



MFDA Investor Protection Corporation

Corporation de protection des investisseurs de l'ACFM
2007 Annual Report

Information about the MFDA Investor Protection Corporation

The MFDA Investor Protection Corporation ("IPC") is a not-for-profit corporation established by the Mutual Fund Dealers Association of Canada ("MFDA") to administer an investor protection fund ("Fund") for the benefit of clients of mutual fund dealers that are members of the MFDA ("Member Firms"). The Fund protects client assets held by a Member Firm in the event that the Member Firm becomes bankrupt.

The MFDA is the sole self-regulatory organization that is a sponsor of the IPC. At June 30, 2007, 162 mutual fund dealers across Canada participated in the Fund. The IPC began offering coverage on July 1, 2005.

IPC Coverage Policy and Limits

IPC covers customers who incur losses as a result of the insolvency of a Member Firm. Loss of customer assets may take the form of shortfalls in the amount and type of assets which are held by the Member Firm at the time of bankruptcy. The IPC's objective is to return assets to customers or compensate customers when the assets are not available to the customer because the Member Firm has become insolvent.

Coverage is available in the amount of up to \$1 million for each of a customer's aggregated general and separate accounts. Most customers will have two "accounts" for coverage purposes, the aggregate of their trading accounts (general account) and the aggregate of their RRSP accounts (separate account). Securities, cash and other property of the customer such as segregated funds that are unavailable due to the insolvency of the Member Firm are covered by the IPC.

Customer losses which do not result from the insolvency of a Member Firm such as losses that result from changing market values of securities, unsuitable investments or the default of an issuer of securities, are not covered.

The coverage by IPC of losses suffered by customers of insolvent Member Firms is within the discretion of the IPC Board of Directors (the "Board"). The policy that has been adopted to define the way the Board intends to use its discretion in determining whether a customer is eligible for protection and the amount of that protection is available on the MFDA's website: www.mfda.ca.

Funding/Size of Fund/Administration

Funds are obtained by the IPC through the levy of quarterly assessments on MFDA Member Firms. Presently, Member Firms contribute to the Fund at the rate of approximately \$5 million per year and will continue to do so until the initial funding target of \$30 million is reached. As at June 30, 2007, the balance in the Fund stood at \$12.6 million. In addition, the IPC has obtained a credit facility from a Canadian chartered bank with a maximum limit of \$30 million. Repayment of this facility is guaranteed by the MFDA.

The IPC is engaged in continuous evaluation of the risk to the Fund and expects to periodically reset the size of the Fund, as appropriate.

Year in Review

The Board met 6 times during fiscal year ended June 30, 2007. Four meetings were the regular quarterly meetings of the Board and 2 meetings were held for special purposes.

Initiatives in 2006-2007

Several initiatives took place during the year. The Board monitored the progress of the IPC Working Group and received its final report at a special meeting in September 2006 (see below). The Board is monitoring the progress of information-sharing agreements in the industry and has developed a draft for its own use. The Board reviewed and approved changes to its investment policy to improve the return on its investment portfolio. The Board commenced a risk assessment review in November 2006 and the initiative is ongoing.

IPC Staff and Consultants

Joni Alexander and Ellipsis Consulting Group, Inc. were engaged as consultants to the IPC. Ms. Alexander has an ongoing role in an executive staff function and Ellipsis is a risk management consultant. In December 2006, Ms. Alexander was appointed President of the IPC.

IPC Working Group

The terms and conditions of the approval orders of the IPC required that a Working Group (the "Group") be established in October 2005 to review a number of aspects of the IPC, including identification of risks of mutual fund dealer failures leading to investor losses, appropriate fund size, types of products that should be covered, the appropriate coverage amount per customer account, assessment methodology, long-term funding and risk management tools required by the IPC.

The Report of the Group was received by the IPC Board in September 2006. The Group's summarized recommendations included the following:

a) "Investment dealers and mutual fund dealers are subject to a range of requirements that are intended to reduce the risk of insolvency and to protect client assets from losses if insolvency occurs, including participation in an investor compensation scheme, minimum capital, client asset segregation and risk management requirements and regular

oversight by their SROs. Other market participants with whom an investor may deal directly or indirectly and who may handle client assets such as portfolio managers and mutual fund managers are subject to less comprehensive requirements. The CSA [Canadian Securities Administrators] should recognize the investor protection gap that may result and consider what actions might be appropriate to take to protect investors;"

b) IPC coverage should ensure that customer assets under the control of the Member Firm are covered, "including losses arising due to any conversion of funds or covered assets of a client while under the control of the dealer that subsequently becomes insolvent;"

c) the policy with respect to the types of clients which are covered and excluded should be continued;

d) the policy of separate coverages (for aggregated general accounts and for aggregated separate accounts such as RRSPs) should continue;

e) the IPC should maintain a "substantial" fund and the primary source of the funding should be regular Member Firm assessments;

f) the initial target fund size of \$30 million to be achieved over five years was reasonable. Fund size should be regularly reassessed by the Board;

g) if assessments continue to be based on Assets under Administration ("AUA"), the AUA number should include all mutual fund assets and other covered assets. These numbers should be reported to the MFDA on Member Firms' monthly and annual reports;

h) oversight of Member Firms' activities should remain with the MFDA and the IPC should use the MFDA risk-based supervision model and observe other precedents such as the methodology of the Canadian Investor Protection Corporation to facilitate its risk management activities; and

i) several recommendations were made with regard to communications of IPC Coverage Policy. The policy should be such that the average investor can understand it, the MFDA and IPC should provide a definition of "assets held for clients", and the MFDA should revise the requirements regarding communications of IPC policies and the use of IPC logos.

The Board considered the recommendations and formally responded to the CSA on the Working Group Report in October 2006. The Board has built upon the recommendations of the Group in establishing its risk management process.

Commentary on Financial Results

The IPC's excess of revenue over expenses was \$4,972,209 for the year ended June 30, 2007. This compares to \$7,645,565 for the previous period. Revenue for the previous period, the IPC's initial year of operation, included contributions from the MFDA of fine monies and the Ontario Securities Commission ("OSC") of a settlement totaling \$3,934,112. These revenues were not expected to recur.

The IPC's revenue was \$5,460,069 for the year ended June 30, 2007. This compares to \$5,302,645 for the previous year, after the exclusion of the non-recurring revenues received last fiscal period. This year, IPC assessments to MFDA Member Firms totaled \$5,047,619, compared to \$5,172,367 previously. Investment revenue was \$412,450, an increase of \$282,172 over the previous period due to larger investment holdings as the size of the Fund grew with the accumulation of Member Firm assessments and investment revenue.

The IPC's chief source of revenue is Member Firm assessments, which are calculated based on the amount of AUA under the Member Firm's control. Each year, the fees are reset based on updated reports of AUA numbers. The assessment rates are set to generate an annual total assessment of approximately \$5 million. Investment income is expected to increase as the fund accumulates, and, starting in fiscal year ended June 30, 2008 should cover the normal annual operating expenses of the IPC.

Operating expenses were \$487,860 in fiscal 2007, \$1,103,332 less than the previous year. Prior year expenses were considerably higher than the current year due to the outlay to the MFDA for start-up costs of \$837,672, higher first year legal costs, and one-time bank charges for the set up of the credit line.

The Operating Fund increased by \$4,972,209 during fiscal 2007 resulting in a year-end balance of \$12,617,774.

Summarized Balance Sheet

As at June 30

	2007	2006
ASSETS		
Cash	\$ 111,076	\$ 455,116
Investments, at market	12,558,052	7,257,518
MFDA Investor Protection Corporation assessments receivable from the MFDA	8,727	42,992
Interest receivable	152	3,261
	\$ 12,678,007	\$ 7,758,887
LIABILITIES		
Accounts payable and accrued liabilities	\$ 44,733	\$ 98,405
Support costs due to MFDA	15,500	14,917
	60,233	113,322
FUND BALANCE		
Operating Fund	12,617,774	7,645,565
	12,617,774	7,645,565
	\$ 12,678,007	\$ 7,758,887

Summarized Statements of Revenues and Expenses and Changes in Fund Balance

For the year ended June 30

	2007	2006
REVENUE		
Assessments of MFDA Members	\$ 5,047,619	\$ 5,172,367
Investment income	412,450	130,278
Contribution from MFDA fine revenue	–	2,500,000
Contribution from OSC settlement revenue	–	1,434,112
	5,460,069	9,236,757
EXPENSES		
Operating expenses	487,860	753,520
Repayment of expenses to the MFDA for start-up costs	–	837,672
	487,860	1,591,192
EXCESS OF REVENUE OVER EXPENSES	4,972,209	7,645,565
FUND BALANCE, BEGINNING OF YEAR	7,645,565	–
FUND BALANCE, END OF YEAR	\$ 12,617,774	\$ 7,645,565

Reference may be made to the complete set of IPC financial statements which are available in the IPC section of the MFDA website www.mfda.ca.

Auditors' Report on Summarized Financial Statements

To the Members of the Board of Directors of MFDA Investor Protection Corporation

The accompanying summarized balance sheet and summarized statements of revenues and expenses and changes in fund balance (collectively the “summarized financial statements”) are derived from the complete financial statements of the MFDA Investor Protection Corporation as at June 30, 2007 and for the year then ended on which we expressed an opinion without reservation in our report dated August 17, 2007. The fair summarization of the complete balance sheet and statements of revenues and expenses and changes in fund balance is the responsibility of management. Our responsibility, in accordance with the applicable Assurance Guideline of The Canadian Institute of Chartered Accountants, is to report on the summarized financial statements.

In our opinion, the accompanying summarized financial statements fairly summarize, in all material respects, the related complete balance sheet and statements of revenues and expenses and changes in fund balance in accordance with the criteria described in the Guideline referred to above.

The summarized financial statements do not contain all the disclosures required by Canadian generally accepted accounting principles. Readers are cautioned that these summarized financial statements may not be appropriate for their purposes. For more information on the entity’s financial position, results of operations and cash flows, reference should be made to the related complete financial statements.

Deloitte & Touche LLP

Chartered Accountants
Licensed Public Accountants
Toronto, Ontario
August 17, 2007

IPC Board of Directors and Officer

The IPC Board of Directors is comprised of two Public Directors and one Industry Director.

Public Directors



Lawrence A. Wright, Chair
Executive Vice-President
Multimatic Inc.
(Markham, Ontario)



Donald H. Page, FCGA
Former Toronto Stock
Exchange Executive
(Wallacetown, Ontario)

Industry Director



W. David Wood
Executive Vice-President
Partnerships & Vice-Chairman
National Bank Financial Group
(Montreal, Quebec)

Officer



Joni Alexander
IPC President

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