

Summary of Public Comments Respecting Proposed Amendments to MFDA Rules 2.8.3 (Rates of Return), 5.3 (Client Reporting) and 5.4 (Trade Confirmations) and Responses of the MFDA

On June 12, 2014, the British Columbia Securities Commission (“BCSC”) published for public comment proposed amendments to MFDA Rules 2.8.3 (Rates of Return), 5.3 (Client Reporting) and 5.4 (Trade Confirmations) (the “**Proposed Amendments**”) for a 90-day public comment period that expired on September 10, 2014.

Nine submissions were received during the public comment period:

1. Kenmar Associates (“Kenmar”) (submission dated June 20, 2014);
2. Kenmar (submission dated September 15, 2014);
3. Tangerine Investments (“Tangerine”);
4. Canadian Foundation for Advancement of Investor Rights (“FAIR Canada”);
5. B2B Bank Financial Services (“B2B”);
6. Royal Mutual Funds Inc. / Phillips, Hager & North Investment Funds Ltd. (“RMFI / PH&N IF”);
7. The Investment Funds Institute of Canada (“IFIC”);
8. Univeris Corporation (“Univeris”); and
9. The Small Investor Protection Association (“SIPA”).

Copies of the comment submissions may be viewed on the MFDA website at: <http://www.mfda.ca/regulation/comments.html>

The following is a summary of the comments received, together with the MFDA's responses.

General Comments

Three commenters generally supported the proposed conforming MFDA Rule amendments, noting that providing information to investors before the purchase of a security and providing meaningful account statements after the purchase are essential components for increasing an investor's ability to make informed decisions.

MFDA Response

We acknowledge these comments, including those expressing support for the proposed amendments. The purpose of the proposed amendments is to ensure that requirements under MFDA Rules are consistent with those introduced into NI 31-103 as a result of Phase 2 of the CSA's CRM2 amendments.

Client Reporting (Rule 5.3)

Definitions

One commenter referenced the definition of “trailing commission”, set out under proposed Rule 5.3(1)(f), noting that the definition is inaccurate, meaningless and needs to be reworked. This commenter also noted that disclosure regarding the payment of trailing commissions, as set out under proposed Rule 5.3.3(1)(g), also needs to be reworked.

Content of Account Statement

One commenter sought clarification and raised comments in respect of the following requirements under the proposed amendments:

- i. Clarification was sought as to whether reference to “the date of the transaction”, as set out under proposed Rule 5.3.2(b)(i), is intended to mean Trade Date or an alternative date;
- ii. The commenter noted that the requirement for account statements to disclose the total cost of all investment positions, as set out under proposed Rule 5.3.2(c)(ii), is in conflict with section 5.3(1)(a)(i) and (ii). Specifically, the commenter indicated that the definitions for “book cost” and “original cost” allow presentation a) per unit/share or b) on an aggregate basis (taken to mean value per unit/share x number of units held). In this regard, if the member decides to report per unit/share, clarification was sought as to how the Member would present a total of these values for all investment positions in an account;
- iii. The commenter also asked the purpose of presenting book cost at an aggregate for an account, noting that it would have no real meaning to an investor;
- iv. Clarification was sought in respect of: “*the name of the party that holds or controls each security and a description of the way it is held*”, as set out under proposed Rule 5.3.2(c)(ii)(H).

Disclosure of MFDA IPC Coverage

A commenter referenced the requirement under proposed Rule 5.3.2(e) for account statements to include disclosure respecting MFDA IPC coverage. Clarification was sought as to the specific content of the disclosure and where such disclosure should be located on the account statement.

MFDA Response

Definitions

MFDA Rules are required to conform to requirements under NI 31-103. We note that the definition of “trailing commission” and disclosure regarding the payment of trailing commissions, as referred to by the commenter, have been adopted directly from NI 31-103.

Content of Account Statement

With respect to the questions raised by the commenter, we note as follows:

- i. For the purpose of requirements under the proposed amendments, “date of the transaction” is intended to mean trade date;
- ii. The requirement for reporting total cost of all investment positions is not in conflict with proposed Rule 5.3(1)(a)(i) and (ii). Under Rule 5.3.2(c)(ii)(C), Members can present the cost of each investment position on an average cost per unit or share basis or on an aggregate basis. However, in providing the total cost of all investment positions, as required under Rule 5.3.2(c)(ii)(D), the information must be presented on an aggregate basis;
- iii. The purpose of requiring book cost to be presented on an aggregate basis for an account is to provide clients with a source of cost comparison to total market value;
- iv. We acknowledge the comment and will provide future guidance in respect of this matter.

Account Statement Disclosure of MFDA IPC Coverage

We note that the Board of the MFDA IPC has approved wording for the purpose of meeting the disclosure requirement under proposed Rule 5.3.2(e). Staff will, shortly, be issuing a Notice that sets out the approved wording. The Notice will also advise Members that the disclosure will be required to be included on Member account statements as of July 15, 2015, when Rule 5.3.2(e) becomes effective.

The proposed amendments do not prescribe where MFDA IPC disclosure should be located on the account statement.

Report on Charges and Other Compensation (Rule 5.3.3)

Scope of Reporting

A commenter recommended that requirements under this Rule be expanded to include all investments and not just securities, so as to be consistent with performance reporting requirements under the proposed amendments.

Application of Requirements to Carrying Dealers

A commenter sought clarification with respect to the application of requirements under proposed Rule 5.3.3 (Report on Charges and Other Compensation) to introducing/carrying dealer arrangements in circumstances where fees, commissions and payments paid to the introducing dealer are not received by, processed through or known to the carrying dealer. By way of example, the commenter noted: trailing commissions, referral fees; payments other than trailing commissions where the payout amount per account is not readily available or easy to calculate; and other types of fees/commissions not transacted through the dealer.

Report Content / Consolidated Reporting

A commenter sought clarification in respect of “*the Member’s current operating charges which might be applicable to the client’s account*”, as set out under Rule 5.3.3(1)(a).

The commenter also noted that it is unclear why a separate Report on Charges and Other Compensation is required for each account. The commenter suggested that a consolidated report be allowed without client consent with the requirement of Section 5.3.3(3)(b) always applying. The commenter made the same comment in respect of Policy No. “X”, (General Requirements).

MFDA Response

Scope of Reporting

Where reliable data is available, we encourage Members to provide charges and compensation information in respect of other investment products transacted through, or transferred into, the Member. However, as set out in the Publication Notice, obtaining reliable data from product issuers in respect of all investment products might present challenges, particularly as other issuers are not subject to the jurisdiction of securities regulators. To address this issue, the proposed amendments require, where the charges and compensation report does not include all compensation received, in respect of investments that are not securities, that Members provide disclosure making clients aware of this fact.

Application of Requirements to Carrying Dealers

As set out under proposed MFDA Rule 5.3.5, and similar requirements under NI 31-103, the Report on Charges and Other Compensation may be combined with or accompany the account statement or may be delivered within 10 days after the delivery of the account statement.

The Report on Charges and Other Compensation must contain consolidated information respecting the charges and compensation earned by both the introducing dealer and carrying dealer during the period covered by the report. To allow for such consolidated reporting, it may become necessary for the introducing dealer and carrying dealer to develop systems and procedures to facilitate the sharing of information between each of them. We will work with carrying dealers to assist them in implementing requirements under the proposed amendments.

Content and Consolidated Reporting

Rule 5.3.3(1)(a) requires the Member to provide disclosure respecting the Member's current fee schedule, so that clients are aware of the charges that they may incur going forward.

Rule 5.3.3(3) and section (2) of Policy No. "X" (General Requirements) permit consolidated reporting, for more than one of a client's accounts, where the client has consented in writing and the consolidated report specifies which accounts it consolidates. Where a client has multiple accounts, it is important that the client be able to understand how reported charges are attributable to each of those accounts. Client consent is required as some clients may find it easier to understand, or otherwise prefer to receive, such information on a non-consolidated basis.

Performance Reporting (Rule 5.3.4)

Performance Reporting Inception Date

Three commenters referenced performance reporting requirements under proposed Rule 5.3.4 (Performance Report) and noted that client confusion could be caused by the proposed performance reporting inception date of July 15, 2015. To avoid such confusion, these commenters recommended that Members be given the option to align the performance reporting inception date with the beginning of a calendar year.

Treatment of GICs

A commenter noted that the proposed amendments do not address the valuation of investment products that are not securities. In this regard, the commenter sought clarification that its treatment of guaranteed investment certificates ("GICs"), for the purpose of valuation and inclusion in performance reporting, was consistent with industry standards.

Policy No. “X”

A commenter expressed the view that proposed performance reporting requirements set out under Policy No. “X” should be relocated within MFDA Rules, so as to have *rules* that are substantially similar to those made under the Phase 2 CRM2 amendments to NI 31-103. Additionally, the commenter noted that it is not clear that MFDA Policies are regarded by Members as being binding Rules.

A commenter asked whether it is intentional that the content requirements for the Performance Report, as set out under Policy No. “X”, overlap the content requirements for the Account Statement.

MFDA Response

Performance Reporting Inception Date

We have made appropriate amendments to proposed Policy No. “X” (Performance Reporting) that will allow Members to adopt an earlier performance reporting inception date, subject to the requirements set out in such amendments.

Treatment of GICs

Members currently report the market value of GICs as the principal amount plus accrued interest earned as at the end of the account statement period. This method of reporting will continue to be permitted under the proposed amendments.

Under the proposed amendments, changes have been made to MFDA Form 1, Part 5 (Market Value of a Security). These changes include requirements prescribed under NI 31-103 respecting the determination of market value. Form 1, Part 5, as amended, is based on the International Financial Reporting Standards (“IFRS”) hierarchy approach to assessing the fair value of financial instruments. Accordingly, when determining the market value of investments, Members should consider both IFRS fair value standards and the “market value of a security” definition set out under Form 1, as revised.

We will consider the matters raised by the commenter in the development of future guidance. Where Members require additional guidance and clarification respecting the valuation of any investment product, for the purpose of meeting reporting requirements under the proposed amendments, we would encourage Members to discuss such matters with MFDA staff.

Policy No. “X”

As set out in the Publication Notice accompanying the proposed amendments, NI 31-103 contains detailed requirements in respect of performance reporting. In an effort to ensure that the proposed amendments remain relatively consistent with the current structure and

format of the MFDA Rulebook, some of these requirements have been adopted in proposed new Policy No. “X” (Performance Reporting). Members are required to comply with the minimum standards set out under MFDA Policies. The prescriptive nature of MFDA Policies is reflected in Appendix H to NI 31-103 (Exemptions from Certain Requirements for MFDA Members), which sets out the MFDA requirements that must be complied with by MFDA Members to be exempt from corresponding provisions of the National Instrument. In addition to MFDA Rules, requirements under MFDA Policies are also cited. By way of example, we note that MFDA Policy No. 2 (Minimum Standards for Account Supervision) is our most frequently used and cited Policy. Violations of MFDA Policies are also frequently cited in MFDA enforcement hearings. Amendments to MFDA Policies are also subject to the approval of the recognizing securities regulators.

In addition to the foregoing, and as set out in the proposed amendments, we note that compliance with requirements under Policy No. “X” is prescribed under Rule 5.3.4.

Overlap in Account Statement and Performance Report Content

The performance report is intended to be a document that clients can understand without the need to refer to any other documents (i.e. clients should not have to refer to any other client statement to be able to understand the performance report). As a result, information on the account statement that is used in the performance reporting calculation (i.e. market value at the beginning and end of the 12 month reporting period) has been reproduced on the performance report.

Exempt Market Dealers and Scholarship Plan Dealers – Client Reporting (Rule 5.3.6)

A commenter recommended that Rule 5.3.6 be clarified so that it is clear that, in addition to requirements under MFDA Rules, Members also registered as exempt market dealers are subject to any additional client reporting requirements applicable to exempt market dealers and scholarship plan dealers, as set out under securities legislation.

MFDA Response

The recommendation made by the commenter is already addressed under the amendments, as proposed. Proposed Rule 5.3.6 currently requires that: *“the Member must comply with any additional client reporting requirements applicable to exempt market dealers and scholarship plan dealers, as set out under securities legislation.”* MFDA staff will be issuing a Notice that provides guidance and clarification in respect of reporting obligations, as set out under NI 31-103, for Members that are also registered as exempt market dealers and scholarship plan dealers.

Trade Confirmations (Rule 5.4)

A commenter referenced trade confirmation content requirements under proposed Rule 5.4.3(m) that would require disclosure as to whether the security was issued by a related or connected issuer. It was noted that “connected issuer” and “related issuer” are technical terms that the MFDA should define in its final Rules. Where a definition is adopted, the commenter asked that the MFDA specify if these terms are to be defined in the same manner as under National Instrument 33-105 *Underwriting Conflicts*. Additionally, it was noted that, under section 14.12(3)(b) of NI 31-103, trade confirmation disclosure respecting related and connected issuers does not have to be provided where the names of the dealer and mutual fund are sufficiently similar to indicate that they are affiliated or related. The commenter recommended that the proposed amendments adopt a similar exemption.

MFDA Response

We have amended the Definitions section of Rule 5.3 to include definitions of “connected issuer” and “related issuer”, as set out under NI 31-103. We have also amended trade confirmation requirements under Rule 5.4.3 to include the exemption set out under section 14.12(3)(b) of NI 31-103.

Comments on Additional Amendments to Rule 2.4.4 (Transaction Fees or Charges)

Transaction Fees or Charges (Rule 2.4.4)

Three commenters recommended that pre-trade disclosure of charges require disclosure of the dollar and cents amounts of trailing commissions.

Two of these commenters referenced proposed additional amendments to Rule 2.4.4 that would make disclosure requirements under the Rule consistent with similar requirements under NI 31-103, by limiting Rule 2.4.4 disclosure requirements to transactions in securities. One of these two commenters expressed the view that the existing scope of the Rule should not be narrowed and that the proposed changes to Rule 2.4.4 should apply to all investments, not just securities.

MFDA Response

Transaction Fees or Charges (Rule 2.4.4)

Trailing Commission Disclosure

The disclosure required under Rule 2.4.4 is intended to give clients a reasonable idea of fees and charges that will apply at the time of the transaction and is not intended to impair the timely execution of client orders. In meeting the requirements of Rule 2.4.4, Members and Approved Persons are expected to act reasonably and in the best interests

of clients and provide the most current and accurate information in respect of fees and charges that can be reasonably provided in the circumstances. There may be circumstances where specific information (such as an exact dollar figure) may not be available at the time of the transaction. To the extent that the client requests more specific information, the Member or Approved Person may obtain the client's instruction to delay the execution of the transaction until more detailed information regarding applicable fees and charges can be provided.

Scope of Rule 2.4.4

We have made certain drafting changes to Rule 2.4.4. These changes clarify that Members are required to provide clients with disclosure in respect of any transaction charges paid to the Member, regardless of the type of investment, and charges in respect of the purchase or sale of a security. "Transaction charges" are amounts charged by the Member and, thus, known to the Member (e.g. switch fees or transaction fees). Disclosure of "charges in respect of the purchase or sale of a security" would include charges paid to a securities issuer in respect of a transaction (e.g. short-term trading fees or redemption fees).

DOCs#392791v7