with the guidance on clear and meaningful disclosure to clients in section 1.1 of this Policy Statement, we expect registrants to present client statements and reports in an understandable manner and to explain, if applicable, what securities are included in different statements. Registered firms should encourage clients to contact their dealing or advising representative or the firm directly with questions about their statements and reports. We expect registered firms to ensure that clients know how their investments will be held (for example, by the firm or at an issuing fund company) and understand the different implications that this will have for them in such matters as client reporting, investor protection fund coverage and custody of their assets. If a registered firm trades in exempt market securities for a client, the firm should also explain the reasons why it is not always possible for the firm to determine a market value for products sold in the exempt market or whether the client still owns the security, and the implications that this may have for reporting on exempt-market securities.

It is the responsibility of the registered firm to produce these client statements and reports, not that of individual representatives. Registered firms should have policies and procedures in place to ensure that they are adequately supervising their registered representatives' communications with clients about the prescribed information.

The requirement to produce and deliver a trade confirmation under section 14.12, an account statement under section 14.14, an additional statement under section 14.14.1, position cost information under section 14.14.2, a security holder statement under section 14.15, a scholarship plan dealer statement under section 14.16 or client reports under sections 14.17 and 14.18 may be outsourced by a registered firm to a third-party service provider that acts as its agent. Third-party pricing providers may also be used to value securities for these purposes. Like all outsourcing arrangements, the registrant is ultimately responsible for the function and must supervise the service provider. See Part 11 of this Policy Statement for more guidance on outsourcing.

For the most part, the client reporting requirements in Part 14 do not differentiate between categories of registrant. Except for certain provisions which expressly apply only to a specific registration category (such as those tailored to scholarship plan dealers), differences in the application of these requirements between different registered dealers or registered advisers will be the result of their different operating models. In particular, exempt market dealers that are not also registered as advisers or in another category of dealer may find that not all of the client reporting requirements will apply to their operating model. Appendix F discusses how these requirements may apply in the case of some of these "sole EMDs".

14.11.1. Determining market value

Section 14.11.1 sets out the basis on which market value must be determined for client reporting purposes.

Paragraph 14.11.1(1)(a) requires the market value of a security that is issued by an investment fund not listed on an exchange to be determined by reference to the net asset value provided by the investment fund manager of the fund on the relevant date.

For other securities, a hierarchy of valuation methods that depend on the availability of relevant information is prescribed in paragraph 14.11.1(1)(b). Registrants are required to act reasonably in applying these methodologies and we understand that this process will often require a registrant to exercise professional judgment. A registered firm may not simply take valuation information from an issuer and pass it on to clients as the market value for purposes of meeting the firm's market value reporting obligations. We expect a firm to use its professional judgment as to the reliability of information provided by an issuer as an input to the firm's determination of market value in accordance with the applicable methodology prescribed in section 14.11.1.

Where possible, market value should be determined by reference to a quoted value on a marketplace. The quoted value will be the last bid or ask price on the relevant date or the last trading day prior to the relevant date. In the case of a liquid security for which a reliable price is quoted on a market place, if it can be demonstrated through use of a periodic assessment that a "last traded price" valuation approach results in security market values that are materially the same as under the "last bid and ask prices" valuation approach, it may be acceptable to use this current "last traded price" valuation approach. Registered firms should ensure that any quoted values used to determine market value do not represent stale or old prices that are not reflective of current values. If no current value for a security is quoted on a marketplace, market value should be determined by reference to published market reports or inter-dealer quotes.

We recognize that it is not always possible to obtain a market value by these methods. In such cases, we will accept a valuation policy that is consistently applied and includes procedures that assess the reliability of any valuation inputs and assumptions. If available, valuation inputs and assumptions should be based on observable market data or inputs, such as market prices or yield rates for comparable securities and quoted interest rates. If observable inputs are not available, valuation can be based on unobservable inputs and assumptions. In some cases, it may be reasonable and appropriate to value at cost, where there has been no material subsequent event affecting value (e.g. a market event or new capital raising by the issuer). "Observable" and "unobservable" inputs are concepts under International Financial Reporting Standards (IFRS), and we expect them to be applied consistent with IFRS.

If, having applied the prescribed methodology, a registered firm reasonably believes it cannot determine the market value of a security, the firm must then report its value as "not determinable" and exclude it from the calculations in client statements as prescribed in subsection 14.11.1(3).

This is not the same as determining that the market value of a security *is* zero. However, we would expect that if the market value of a security cannot be determined for a prolonged period of time, that fact may be an indication that the market value of the security should now be determined to be zero.

The following considerations can be used in determining when the market value for a security is not determinable:

- the position is illiquid

- there is little or no issuer and issuer-related financial data available, or the data is stale

- there is little or no financial data available for comparable issuers or for the issuer's business sector

- there is not enough data to use the valuation methodology prescribed in paragraph 14.11.1(1)(b) and/or the results of the various IFRS methodologies used have been determined to be unreliable because of the use of unreliable data or the results indicate a wide range in possible values

- the acquisition cost of the security is no longer a good estimate of the security's market value as the cost is outside the range of possible values for the security

Important to applying these considerations is establishing and maintaining a firm policy as to how many days beyond which the last data available is considered to be stale.

If the market value for a security subsequently becomes determinable, a registered firm must begin to report it in client statements and add that value to the opening market values or deposits included in the calculations in subsection 14.19(1). This would be expected if the firm had previously assigned the security a value of zero in the calculation of opening market values or deposits because it could not determine the security's market value, as required by subsection 14.19(7). This would reduce the risk of presenting a misleading improvement in the performance of the investment by only adding the value of the security to the other calculations required under section 14.19. If the deposits used to purchase the security were already included in the calculation of opening market values or deposits, the registered firm would not need to adjust these figures.

We encourage firms to disclose the foreign exchange rate used in calculating the market value of non-Canadian dollar denominated securities as a best practice.

14.12. Content and delivery of trade confirmation

Section 14.12 requires registered dealers to deliver trade confirmations.

Under paragraph 14.12(1)(b.1), registered dealers must provide the yield on a purchase of a debt security in a trade confirmation. For non-callable debt securities, the yield to maturity would be appropriate. For callable securities, the yield to call may be more useful.

Under paragraph 14.12(1)(c.1), registrants may disclose the total dollar amount of compensation (which may consist of any mark-up or mark-down, commission or other service charge) or, alternatively, the total dollar amount of commission, if any, and if the registrant applied a mark-up or mark-down or any service charge other than a commission, a prescribed general notification. The notification is a minimum requirement and a firm may elect to provide more information in its trade confirmations.

Each trade should be reported in the currency in which it was executed. If a trade is executed in a foreign currency through a Canadian dollar account, the exchange rate should be reported to the client.

Under subsection 14.12(7), a registered dealer that complies with the requirements of section 14.12 in respect of a purchase or sale of a security is not subject to the corresponding written confirmation requirements contained in any of subsections 37(1), (2) or (3) of the *Securities Act* (R.S.N.L. 1990, c. S-13), subsection 36(1) of the *Securities Act* (R.S.O. 1990, chapter S.5) and subsection 42(1) of *The Securities Act, 1988* (S.S. 1988-89, c. S-42.2). For these purposes, a firm that has an exemption from section 14.12 and complies with the terms of that exemption would be considered to have complied with the requirements of that section.

14.14. Account statements

Section 14.14 requires registered dealers and advisers to deliver statements to clients at least once every 3 months. There is no prescribed form for these statements but they must contain the information referred to in subsections 14.14(4) and (5). The types of transactions that must be disclosed in an account statement include any purchase, sale or transfer of securities, dividend or interest payment received or reinvested, any fee or charge, and any other account activity. A firm must deliver an account statement with the information referred to in subsection (4) if any transaction was made for the client in the reporting period. A firm is only required to provide the account position information referred to in subsection (5) if it holds securities owned by a client in an account of the client.

There is no provision for consolidated statements in section 14.14 (or 14.14.1), so a registered firm must provide every client with an applicable statement for each of their accounts. Firms may provide supplementary reporting that they think a client might find useful. For example, a firm might provide a consolidated year-end statement where a client has requested a consolidated performance report under subsection 14.18(4).

14.14.1. Additional statements

A firm is required to deliver additional statements if the circumstances described in subsection 14.14.1(1) apply. The additional statements must be delivered once every 3 months, except that an adviser must deliver the statements on a monthly basis if requested by the client as provided in subsection 14.14.1(3). The requirements set out for the frequency of delivering account statements and additional statements are minimum standards. Firms may choose to provide the statements more frequently.

Paragraph 14.14.1(2)(g) requires disclosure about applicable investor protection funds. However, subsection 14.14.1(2.1) exempts a firm from this requirement where a client's securities are held or controlled by an IIROC or MFDA member. SRO rules require members to be participants in specified investor protection funds and prescribe client disclosures about them. To avoid the potential that clients may be confused or misinformed, registrants that are not participants in an investor protection fund should refrain from discussing its terms and conditions with clients.

Firms may choose to include securities that must be reported under the additional statement requirement in a document that it refers to as an account statement, consistent with their clients' expectations that their accounts are not limited to securities held by the firm, provided it satisfies the requirements for content of statements set out in sections 14.14 and 14.14.1.

14.14.2. Security position cost information

Section 14.14.2 requires the delivery on a quarterly basis of position cost information for securities reported in account statements and additional statements. For purposes of section 14.14.2, a security position is “opened” when the registered firm that is providing a statement to a client first acquires or holds securities for that client or when it first obtains trading authority over securities (as in the case of securities transferred into a discretionary account of a portfolio manager).

Position cost information is an investment performance measurement tool that provides investors with a comparison to the market value of each security position they have open. Position cost may be either the book cost or the original cost of the securities, determined in accordance with their respective definitions in section 1.1.

Position cost is not tax information and a registered firm may not depart from the defined meaning of “original cost” or “book cost” in order to align position cost with tax cost for a security position. Registered firms may provide clients with tax cost as supplementary information if they wish to do so, provided the difference is made clear to clients. If the tax treatment of a security is an important part of its marketing to investors, we would expect a registered firm to provide tax information as well as position cost information, consistent with the duty to deal fairly, honestly and in good faith with clients.

Registered firms must include the definition of book cost or original cost, depending on which method the firm is using, in the statement or document where the position cost information appears as contemplated under subsection 14.14.2(4). Firms can comply with this requirement in a footnote.

In determining position cost for transferred securities, a registered firm may rely on position cost information provided by the transferring firm, if

- the transferring-out firm is also subject to the requirement to provide individual position cost information to clients, and

- the transferring-in firm has no reason to believe the information is not reliable.

Where securities were transferred from another registrant firm, a registrant may also elect to use market value information as at the date of the transfer as the position cost. Firms must specify each security position where market value has been used rather than book or original cost. A footnote could be used for this purpose, with disclosure such as “because book cost information for this security position was unavailable, we have used market value information as of the transfer date as the position cost”.

If a security position was opened before July 15, 2015, a registered firm can choose to report (a) the cost of the security position, (b) the market value of the security position as at December 31, 2015, or (c) the market value of the security position as at a date earlier than December 31, 2015, if the firm reasonably believes accurate recorded historical market value information is available for the client's account, and it would not be misleading to the client to provide that information as at the earlier date. Examples of circumstances under which we would consider it to be reasonable and not misleading for a firm to use a date earlier than December 31, 2015 for some but not all of its clients' security positions opened before July 15, 2015 include when a firm that uses the same earlier date for:

- all client accounts or security positions that were transferred to the firm at the same time, or

- all clients that are on the same reporting system of the registered firm, if the firm has more than one reporting system.

If a security position is built up over time with successive transactions (purchases or transfers), an average can be used to determine the cost of the position. The average may include both book or original cost information used for some of the transactions and market value used for others. In such cases, the disclosure applicable where market value has been used should be modified as necessary. For example: "The cost of this security position has been determined using an average of market value as of the date on which some securities were transferred into your account when it was opened, and the book cost of securities that we subsequently purchased for your account." It is also permissible to differentiate between positions in the same security that were opened in separate transactions by reporting positions valued at book cost or original cost separately from those where market value was used, instead of averaging them into a single number. However, this alternative approach has the potential to confuse clients, so clear explanatory notes should be provided if it is used.

Position cost information must be delivered at least quarterly. A firm may combine position cost information with an account statement or additional statement for the period, or it may send it separately. If it chooses to send position cost information separately, the firm must deliver it within 10 days after the statement(s) have been delivered and must also include the market value information from the statement(s) for the period in order that the client will be able to readily compare the information. Although a firm may deliver statements under section 14.14 or section 14.14.1 more frequently than quarterly, it is not required to provide position cost information except on a quarterly basis.

14.15. Security holder statements

Section 14.15 sets out the client reporting requirements applicable to a registered investment fund manager where there is no dealer or adviser of record for a security holder on the records of the investment fund manager.

14.16. Scholarship plan dealer statements

Section 14.16 provides that sections 14.14, 14.14.1 and 14.14.2 do not apply to a scholarship plan dealer that delivers prescribed information to a client at least once every 12 months. Subsection 14.19(4) sets out performance reporting requirements for scholarship plans.

14.17. Report on charges and other compensation

Registered firms must provide clients with an annual report on the firm's charges and other compensation received by the firm in connection with their investments. Examples of operating charges and transaction charges are provided in the discussion of the disclosure of charges and other compensation in section 14.2 of this Policy Statement. The annual report must include information about all of the firm's current operating charges that might be applicable to a client's account. A firm is only required to include the charges for those of its services that it would reasonably expect the particular client to utilize in the coming 12 months.

The discussion of debt security disclosure requirements in section 14.12 of this Policy Statement is also relevant with respect to paragraph 14.17(1)(e).

Scholarship plans often have enrolment fees payable in instalments in the first few years of a client's investment in the plan. Paragraph 14.17(1)(f) requires that scholarship plan dealers include a reminder of the unpaid amount of any such fees in their annual reports on charges and other compensation.

Payments that a registered firm or its registered representatives receive from issuers of securities or other registrants in relation to registerable services to a client must be reported under paragraph 14.17(1)(g). This disclosure requirement includes any form of payment to the firm or a representative of the firm linked to sales or other registerable services to the client receiving the report. Examples of payments that would be included in this part of the report on charges and other compensation include some referral fees, success fees on the completion of a transaction, or finder's fees. This part of the report does not include trailing commissions, as they are specifically addressed in paragraph 14.17(1)(h).

Registered firms must disclose the amount of trailing commissions they received related to a client's holdings. The disclosure of trailing commissions received in respect of a client's investments must be included with a notification prescribed in paragraph 14.17(1)(h). The notification must be in substantially the form prescribed, so a registered firm may modify it to be consistent with the actual arrangements. For example, a firm that receives a payment that falls within the definition of "trailing commission" in section 1.1 in respect of securities that are not investment funds can modify the notification accordingly. The notification set out is the required minimum and firms can provide further explanation if they believe it will be helpful to their clients.

Registered firms may want to organize the annual report on charges and other compensation with separate sections showing the charges paid by the client to the firm, and the other compensation received by the firm in respect of the client's account.

Appendix D of this Policy Statement includes a sample Report on Charges and Other Compensation, which registered firms are encouraged to use as guidance.

14.18. Investment performance report

Where more than one registrant provides services pertaining to a client's account, responsibility for performance reporting rests with the registered firm with the client-facing relationship. For example, if a registered adviser has trading authority over a client's account at a registered dealer, the adviser must provide the client with an annual investment performance report; this is not an obligation of the dealer that only executes adviser-directed trades or provides custodial services in respect of the client's account.

Performance reporting to clients is required to be provided separately for each account. Securities of a client required to be reported in an additional statement under section 14.14.1, if any, must be covered in a performance report that also includes any other securities in the account through which they were transacted. However, subsection 14.18(4) provides that with client consent, a registrant may provide consolidated performance reporting for that client. A registrant may also provide a consolidated performance report for multiple clients, such as a family group, but only as a supplemental report, in addition to reports required under section 14.18.

14.19. Content of investment performance report

Subsection 14.19(5) requires the use of each of text, tables and charts in the presentation of investment performance reports. Explanatory notes and the definition of "total percentage return" must also be included. The purpose of these requirements is to make the information as understandable to investors as possible.

To help investors get the most out of their investment performance reports and encourage informed discussion with their registered dealing representative or advising representative, we encourage registered firms to consider including:

- additional definitions of the various performance measures used by the registrant
- additional disclosure that enhances the performance presentation
- a discussion with clients about what the information means to them

Registrants should not mislead a client by presenting a return of the client's capital in a manner that suggests it forms part of the client's return on an investment.

Registered representatives are also encouraged to meet with clients, as part of an in-person or telephone meeting, to help ensure they understand their investment performance reports and how the information relates to the client's investment objectives and risk tolerance.

Appendix E of this Policy Statement includes a sample Investment Performance Report which registered firms are encouraged to use as guidance.

Opening market value, deposits and withdrawals

As part of paragraphs 14.19(1)(a) and (b), registered firms must disclose the market value of cash and securities in the client's account as at the beginning and the end of the 12-month period covered by the investment performance report. The market value of cash and securities at account opening is assumed to be zero.

Under paragraphs 14.19(1)(c), (d) and subsection 14.19(1.1), registered firms must also disclose the market value of all deposits and transfers of cash and securities into the account, and the market value of all withdrawals and transfers of cash and securities out of the account, for the 12-month period covered by the performance report, as well as, subject to certain exceptions discussed below, since account opening. Deposits and transfers into the account (which do not include reinvested distributions or interest income) should be shown separately from withdrawals and transfers out of the account.

If an account was opened before July 15, 2015, registered firms must present the market value of all cash and securities in the client's account as at one of the following dates:

(a) January 1, 2016 or an earlier date, if the firm's first performance report to the client covered the 2016 calendar year (paragraph 14.19(1.1)(c)),

(b) July 15, 2015 or an earlier date, if the firm's first performance report to the client covered some other period (paragraph 14.19(1.1)(b)).

A registered firm may choose a date earlier than July 15, 2015 or January 1, 2016, as applicable under paragraph 14.19(1.1)(b) or (c), only if the firm reasonably believes accurate recorded historical market value information is available for the client's account, and it would not be misleading to the client to provide that information as at the earlier date. As with position cost information, examples of circumstances under which we would consider it to be reasonable and not misleading for a firm to use a date earlier than July 15, 2015 or January 1, 2016, as applicable, for some but not all of its clients' accounts include when a firm that uses the same earlier date for:

- all client accounts that were transferred to the firm at the same time, or
- all clients that are on the same reporting system of the registered firm, if the firm has more than one reporting system.

The registered firm must also present the market value of all deposits, withdrawals and transfers of cash and securities since the date chosen under paragraph 14.19(1.1)(b) or (c).

Subsection 14.19(7) requires a registered firm that cannot determine the market value for a security position to assign the security a value of zero for the performance reporting purposes and the reason for doing so must be disclosed to the client. The explanation may be included as a note in the performance report. As described in section 14.11.1 of this Policy Statement, if a registered firm is subsequently able to value that security it may need to adjust the calculation of the market values or deposits to avoid presenting a misleading improvement in the performance of the account.

A registered firm is not required to deliver a nil report in circumstances where it reasonably believes that none of a client's securities have a determinable value. We would expect the firm to tell the client that it will not be delivering an investment performance report for the period and explain why.

Change in market value

The opening market value, plus deposits and transfers in, less withdrawals and transfers out, should be compared to the market value of the account as at the end of the 12-month period for which the performance reporting is provided and also since inception in order to provide clients, in dollar terms, with the performance of their account.

The change in the market value of the account since inception is the difference between the closing market value of the account and total of opening market value plus deposits less withdrawals since inception. The change in the value of the account for the 12-month period is the difference between the closing market value of the account and total of opening market value plus deposits less withdrawals during the period. If the client's account was opened before July 15, 2015, a registered firm is required to disclose the change in value of a client's account since one of July 15, 2015, January 1, 2016 or an earlier date determined on the basis of the same criteria as described above with reference to paragraph 14.19(1.1)(b) or (c).

The change in market value includes components such as income (dividends, interest) and distributions, including reinvested income or distributions, realized and unrealized capital gains or losses in the account, and the effect of operating charges and transaction charges if these are deducted directly from the account. Rather than show the change in value as a single amount, registered firms may opt to break this out into its components to provide more detail to clients.

Percentage return calculation method

Paragraph 14.19(1)(i) requires firms to provide the annualized total percentage return using a money-weighted rate of return calculation method. No specific formula is prescribed, but the method used by a firm must be one that is generally accepted in the securities industry. A registered firm may, if it so chooses, provide percentage returns calculated using both money-weighted and time-weighted methods. In such cases, the firm should explain in plain language the difference between the 2 sets of performance returns.

Paragraph 14.19(1)(j) requires that performance reports include a notification with specified information about how the client's percentage return was calculated. This includes an explanation in general terms of what the calculation method takes into account. We do not expect firms to include a formula or an exhaustive list. For example, a firm could explain that under a money weighted method, decisions a client made about deposits and withdrawals to and from the client's account have affected the returns calculated in the report and that this means it represents the client's personal rate of return. We expect firms to use this notification to help clients understand the most important implications of the calculation methodology. A client's personal rate of return should be compared to the client's target rate of return, if the client has one, so that progress toward that goal can be assessed. We expect a firm that also uses a time weighted method to explain the difference between the 2 rates of return in plain language. For example, the firm could explain that the returns calculated under a time weighted method may not be the same as the actual returns in the client's account because they do not necessarily show the effect of deposits and withdrawals to and from the account, and that a time weighted return is useful in determining how well a money manager performed, but not necessarily how the client's account actually grew.

Performance reporting periods

Subsection 14.19(2) outlines the minimum reporting periods of 1, 3, 5 and 10 years and the period since the inception of the account. For accounts opened before July 15, 2015, a registered firm may use a deemed inception date of January 1, 2016, July 15, 2015 or an earlier date determined on the basis of the same criteria as that described above.

Registered firms may opt to provide more frequent performance reporting. However performance returns for periods of less than one year can be misleading and therefore, must not be presented on an annualized basis, consistent with subsection 14.19(6).

Scholarship plans

Under paragraph 14.19(4)(c), for scholarship plans, the information required to be delivered in the investment performance report includes a reasonable projection of future scholarship payments that the plan may pay to the client or the client's designated beneficiary upon the maturity of the client's investment in the plan.

A scholarship plan dealer is also required under paragraph 14.19(4)(d) to provide a summary of any terms of the plan, which if not met by the client or the client's designated beneficiary under the plan, may cause the client or the designated beneficiary to suffer a loss of contributions, earnings or government contributions in the plan. The disclosure here is not intended to be as detailed as the disclosure at account opening. It is intended to remind the client of the unique risks of the plan and the ways in which the client's scholarship plan may be seriously impaired. This disclosure must be consistent with other disclosures required to be delivered to clients under applicable securities legislation.

To the extent that a scholarship plan dealer and the plan itself are not the same legal entity but are affiliates of one another, the dealer may meet obligations to deliver annual investment performance reports by drawing attention to the plan's direct mailing of reports to a client by the plan's administrator.

Benchmarks and investment performance reporting

The use of benchmarks for investment performance reporting is optional. There is no requirement to provide benchmarks to clients in any of the reports required under Regulation 31-103.

However, we encourage registrants to use benchmarks that are relevant to a client's investments as a useful way for a client to assess the performance of their portfolio. Benchmarks need to be explained to clients in terms they will understand, including factors that should be considered by the client when comparing their investment returns to benchmark returns. For example, a registrant could discuss the differences between the composition of a client's portfolio that reflects the investment strategy they have agreed upon and the composition of an index benchmark, so that a comparison between them is fair and not misleading. A discussion of the impact of operating charges and transaction charges as well as other expenses related to the client's investments would also be helpful to clients, since benchmarks generally do not factor in the costs of investing.

If a registered firm chooses to present benchmark information, the firm should ensure that it is not misleading. We expect registrants to use benchmarks that are

- discussed with clients to ensure they understand the purpose of comparing the performance of their portfolio to the chosen benchmarks and determine if their information needs will be met

- reasonably reflective of the composition of the client's portfolio so as to ensure that a relevant comparison of performance is presented

- relevant in terms of the investment time horizon of the client

- based on widely recognized and available indices that are credible and not manufactured by the registrant or any of its affiliates using proprietary data

- broad-based securities market indices which can be linked to the major asset classes into which the client's portfolio is divided. The determination of a major asset class should be based on the firm's own policies and procedures and the client's portfolio composition. An asset class for benchmarking purposes may be based on the type of security and geographical region. We do not expect an asset class to be determined by industry sector

- presented for the same reporting periods as the client's annualized total percentage returns

- clearly named

- applied consistently from one reporting period to the next for comparability reasons, unless there has been a change to the pre-determined asset classes. In this case, the change in the benchmark(s) presented should be discussed with the client and included in the explanatory notes, along with the reasons for the change

Examples of acceptable benchmarks would include, but are not limited to, the S&P/TSX Composite index for Canadian equities, the S&P 500 index for U.S. equities, and the MSCI EAFE index as a measure of the equity markets outside of North America.

14.20. Delivery of report on charges and other compensation and investment performance report

Registered firms must deliver the annual report on charges and other compensation under section 14.17 and the investment performance report under section 14.18 for a client together. These client reports may be combined with or accompany an account statement or additional statement for a client, or must be sent within 10 days after an account statement or additional statement for the client.

Appendix A Contact Information

Jurisdiction	E-mail	Fax	Address
Alberta	registration@asc.ca	(403) 297-4113	Alberta Securities Commission, Suite 600, 250–5th St. SW Calgary, AB T2P 0R4 Attention: Registration
British Columbia	registration@bcsc.bc.ca	(604) 899-6506	British Columbia Securities Commission P.O. Box 10142, Pacific Centre 701 West Georgia Street Vancouver, BC V7Y 1L2 Attention: Registration
Manitoba	registrationmsc@gov.mb.ca	(204) 945-0330	The Manitoba Securities Commission 500-400 St. Mary Avenue Winnipeg, MB R3C 4K5 Attention: Registrations
New Brunswick	registration-inscription@fcnb.ca	(506) 658-3059	Financial and Consumer Services Commission of New Brunswick / Commission des services financiers et des services aux consommateurs du Nouveau-Brunswick Suite 300, 85 Charlotte Street Saint John, NB E2L 2J2 Attention: Registration
Newfoundland & Labrador	scon@gov.nl.ca	(709) 729-6187	Superintendent of Securities, Service NL P.O. Box 8700, 2nd Floor, West Block Confederation Building St. John's, NL A1B 4J6 Attention: Manager of Registrations
Northwest Territories	SecuritiesRegistry@gov.nt.ca	(867) 873-0243	Government of the Northwest Territories P.O. Box 1320 Yellowknife, NWT X1A 2L9 Attention: Deputy Superintendent of Securities
Nova Scotia	nrs@novascotia.ca	(902) 424-4625	Nova Scotia Securities Commission Suite 400, 5251 Duke Street P.O. Box 458 Halifax, NS B3J 2P8 Attention: Deputy Director, Capital Markets

Nunavut	CorporateRegistrations@gov.nu.ca	(867) 975-6590 (Faxing to NU is unreliable. The preferred method is e-mail.)	Legal Registries Division Department of Justice Government of Nunavut P.O. Box 1000 Station 570 Iqaluit, NU X0A 0H0 Attention: Deputy Registrar
Ontario	registration@osc.gov.on.ca	(416) 593-8283	Ontario Securities Commission 22nd Floor 20 Queen Street West Toronto, ON M5H 3S8 Attention: Compliance and Registrant Regulation
Prince Edward Island	ccis@gov.pe.ca	(902) 368-6288	Consumer and Corporate Services Division, Office of the Attorney General P.O. Box 2000, 95 Rochford Street Charlottetown, PE C1A 7N8 Attention: Superintendent of Securities
Québec	inscription@lautorite.qc.ca	(514) 873-3090	Autorité des marchés financiers Direction de l'encadrement des intermédiaires 800 square Victoria, 22e étage C.P 246, Tour de la Bourse Montréal (Québec) H4Z 1G3
Saskatchewan	registrationfcaa@gov.sk.ca	(306) 787-5899	Financial and Consumer Affairs Authority of Saskatchewan Suite 601 1919 Saskatchewan Drive Regina, SK S4P 4H2 Attention: Registration
Yukon	securities@gov.yk.ca	(867) 393-6251	Department of Community Services Yukon Yukon Securities Office P.O. Box 2703 C-6 Whitehorse, YT Y1A 2C6 Attention: Superintendent of Securities

Appendix B Terms Not Defined in Regulation 31-103 or this Policy Statement

Terms defined in *Regulation 14-101 respecting Definitions* (chapter V-1.1, r. 3):

- adviser registration requirement
- Canadian securities regulatory authority
- dealer registration requirement
- exchange contract (AB, SK, NB and NS only)
- foreign jurisdiction
- jurisdiction or jurisdiction of Canada
- local jurisdiction
- investment fund manager registration requirement
- prospectus requirement
- registration requirement
- regulator
- securities directions
- securities legislation
- securities regulatory authority
- SRO
- underwriter registration requirement

Terms defined in *Regulation 45-106 respecting Prospectus Exemptions* (chapter V-1.1, r. 21):

- accredited investor
- eligibility adviser
- financial assets

Terms defined in *Regulation 81-102 respecting Investment Funds* (chapter V-1.1, r. 39):

- money market fund

Terms defined in the *Securities Act* of most jurisdictions:

- adviser
- associate
- company
- control person
- dealer
- director
- distribution
- exchange contract (BC only)
- insider
- individual
- investment fund
- investment fund manager
- issuer
- mutual fund
- officer
- person
- promoter
- records
- registrant
- reporting issuer
- security
- trade
- underwriter

Appendix C Proficiency Requirements for Individuals Acting on Behalf of a Registered Firm

The tables in this Appendix set out the education and experience requirements, by firm registration category, for individuals who are applying for registration under securities legislation.

An individual must not perform an activity that requires registration unless the individual has the education, training and experience that a reasonable person would consider necessary to perform the activity competently, including, in the case of registered representatives, understanding the structure, features and risks of the securities as well as the initial and ongoing costs of the securities and the impact of those costs. An understanding of all securities that registered individuals purchase or sell for, or recommend to, clients is necessary in order for registered individuals to make the suitability determination that is required by section 13.3.

CCOs must also not perform an activity set out in section 5.2 unless they have the education, training and experience that a reasonable person would consider necessary to perform the activity competently.

Acronyms used in the tables

BMP: Branch Manager Proficiency Exam	**CIM:** Canadian Investment Manager designation
CA: Chartered Accountant	**CSC:** Canadian Securities Course Exam
CCO: Chief Compliance Officer	**EMP:** Exempt Market Products Exam
CCOQ: Chief Compliance Officers Qualifying Exam	**IFIC:** Investment Funds in Canada Course
CFA: CFA Charter	**MFDC**: Mutual Funds Dealer Compliance Exam
CGA: Certified General Accountant Exam/Partners, Directors	**PDO:** Officers', Partners' and Directors' and Senior Officers Course Exam
CMA: Certified Management Accountant	**SRP:** Sales Representative Proficiency Exam
CIF: Canadian Investment Funds Course Exam	

Investment dealer	
Dealing representative	**CCO**
Proficiency requirements set by IIROC	Proficiency requirements set by IIROC
Mutual fund dealer	
Dealing representative	**CCO**
One of these 5 options: 1. CIF 2. CSC 3. IFIC 4. CFA Charter and 12 months of relevant securities industry experience in the 36-month period before applying for registration 5. Advising representative requirements – portfolio manager or exempt from these under subsection 16.10(1)	One of these 2 options: 1. CIF, CSC or IFIC; and PDO, MFDC or CCOQ and 12 months of relevant securities industry experience in the 36-month period before applying for registration 2. CCO requirements – portfolio manager or exempt from these under subsection 16.9(2)

Exempt market dealer	
Dealing representative	**CCO**
One of these 4 options: 1. CSC 2. EMP 3. CFA Charter and 12 months of relevant securities industry experience in the 36-month period before applying for registration 4. Advising representative requirements – portfolio manager or exempt from these under subsection 16.10(1)	One of these 2 options: 1. PDO or CCOQ and EMP or CSC and 12 months of relevant securities industry experience in the 36-month period before applying for registration 2. CCO requirements – portfolio manager or exempt from these under subsection 16.9(2)

Scholarship plan dealer	
Dealing representative	**CCO**
	SRP, BMP, and PDO or CCOQ and 12 months of relevant security industry experience in the 36-month period before applying for registration
Restricted dealer	
Dealing representative	**CCO**
Regulator to determine on a case-by-case basis	Regulator to determine on a case-by-case basis

Portfolio manager		
Advising representative	**Associate advising representative**	**CCO**
One of these 2 options: 1. CFA and 12 months of relevant investment management experience in the 36-month period before applying for registration 2. CIM and 48 months of relevant investment management experience (12 months gained in the 36-month period before applying for registration)	One of these 2 options: 1. Level 1 of the CFA and 24 months of relevant investment management experience 2. CIM and 24 months of relevant investment management experience	One of these 3 options: 1. CSC except if the individual has the CFA or CIM designation, PDO or CCOQ, and CFA or a professional designation as a lawyer, CA, CGA, CMA, notary in Québec or the equivalent in a foreign jurisdiction, and: • 36 months of relevant securities experience working at an investment dealer, registered adviser or investment fund manager, or • 36 months providing professional services to the securities industry and 12 months working at a registered dealer, registered adviser or investment fund manager, for a total of 48

		months 2. CSC except if the individual has the CFA or CIM designation, PDO or CCOQ and 5 years working at: • an investment dealer or a registered adviser (including 36 months in a compliance capacity), or • a Canadian financial institution in a compliance capacity relating to portfolio management and 12 months at a registered dealer or registered adviser, for a total of 6 years 3. PDO or CCOQ and advising representative requirements – portfolio manager
Restricted portfolio manager		
Advising representative	**Associate advising representative**	**CCO**
Regulator to determine on a case-by-case basis	Regulator to determine on a case-by-case basis	Regulator to determine on a case-by-case basis
Investment fund manager		
CCO		
One of these 3 options: 1. CSC except if the individual has the CFA or CIM designation, PDO or CCOQ, and CFA or a professional designation as a lawyer, CA, CGA, CMA, notary in Québec or the equivalent in a foreign jurisdiction, and: • 36 months of relevant securities experience working at a registered dealer, registered adviser or investment fund manager, or • 36 months providing professional services in the securities industry and 12 months working in a relevant capacity at an investment fund manager, for a total of 48 months 2. CIF, CSC or IFIC; PDO or CCOQ and 5 years of relevant securities experience working at a registered dealer, registered adviser or an investment fund manager (including 36 months in a		

compliance capacity) 3. CCO requirements for portfolio manager or exempt from these requirements under subsection 16.9(2)

Appendix D Annual Charges and Compensation Report

[Name of Firm]

Annual Charges and Compensation Report

Client name — Your Account Number: 123456

Address line 1

Address line 2

Address line 3

This report summarizes the compensation that we received directly and indirectly in 20XX. Our compensation comes from 2 sources:

1. What we charge you directly. Some of these charges are associated with the operation of your account. Other charges are associated with purchases, sales and other transactions you make in the account.

2. What we receive through third parties.

Charges are important because they reduce your profit or increase your loss from investing. If you need an explanation of the charges described in this report, your representative can help you.

Charges you paid directly to us

RSP administration fee	$100	
Total charges associated with the operation of your account		**$100**
Commissions on purchases of mutual funds with a sales charge	$101	
Switch fees	$45	
Total charges associated with transactions we executed for you		**$146**
Total charges you paid directly to us		**$246**

Compensation we received through third parties

Commissions from mutual fund managers on purchases of mutual funds (see note 1)	$503
Trailing commissions from mutual fund managers (see note 2)	$286
Total compensation we received through third parties	**$789**
Total charges and compensation we received in 20XX	**$1,035**

Notes:

1. When you purchased units of mutual funds on a deferred sales charge basis, we received a commission from the investment fund manager. During the year, these commissions amounted to $503.

2. We received $286 in trailing commissions in respect of securities you owned during the 12-month period covered by this report.

Investment funds pay investment fund managers a fee for managing their funds. The managers pay us ongoing trailing commissions for the services and advice we provide you. The amount of the trailing commission depends on the sales charge option you chose when you purchased the fund. You are not directly charged the trailing commission or the management fee. But, these fees affect you because they reduce the amount of the fund's return to you. Information about management fees and other charges to your investment funds is included in the prospectus or fund facts document for each fund.

Our current schedule of operating charges

[*As part of the annual report of charges and compensation, registrants are required to provide their current operating charges that may be applicable to their clients' accounts. For the purposes of this sample document, we are not providing such a list.*]

Appendix E Your investment performance report

For the period ending December 31, 2030

Investment account 123456789

Client name

Address line 1

Address line 2

Address line 3

This report tells you how your account has performed to December 31, 2030. It can help you assess your progress toward meeting your investment goals.

Speak to your representative if you have questions about this report. It is important that you tell your representative if your personal or financial circumstances have changed. Your representative can recommend adjustments to your investments to keep you on track to meeting your goals.

Amount invested means opening market value plus deposits including:

the market value of all deposits and transfers of securities and cash into your account, not including interest or dividends reinvested.

Less withdrawals including:

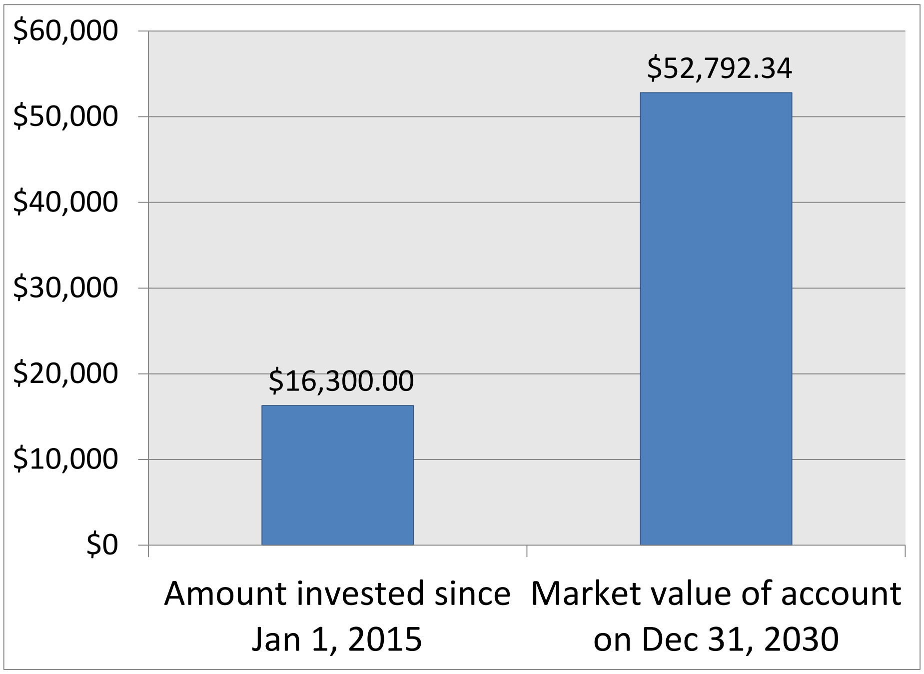
the market value of all withdrawals and transfers out of your account.

Total value summary

Your investments have increased by $36,492.34 since you opened the account

Your investments have increased by $2,928.85 during the past year

Amount invested since you opened	
your account on January 1, 2015	$16,300.00
Market value of your account on December 31, 2030	**$52,792.34**



Change in the value of your account

This table is a summary of the activity in your account. It shows how the value of your account has changed based on the type of activity.

	Past year	**Since you opened your account**
Opening market value	$51,063.49	$0.00
Deposits	$4,000.00	$21,500.00
Withdrawals	$(5,200.00)	$(5,200.00)
Change in the market value of your account	$2,928.85	$36,492.34
Closing market value	**$52,792.34**	**$52,792.34**

What is a total percentage return?

This represents gains and losses of an investment over a specified period of time, including realized and unrealized capital gains and losses plus income, expressed as a percentage.

For example, an annual total percentage return of 5% for the past 3 years means that the investment effectively grew by 5% a year in each of the 3 years.

Your personal rates of return

The table below shows the total percentage return of your account for periods ending December 31, 2030. Returns are calculated after charges have been deducted. These include charges you pay for advice, transaction charges and account-related charges, but not income tax.

Keep in mind your returns reflect the mix of investments and risk level of your account. When assessing your returns, consider your investment goals, the amount of risk you're comfortable with, and the value of the advice and services you receive.

	Past year	**Past 3 years**	**Past 5 years**	**Past 10 years**	**Since you opened your account**
Your account	5.51%	10.92%	12.07%	12.90%	13.09%

Calculation method

We use a money weighted method to calculate rates of return. Contact your representative if you want more information about this calculation.

The returns in this table are your personal rates of return. Your returns are affected by changes in the value of the securities you have invested in, dividends and interest that they paid, and also deposits and withdrawals to and from your account.

If you have a personal financial plan, it will contain a target rate of return, which is the return required to achieve your investment objectives. By comparing the rates of return you actually achieved (shown in the table) with your target rate of return, you can see whether you are on track to meet your investment objectives.

Contact your representative to discuss your rate of return and investment objectives.

Appendix F Part 14 Client reporting requirements and sole EMDs

This appendix discusses how the client reporting requirements in Part 14 may apply to some exempt market dealers that are not also registered as advisers or in another category of dealer (sole EMDs) as a result of their limited operating model.

Overview:

Holding client assets and other specified criteria

The applicability of some of the client statement requirements depends on whether a registered firm holds client assets (account statements) or, if it does not, whether certain other specific criteria apply (additional statements). Other client reporting requirements may or may not apply depending on whether a registered firm has a "client" at the relevant point in time (annual report on charges and other compensation, and annual report on investment performance).

Sole EMDs do not normally hold client assets and where that is the case, they can disregard provisions that only apply where client assets are held by a registered firm. In circumstances where a sole EMD holds client assets (as may be the case with mortgage syndications), it must deliver account statements with the information required under subsections 14.14(4) and 14.14(5) along with position cost information under section 14.14.2. Furthermore, since holding client assets is a clear indication of an ongoing client relationship, a sole EMD is also subject to the requirement to deliver an annual report on charges and other compensation under section 14.17 and an annual investment performance report under section 14.18.

Transactional vs ongoing client relationship

Some sole EMDs have only limited, transactional relationships with their clients – as opposed to the ongoing client relationships that are typical of most other registrants' operating models. An example of a transactional relationship would be where an EMD's relationship with a client is limited to a specific private placement transaction and does not involve

- a security specified in paragraph 14.14.1(1)(c)

- any trailer fee or similar ongoing compensation in relation to the client's ownership of a security

- the EMD holding client assets

- any expectation on the part of the EMD that there may be further transactions with the client or services provided to the client. For example, if an EMD regularly contacts the client regarding any securities offered by the EMD, this will be considered an ongoing relationship

- any expectation on the part of the client that the EMD will continue to provide services to the client after the completion of the transaction. The example described above applies in this case as well.

In this example, the EMD would be required to deliver one account statement with transactional information under subsection 14.14(4), but would not be required to deliver any

- further account statements under section 14.14
- additional statements under section 14.14.1
- position cost information under section 14.14.2
- annual report on charges and other compensation under section 14.17
- annual investment performance report under section 14.18

A sole EMD should consider carefully whether it is in an ongoing client relationship before concluding that any of the client statement requirements do not apply to it.

Section-by-section analysis:

Relationship disclosure information, pre-trade disclosure of charges and trade confirmation

A sole EMD always has a client at the time of the transaction and will be subject to other requirements relating to relationship disclosure (section 14.2), pre-trade disclosure of charges (section 14.2.1) and trade confirmations (section 14.12). However, if it has no other dealings with the investor, the EMD might conclude that it is no longer in a client relationship at the point in time when it would otherwise be required to prepare further client statements and reports, as discussed below.

Account statements

An account statement has two principal elements: transactional information and account position information. Transactional information is specific to the securities involved and is required in almost all circumstances where there has been a transaction. Account position information is a snap-shot of the whole account and is required only where the firm holds client assets.

Subsection 14.14(1) requires an EMD to deliver transactional information prescribed under subsection 14.14(4) to clients on a quarterly basis or, if so requested, each month. This requirement applies regardless of whether the firm holds client assets. For EMDs that hold client assets, account position information under subsection 14.14(5) is also required. Note that subsection 14.14(2) requires an EMD to deliver an account statement with transactional information under subsection 14.14(4) "after the end of ***any month*** in which a transaction was effected in securities ***held*** by the dealer in the client's account" [emphasis added].

The effect of these requirements is that, if one or more transactions occurred in the reporting period, a sole EMD must provide the client with an account statement with transactional information (but not account position information if no clients assets are held) either

- at the end of the month, if requested by a client, or

- at the end of the quarter, by default.

This applies even where an EMD does not have an ongoing client relationship.

Additional statements

An "additional statement" (registered firms subject to the requirements in section 14.14.1 are not required to call it this in client communications – "account statement" would do for those purposes) is the way clients get the equivalent of account position information where the registered firm does not hold their assets. It only applies in certain circumstances. More specifically, subsection 14.14.1(1) requires a registered dealer or adviser that does not hold client assets to provide an additional statement with account position information under subsection 14.14.1(2) on a quarterly basis if

- it has trading authority over the client's account in which the securities are held or were transacted (not, of course, applicable to a sole EMD),

- it receives certain continuing payments in respect of securities it traded for a client (e.g., trailing commission), or

- it is the dealer of record for a client's securities issued by a mutual fund or certain labour-sponsored investment vehicles (EMDs trading securities of an investment fund should be aware of the definition of "mutual fund" under securities legislation).

In effect, a registered firm is deemed to have an ongoing client relationship in these circumstances. If none of these circumstances apply, there is no requirement for a sole EMD to provide clients with an additional statement.

Position cost information

Subsection 14.14.2(1) requires quarterly delivery of position cost information under criteria which effectively mean that if a sole EMD has to provide account position information to a client, either in an account statement or an additional statement, it also has to provide position cost information to the client.

Annual report on charges and other compensation

Subsection 14.17(1) requires delivery of a report on charges and other compensation to a client every 12 months. It will apply if the sole EMD is subject to the requirement to provide account position information to a client, either in an account statement under subsection 14.14(5) or an additional statement under subsection 14.14.(1).

However, even if the requirement in subsection 14.17(1) is triggered, the EMD would not be required to send a "nil" report if it did not receive any of the specified charges or other compensation during the 12-month period.

Annual investment performance report

Subsection 14.18(1) requires annual delivery of an investment performance report to a client. Note that the elements of the performance report set out in section 14.19 will depend on market values that are contained in the account position information provided in the account statements and additional statements sent under sections 14.14 and 14.14.1, respectively. The effect of subsection 14.18(6) is that no investment performance report is required if a firm reasonably believes that either (a) there are no securities of a client in respect of which it would be required to provide account position information to a client, either in an account statement or an additional statement, or (b) if there are such securities, no market value can be determined for any of them.

Appendix G Part 13 – Addressing Issues of Financial Exploitation and Concerns About Clients' Mental Capacity

This appendix sets out how we interpret the requirements under sections 13.2.01 and 13.19 relating to trusted contact persons and temporary holds. This appendix also provides general commentary and guidance surrounding issues of financial exploitation of vulnerable clients, and concerns about clients' mental capacity to make decisions involving financial matters.

1. Financial exploitation

Financial exploitation of a client may be committed by any person. Examples of warning signs of financial exploitation of a client may include:

- unexplained or sudden withdrawals from accounts or account closures,
- unexplained changes in the risk profile of an account from low risk or capital preservation to high risk,
- sudden reluctance to discuss financial matters,
- being accompanied to meetings by new or unknown caregivers, friends or family members, or the registrant having difficulty communicating directly with the client without the involvement of others,
- sudden or unusual requests to change ownership of assets (for example, requesting that investments be transferred to a joint account held by family members, friends or caregivers),
- sudden or unexplained changes to legal or financial documents, such as a power of attorney (POA) or a will, or account beneficiaries,
- an attorney under a POA providing instructions that seem inconsistent with the client's pattern of instructions to the firm,
- unusual anxiety when meeting or speaking to the registrant (in-person or over the phone),
- unusual difficulty with, or lack of response to, communications or meeting requests,
- limited knowledge about their financial investments or circumstances when the client would have customarily been well informed in this area,
- increasing isolation from family or friends, or
- signs of physical neglect or abuse.

One warning sign alone may not be indicative of financial exploitation. Additionally, the warning signs listed above are not exhaustive; a registrant may notice other signs that are not listed above.

2. Vulnerable client

Vulnerable clients are those clients that might have an illness, impairment, disability or aging process limitation that places them at risk of financial exploitation. Registered firms and individuals should recognize that not all older clients are vulnerable or unable to protect their own interests. Vulnerability can affect a client of any age, take many forms, and can be temporary, sporadic or permanent in nature.

It is important to recognize vulnerabilities in clients because such vulnerabilities could make clients more susceptible to financial exploitation. While financial exploitation may be committed by any person, vulnerable clients may be especially susceptible to such exploitation by an individual who is close to the vulnerable client, such as a family member, friend, neighbour or another trusted individual such as an attorney under a POA, service provider or caregiver.

3. Mental capacity

Registrants can be in a unique position to notice the warning signs that a client lacks mental capacity to make decisions involving financial matters because of the interactions they have with the client, and the knowledge they acquire through the client relationship.

We acknowledge that registrants do not have the expertise to assess and determine whether clients lack mental capacity, and we do not expect registrants to make such a determination. However, where a registrant detects signs that a client lacks mental capacity to make decisions involving financial matters, the registrant may wish to take certain actions. For example, the registrant may wish to contact a trusted contact person or, in the case of a registered firm having formed a reasonable belief that the client lacks mental capacity to make decisions involving financial matters, place a temporary hold.

When considering whether one or more warning signs that a client lacks mental capacity to make decisions involving financial matters is present, registrants might consider, among others things, the client's ability to understand information that is relevant to their decision making and appreciate the reasonably foreseeable consequence of making or failing to make a decision. Examples of warning signs that a client lacks mental capacity to make decisions involving financial matters may include:

- memory loss, such as forgetting previously given instructions or repeating questions,

- increased difficulty completing forms or understanding disclosure documents,

- increased difficulty making decisions involving financial matters or understanding important aspects of investment accounts,

- confusion or unfamiliarity with previously understood basic financial terms and concepts,

- reduced ability to solve everyday math problems,

- exhibiting unfamiliarity with surroundings or social settings or missing appointments,

- difficulty communicating, including expressing their will, intent or wishes, or

- increased passivity, anxiety, aggression or other changes in mood or personality, or an uncharacteristically unkempt appearance.

We acknowledge that one sign alone may not be indicative of a client's lack of mental capacity and that signs may arise subtly and over time. The warning signs listed above are not exhaustive; a registrant may notice other signs that are not listed above. It is also important to note that mental capacity can fluctuate over time, is contextual and depends on the type of decision to be made.

4. Trusted contact person

Purpose of the trusted contact person

Subsection 13.2.01(1) requires registrants to take reasonable steps to obtain the name and contact information of a trusted contact person or "TCP" with whom they may communicate in specific circumstances in accordance with the client's written consent. Although this requirement only applies with respect to clients who are individuals, a registrant is not precluded from asking for TCP information from a non-individual client that, for example, is closely held and is part of an individual's personal investment plan.

A TCP is intended to be a resource for a registrant to assist in protecting a client's financial interests or assets when responding to possible circumstances of financial exploitation or concerns about a client's mental capacity. A TCP could also be utilized by the registrant to confirm or make inquiries about the name and contact information of a legal representative of the client, including a legal guardian of the client, an executor of an estate under which the client is a beneficiary, or a trustee of a trust under which the client is a beneficiary.

A client may name more than one TCP on their account.

While there is no requirement for the TCP to be at or over the age of majority, registrants should encourage their clients to name as the TCP an individual who is trusted, is mature and has the ability to communicate and engage in potentially difficult conversations with the registrant about the client's personal situation.

A TCP does not replace or assume the role of a client-designated attorney under a POA, nor does a TCP have the authority to transact on the client's account or to make any other decision on behalf of the client by virtue of being named a TCP. A client-designated attorney under a POA can be named as a TCP, but clients should be encouraged to select an individual who is not involved in making decisions with respect to the client's account. A TCP should not be the client's dealing representative or advising representative on the account.

Obtaining trusted contact person information and consent

There is no prescribed form for obtaining TCP information. Registrants may wish to develop a stand-alone form or incorporate the information into an existing form such as an account application form. The stand-alone form or relevant sections of an existing form might include:

- an overview of the circumstances under which the registrant may contact the TCP,

- space to document information about the TCP, including the TCP's name, mailing address, telephone number, email address and nature of the relationship with the client,

- a signature box to document the client's consent to contact the TCP,

- a statement that confirms the client's right to withdraw consent to contact the TCP, and

- a description of how to change a TCP.

Understanding the nature of the relationship between the client and the TCP may provide insight into the support network that the client has so that the registrant can assess whether it is appropriate to contact the TCP. Also, demonstrating that the registrant has knowledge of the relationship between the client and the TCP may alleviate concerns the TCP may have about speaking to the registrant about the client.

Registrants are not prevented from opening and maintaining a client account if the client refuses or fails to identify a TCP; however, they must still take reasonable steps to obtain the information as part of the know your client or "KYC" process. Examples of reasonable steps include explaining to the client the purpose of a TCP, providing the client with the disclosure required by paragraph 14.2(2)(l.1), and asking the client to provide the name and contact information of a TCP. If a client refuses to provide the name and contact information for a TCP, the registrant may make further inquiries about the reasons for the refusal. Registered firms are reminded of the requirement to maintain records which demonstrate compliance with section 13.2.01, document correspondence with clients, and document compliance, training and supervision actions taken by the firm, under paragraphs 11.5(2)(l), (n) and (o), respectively.

Updating trusted contact person information

Under subsection 13.2.01(2), registrants are required to take reasonable steps to keep the TCP information current. Registrants are expected to update the TCP information as part of the process to update KYC information. In a situation where a client may have previously refused to provide TCP information, at each update, registrants should ask such clients if they would like to provide the information.

Contacting the trusted contact person and other parties

When concerns about financial exploitation or mental capacity to make decisions involving financial matters arise, registrants should speak with the client about concerns they have with the client's account or wellbeing before contacting others, including the TCP.

Although there is no requirement to notify a TCP that they have been named by a client, registrants should encourage their clients to notify their TCP that they have been named and explain that the TCP will only be contacted in specific circumstances in accordance with the client's written consent.

If the client's consent has been obtained, a registrant might contact a TCP if the registrant notices signs of financial exploitation or if the client exhibits signs that they lack mental capacity to make decisions involving financial matters. Examples of warning signs of financial exploitation and a lack of mental capacity are discussed in sections 1 and 3 of this appendix. If the TCP is suspected of being involved in the financial exploitation of the client, the TCP should not be contacted and consideration should be given as to whether there are other more appropriate resources from which to seek assistance, such as the police, the public guardian and trustee or an alternative TCP, if named. A registrant might also contact the TCP to confirm the client's contact information if the registrant is unsuccessful in contacting the client after repeated attempts and where failure to contact the client would be unusual. A registrant may also ask the TCP to confirm the name and contact information of a legal guardian, executor, trustee, an attorney under a POA or any other legal representative.

When contacting a TCP, registrants should be mindful of privacy obligations under applicable privacy legislation and client agreements relating to the collection, use and disclosure of personal information.

Notwithstanding that the client has named a TCP, a registrant may also contact an attorney under a POA, government organizations, departments or individuals (including police, or the public guardian and trustee) that they might otherwise consult with in instances where the registrant suspects financial exploitation or has concerns about a client's mental capacity to make decisions involving financial matters.

Policies and procedures

We expect registered firms to have written policies and procedures in respect of TCPs. These policies and procedures should address:

- how to collect and document TCP information and keep this information up-to-date,

- how to obtain the written consent of a client to contact their TCP, and document any restrictions on contacting the TCP and what type of information can be shared,

- the specific circumstances in which a registrant may wish to contact a TCP,

- how to document discussions with a TCP, and

- circumstances where a decision to contact a TCP must be escalated for review (for example, to the CCO or to authorized and qualified supervisory, compliance or legal staff), and how to document this review.

Having written policies and procedures that address situations that may result in contacting a TCP or placing a temporary hold under section 13.19 will help the registered firm demonstrate that it has a system of controls and supervision in accordance with section 11.1.

5. Temporary Holds

General principles

Registered firms and individuals can be in a unique position to notice signs of financial exploitation, vulnerability and a lack of mental capacity in clients because of the interactions they have with them, and the knowledge they acquire through the client relationship. Yet, many firms and individuals express concerns about acting to protect their clients, particularly by placing temporary holds, fearing regulatory repercussion. The intent of section 13.19 is to clarify that if a registered firm reasonably believes that financial exploitation of a vulnerable client has occurred, is occurring, has been attempted or will be attempted, or that a client lacks mental capacity to make decisions involving financial matters, there is nothing in securities legislation that prevents the firm or its registered individuals from placing a temporary hold that they are otherwise legally entitled to place. Section 13.19 also prescribes requirements on how temporary holds in these circumstances must be placed. We acknowledge that there may be other circumstances under which a registered firm and its registered individuals may want to place a hold on an account. Section 13.19 and this guidance do not address these circumstances.

When placing temporary holds in accordance with section 13.19, registered firms and their registered individuals must act in a manner that is consistent with their obligation to deal fairly, honestly and in good faith with their clients. Registered firms and their registered individuals must not use a temporary hold for inappropriate reasons, for example, to delay a disbursement for fear of losing a client. Before a temporary hold is placed, the registered firm must reasonably believe that either financial exploitation of a vulnerable client has occurred, is occurring, has been attempted or will be attempted, or the client does not have the mental capacity to make decisions involving financial matters. Decisions to place temporary holds should be made by the CCO or authorized and qualified supervisory, compliance or legal staff.

We do not expect registered firms and their registered individuals to be the final arbiter in matters of vulnerability, financial exploitation or mental capacity, but rather, believe that they may want to place temporary holds in these circumstances so that they can take steps to protect their clients.

A temporary hold contemplated under section 13.19 is not intended as a hold on the entire client account, but rather as a temporary hold over a specific purchase or sale of a security or withdrawal or transfer of cash or securities from a client's account. Transactions unrelated to the suspected financial exploitation or lack of mental capacity should not be subject to the temporary hold. Each purchase or sale of a security or withdrawal or transfer of cash or securities should be reviewed separately. If the transaction, withdrawal or transfer involves all the assets in the account, it may be reasonable to place a temporary hold on the entire account while not limiting the payment of regular expenses.

A temporary hold contemplated under section 13.19 is not intended to be available where a registrant has decided not to accept a client order or instruction that does not, in their view, meet the criteria for a suitability determination. In this circumstance, the registrant must comply with the requirements set out in subsection 13.3(2.1).

A client may provide an instruction to take an investment action which would not, in the registrant's view, meet the criteria for suitability determination and which may otherwise be considered a poor financial decision; however, these facts alone do not necessarily mean that financial exploitation of a vulnerable client has occurred, is occurring, has been attempted or will be attempted, or that the client lacks mental capacity to make decisions involving financial matters.

Conditions for temporary hold

Section 13.19 contains the steps that a registered firm must take if it or its registered individuals place a temporary hold. These steps, when taken in good faith, are consistent with the obligation to deal fairly, honestly and in good faith with the client.

We expect registered firms to have written policies and procedures in respect of temporary holds. These policies and procedures should:

- set out detailed warning signs of financial exploitation of a vulnerable client, and signs of a lack of mental capacity of a client to make decisions involving financial matters,

- clearly delineate firm and individual responsibilities for addressing concerns of financial exploitation of a vulnerable client or a lack of mental capacity of a client, such as:

  - who at the firm is authorized to place and revoke a temporary hold, for example, the CCO or authorized and qualified supervisory, compliance or legal staff;

  - who at the firm is responsible for supervising client accounts when a temporary hold is in place,

- set out the steps to take once a concern regarding financial exploitation of a vulnerable client, or a lack of mental capacity of a client, has been identified, such as:

  - escalating the concern;

  - proceeding or not proceeding with the instructions,

- establish lines of communication within the firm to ensure proper reporting, and

- outline when suspected abuse of a POA should be escalated to the appropriate external authorities, for example the public guardian and trustee or local law enforcement pursuant to section 331 of the *Criminal Code* (R.S.C., 1985, c. C-46).

Under paragraph 13.19(3)(a), when documenting the facts and reasons that caused the registered firm or its registered individuals to place and, if applicable, to continue the temporary hold, the firm is expected to include signs of financial exploitation and client vulnerability, or a lack of mental capacity of a client to make decisions involving financial matters, that were observed. As the signs of financial exploitation, vulnerability, and declining mental capacity often appear and change over a period of time, it is important to document signs and interactions with the client, the client's representatives, family or other individuals which led to the decision to place and, if applicable, to continue the temporary hold.

Under paragraph 13.19(3)(b), the registered firm must, as soon as possible, provide notice of the temporary hold and the reasons for the temporary hold to the client. While firms often opt to send written notice, there may be circumstances where they may also want to attempt to contact the client verbally. In cases of financial exploitation, the person perpetrating the exploitation may be withholding the client's mail. Additionally, if a client is experiencing a decline in mental capacity, they may not be reviewing their mail on a regular basis. Firms should be as transparent as possible with their clients about the reasons for placing the temporary hold, and be mindful of their obligation to deal fairly, honestly and in good faith with their clients.

Under paragraph 13.19(3)(c), once a registered firm or a registered individual places a temporary hold, the firm must, as soon as possible after placing the temporary hold, and on a reasonably frequent basis, review the relevant facts to determine if continuing the hold is appropriate. This review should include verifying whether the reasons for placing the temporary hold are still present, and considering any other information that is relevant to determining whether continuing the hold is appropriate. The review may prompt the registered firm to review account activity or initially contact or follow up with other parties who could provide assistance to the client, such as an attorney under a POA, a TCP, or provincial or federal government organizations and services such as the police, public guardian and trustee, which may be conducting their own review, or provincial seniors advocate offices. Firms may also consider whether there are other trusted friends and family in the client's network that could assist the client, for example, by accompanying the client to meetings. Before contacting another party, the firm should consider whether there may be a risk that the other party is involved in the financial exploitation of the vulnerable client. The review conducted under paragraph 13.19(3)(c) and, if applicable, the reasons for continuing the temporary hold are required to be documented under paragraph 13.19(3)(a).

While there is no requirement for firms to contact a TCP prior to or when a temporary hold is placed, firms may wish to contact a TCP at this point for a number of reasons, if they have not already done so, as outlined in the guidance in section 4 of this appendix. However, before contacting the TCP, firms should assess whether there is a risk that the TCP is a perpetrator of the exploitation. If the firm suspects that the TCP is involved in the financial exploitation, a notification to the TCP may have detrimental effects on the client.

For clarity, the fact that a client has not named a TCP does not preclude a firm from placing a temporary hold in accordance with section 13.19.

Before contacting any third party with the intent of sharing or obtaining personal information regarding a client, firms should assess their obligations under applicable privacy legislation and client agreements.

Paragraph 13.19(3)(d) requires that every 30 days, the firm either notifies the client of its decision to continue the temporary hold, or revokes the temporary hold. If the firm decides to continue the temporary hold, it must also provide the client with the reasons for its decision. Firms should be as transparent as possible with their clients about the reasons for continuing the temporary hold, and be mindful of their obligation to deal fairly, honestly and in good faith with their clients.

If the registered firm no longer has a reasonable belief that financial exploitation of a vulnerable client has occurred, is occurring, has been attempted or will be attempted, or no longer has a reasonable belief that their client does not have the mental capacity to make decisions involving financial matters, the temporary hold must end. If ending the temporary hold would result in an investment action that requires a suitability determination, such a determination will be required. A firm may also decide to end the temporary hold for other reasons, such as if it decides to accept the client instructions with respect to the transaction, withdrawal or transfer, or alternatively, decides not to accept the client's instructions.

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