

## MUTUAL FUND DEALERS ASSOCIATION OF CANADA

### PROPOSED AMENDMENT TO FORM 1

#### I. OVERVIEW

##### A. Current Form

The MFDA recently amended its financial reporting form, Form 1 – *Financial Questionnaire and Report* (“Form 1”) to align it with International Financial Reporting Standards (“IFRS”), except as modified by the MFDA. The new Form 1 was approved by the Recognizing Regulators on January 21, 2011 for implementation by Members commencing with their fiscal years beginning on or after January 1, 2011.

The definition of “market value” was not included in the previous version of Form 1, as it was already defined in Canadian Generally Accepted Accounting Principles (“CGAAP”) as “the amount obtainable from the sale, or payable on the acquisition, of a financial instrument in an active market”. In the rare case where Members may hold securities for which there is no active market, Members would be expected to use the definition set out in the Investment Industry Regulatory Organization of Canada’s (“IIROC”) Form 1.

##### B. The Issues

As "market value" does not exist under IFRS and has been replaced with "fair value", staff of the Recognizing Regulators have requested that the MFDA amend Form 1 to include a definition of "market value".

##### C. Objectives

The objective of the proposed amendment is to explicitly include the definition of “market value” in Form 1 to ensure consistency by MFDA Members in the valuation of their securities.

##### D. Effect of Proposed Amendment

The proposed amendment will clarify the definition of “market value” and ensure that MFDA Members value their securities on a consistent basis, and will harmonize the definition with that used by members of IIROC.

#### II. DETAILED ANALYSIS

##### A. Proposed Amendment

The proposed definition of “market value”, which is the same as the definition contained in the

IIROC's Form 1, has been added to the General Notes and Definitions section of Form 1 as follows:

**"market value of securities"** means:

1. for listed securities, the last bid price of a long security and, correspondingly, the last ask price of a short security, as shown on the exchange quotation sheets as of the close of business on the relevant date or last trading date prior to the relevant date, as the case may be, subject to an appropriate adjustment where an unusually large or unusually small quantity of securities is being valued. If not available, the last sale price of a board lot may be used. Where not readily marketable, no market value shall be assigned.
2. for unlisted and debt securities, and precious metals bullion, a value determined as reasonable from published market reports or inter-dealer quotation sheets on the relevant date or last trading day prior to the relevant date, or based on a reasonable yield rate. Where not readily marketable, no market value shall be assigned.
3. for commodity futures contracts, the settlement price on the relevant date or last trading day prior to the relevant date.
4. for money market fixed date repurchases (no borrower call feature), the market price is the price determined by applying the current yield for the security to the term of maturity from the repurchase date. This will permit calculation of any profit or loss based on the market conditions at the reporting date. Exposure due to future changes in market conditions is covered by the margin rate.
5. for money market open repurchases (no borrower call feature), prices are to be determined as of the reporting date or the date the commitment first becomes open, whichever is the later. Market price is to be determined as in 4 and commitment price is to be determined in the same manner using the yield stated in the repurchase commitment.
6. for money market repurchases with borrower call features, the market price is the borrower call price.

## **B. Issues and Alternatives Considered**

No other alternatives were considered.

## **C. Comparison with Similar Provisions**

As noted above, the proposed definition of "market value" is the same as the definition contained in the IIROC's Form 1.

**D. Systems Impact of Proposed Amendment**

The proposed amendment is not anticipated to result in a significant systems impact to Members.

**E. Best Interests of the Capital Markets**

The Board has determined that the proposed amendment is in the best interests of the capital markets.

**F. Public Interest Objective**

The proposed amendment is in the public interest as it will ensure a consistent valuation method among mutual fund and investment dealers that are Members of a self-regulatory organization, as it relates to the firms' own security positions and thus capitalization of the firm.

**III. COMMENTARY**

**A. Filing in Other Jurisdictions**

The proposed amendment will be filed for approval with the Alberta, British Columbia, Manitoba, New Brunswick, Nova Scotia, and Ontario Securities Commissions and the Saskatchewan Financial Services Commission.

**B. Effectiveness**

The proposed amendment is simple and effective.

**C. Process**

The proposed amendment has been prepared in consultation with relevant departments within the MFDA and has been reviewed by the Regulatory Issues Committee of the Board. The MFDA Board of Directors approved the proposed amendment on March 8, 2011.

**D. Effective Date**

The proposed amendment will be effective on a date to be subsequently determined by the MFDA.

**IV. SOURCES**

MFDA Form 1

**V. REQUIREMENT TO PUBLISH FOR COMMENT**

The MFDA is required to publish for comment the proposed amendment so that the issues referred to above may be considered by the Recognizing Regulators.

**The MFDA has determined that the entry into force of the proposed amendment would be in the public interest and is not detrimental to the capital markets. Comments are sought on the proposed amendment.** Comments should be made in writing. One copy of each comment letter should be delivered within **60** days of the publication of this notice, addressed to the attention of the Corporate Secretary, Mutual Fund Dealers Association of Canada, 121 King St. West, Suite 1000, Toronto, Ontario, M5H 3T9 and one copy addressed to the attention of Sarah Corrigan-Brown, Senior Legal Counsel, British Columbia Securities Commission, 701 West Georgia Street, P.O. Box 10142, Pacific Centre, Vancouver, British Columbia, V7Y 1L2.

Those submitting comment letters should be aware that a copy of their comment letter will be made publicly available on the MFDA website at [www.mfda.ca](http://www.mfda.ca).

Questions may be referred to:

Paige Ward  
Director, Policy & Regulatory Affairs  
Mutual Fund Dealers Association of Canada  
(416) 943-5838

DOCs#246082

## Schedule "A"

### MUTUAL FUND DEALERS ASSOCIATION OF CANADA

#### FORM 1

On March 8, 2011, the Board of Directors of the Mutual Fund Dealers Association of Canada made the following amendment to Form 1:

#### FORM 1 – GENERAL NOTES AND DEFINITIONS

##### GENERAL NOTES:

1. Each Member must comply with the requirements in Form 1 as approved and amended from time to time by the board of directors of the Mutual Fund Dealers Association of Canada (the Corporation).

Form 1 is a special purpose report that includes financial statements and schedules, and is to be prepared in accordance with International Financial Reporting Standards (IFRS), except as prescribed by the Corporation. Each Member must complete and file all of these statements and schedules.

2. The following are Form 1 IFRS departures as prescribed by the Corporation:

	<b>Prescribed IFRS departure</b>
Trading balances	When reporting trading balances relating to Member and client securities and other investment transactions, the Corporation allows the netting of receivables from and payables to the same counterparty.
Preferred shares	Preferred shares issued by the Member and approved by the Corporation are classified as shareholders' capital.
Presentation	Statements A and D contain terms and classifications (such as allowable and non-allowable assets) that are not defined under IFRS. In addition, specific balances may be classified or presented on Statement A and D in a manner that differs from IFRS requirements. The General Notes and Definitions, and the applicable Notes and Instructions to the Statements, should be followed in those instances where departures from IFRS presentation exists.  Statements B, C, E and F are supplementary financial information, which are not statements contemplated under IFRS.
Separate financial statements on a non-consolidated basis	Consolidation of subsidiaries is not permitted for regulatory reporting purposes except for related companies that meet the definition of "related Member" in MFDA By-law No. 1 and the Corporation has approved the consolidation.  Because Statement D only reflects the operational results of the Member, a Member must not include the income (loss) of an investment accounted for by the equity method.
Statement of cash flow	A statement of cash flow is not required as part of Form 1.
Valuation	Securities are to be valued and reported at "market value".

3. The following are Form 1 prescribed accounting treatments based on available IFRS alternatives:

	<b>Prescribed accounting treatment</b>
Hedge accounting	Hedge accounting is not permitted for regulatory reporting purposes. All security and derivative positions of a Member must be marked-to-market at the reporting date. Gains or losses of the hedge positions must not be deferred to a future point in time.
Securities owned and sold short as held-for-trading	A Member must categorize all investment positions as held-for-trading financial instruments. These security positions must be marked-to-market.  Because the Corporation does not permit the use of available for sale and hold-to-maturity categories, a Member must not include other comprehensive income (OCI) and will not have a corresponding reserve account relating to marking-to-market available for sale security positions.
Valuation of a subsidiary	A Member must value subsidiaries at cost.

4. These statements and schedules should be read in conjunction with the Corporation's Bylaws, Rules and Policies.
5. For purposes of these statements and schedules, the accounts of related companies that meet the definition of "related Member" in MFDA By-law No. 1 may be consolidated.
6. For purposes of the statements and schedules, the capital calculations must be on a trade date reporting basis unless specified otherwise in the Notes and Instructions to Form 1.
7. Comparative figures on all statements are required only at the audit date. As a transition exemption for the changeover to International Financial Reporting Standards (IFRS) from Canadian Generally Accepted Accounting Principles (CGAAP), Members are not required to file comparative information for the preceding financial year as part of the first audited Form 1 under IFRS.
8. All statements and schedules must be expressed in Canadian dollars and must be rounded to the nearest dollar.
9. Supporting details should be provided, as required, showing a breakdown of any significant amounts that have not been clearly described on the statements and schedules.
10. **Mandatory security counts.** Securities held in segregation and safekeeping must be counted once in the year in addition to the count as at the year-end audit date.
11. **Mandatory reconciliations.** Reconciliations must be performed monthly in addition to the year-end audit date between the Member's records and the records of the depository or custodian where the Member holds its own and client securities in nominee name accounts.

#### **DEFINITIONS :**

1. **"acceptable entity"** means:
  - (a) Acceptable institutions.
  - (b) Government of Canada, the Bank of Canada and Provincial Governments.
  - (c) Insurance companies licensed to do business in Canada or a province thereof.
  - (d) Canadian provincial capital cities and all other Canadian cities and municipalities, or their equivalents.

- (e) All crown corporations, instrumentalities and agencies of the Canadian federal or provincial governments which are government guaranteed as evidenced by a written unconditional irrevocable guarantee or have a call on the consolidated revenue fund of the federal or provincial governments.
- (f) Canadian pension funds which are regulated either by the Office of Superintendent of Financial Institutions or a provincial pension commission.
- (g) Corporations (other than Regulated Entities) with a minimum net worth of \$75 million on the last audited balance sheet, provided acceptable financial information with respect to such corporation is available for inspection.
- (h) Members of the Corporation.
- (i) Regulated entities.

2. **“acceptable institutions”** means:

- (a) Canadian banks, Quebec savings banks, trust companies licensed to do business in Canada or a province thereof.
- (b) Credit and central credit unions and regional caisses populaires.

3. **“acceptable securities locations”** means those entities considered suitable to hold securities on behalf of a Member, for both inventory and client positions, without capital penalty, given that the locations meet the requirements outlined in the segregation Bylaws, Rules or Policies of the Corporation including, but not limited to, the requirement for a written custody agreement outlining the terms upon which such securities are deposited and including provisions that no use or disposition of the securities shall be made without the prior written consent of the Member and the securities can be delivered to the Member promptly on demand. The Corporation will maintain and regularly update a list of those foreign depositories and clearing agencies that comply with these criteria. The entities are as follows:

(a) Depositories

- i. Canada                                      CDS Clearing and Depository Services Inc.
- ii. United States                                Depository Trust Company

- (b) Government of Canada, the Bank of Canada and Provincial Governments.
- (c) Canadian banks, Quebec savings banks, trust companies and loan companies licensed to do business in Canada or a province thereof.
- (d) Credit and central credit unions and regional caisses populaires.
- (e) Insurance companies licensed to do business in Canada or a province thereof.
- (f) Mutual Funds or their Agents – with respect to security positions maintained as a book entry of securities issued by the mutual fund and for which the mutual fund is unconditionally responsible.
- (g) Regulated entities.

4. **“regulated entities”** means those that are Members covered by the Canadian Investor Protection Fund or Members of recognized exchanges and associations. For the purposes of this definition, recognized exchanges and associations are those that are identified as a "regulated entity" by the Investment Industry Regulatory Organization

of Canada.

5. "market value of securities" means:

- (a) for listed securities, the last bid price of a long security and, correspondingly, the last ask price of a short security, as shown on the exchange quotation sheets as of the close of business on the relevant date or last trading date prior to the relevant date, as the case may be, subject to an appropriate adjustment where an unusually large or unusually small quantity of securities is being valued. If not available, the last sale price of a board lot may be used. Where not readily marketable, no market value shall be assigned.
- (b) for unlisted and debt securities, and precious metals bullion, a value determined as reasonable from published market reports or inter-dealer quotation sheets on the relevant date or last trading day prior to the relevant date, or based on a reasonable yield rate. Where not readily marketable, no market value shall be assigned.
- (c) for commodity futures contracts, the settlement price on the relevant date or last trading day prior to the relevant date.
- (d) for money market fixed date repurchases (no borrower call feature), the market price is the price determined by applying the current yield for the security to the term of maturity from the repurchase date. This will permit calculation of any profit or loss based on the market conditions at the reporting date. Exposure due to future changes in market conditions is covered by the margin rate.
- (e) for money market open repurchases (no borrower call feature), prices are to be determined as of the reporting date or the date the commitment first becomes open, whichever is the later. Market price is to be determined as in 4 and commitment price is to be determined in the same manner using the yield stated in the repurchase commitment.
- (f) for money market repurchases with borrower call features, the market price is the borrower call price.

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