



**Mutual Fund Dealers Association of Canada**  
Association canadienne des courtiers de fonds mutuels

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# MFDA Bulletin

## Policy

**For Distribution to Relevant Parties within your Firm**

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### **National Instrument 31-103 *Registration Requirements***

On July 17, 2009, the Canadian Securities Administrators (“CSA”) published National Instrument 31-103 *Registration Requirements* (“NI 31-103”), which will come into force on September 28, 2009.<sup>1</sup>

The purpose of this Bulletin is to advise Members of the provisions in NI 31-103 that will result in changes to MFDA Rules or Member practices.

#### **Proficiency Requirements in General**

NI 31-103 requires individuals to pass exams, not courses, to fulfill educational requirements for registration. MFDA Rules currently refer to courses that were previously required under securities legislation. Conforming changes will be made to MFDA Rules to ensure consistency with NI 31-103. MFDA will not require new registrants to satisfy the course requirements pending the Rule amendments.

Additions will also be made to the MFDA Rules to reflect proficiency requirements to sell labour sponsored investment funds and commodity pools in order to provide a complete reference of individual proficiency requirements for Members in the MFDA Rulebook.

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<sup>1</sup> In Ontario, NI 31-103 will come into force on the later of: (i) September 28, 2009; or (ii) when certain amendments to the *Budget Measures Act*, 2009 are proclaimed in force.

## **Ultimate Designated Person (“UDP”)**

The UDP is a new individual category of registration in NI 31-103. The UDP must be the chief executive officer of the Member, its sole proprietor or equivalent. There are no proficiency requirements for the UDP. The UDP is responsible for promoting a culture of compliance and overseeing the effectiveness of the Member’s compliance system. The Member’s Chief Compliance Officer (“CCO”) reports to the UDP. The CCO and UDP may be the same person if the individual meets the requirements for both categories. MFDA Rules currently do not require a UDP and, accordingly, MFDA will be making conforming Rule amendments to reflect the new UDP requirement. Members have 3 months from September 28, 2009 to designate and apply for registration for their UDP. Members will also have to notify the MFDA upon successful registration of their UDP which can be done by contacting the MFDA Membership Services Department.

## **Branch Managers**

The individual “Branch Manager” category of registration has not been retained in NI 31-103. NI 31-103 requires dealers to establish a system of controls and supervision to provide reasonable assurance that the dealer, and individuals acting on its behalf, comply with securities legislation and manage risks associated with its business. There are no specific requirements for the designation of a supervisor at branch locations. We are also aware that IIROC is eliminating its “Branch Manager” category of registration and replacing it with a “Supervisor” category given IIROC Members may conduct non-retail or non-advisory business where the branch supervision structure may not be appropriate.

MFDA Members only conduct retail operations. Accordingly, MFDA will be maintaining its Branch Manager requirements in its Rules. Members will be required to maintain information regarding their branch locations and designated Branch Managers on the Members’ Only section of the MFDA website. The MFDA will load branch information from NRD into the Members’ Only site before the NRD freeze on September 25, 2009. Members are asked to review the information on the Members’ Only site after the NRD freeze to ensure it accurately reflects their information. Any changes to branch information will then have to be reported to the MFDA within 5 business days by contacting the MFDA Membership Services Department until the Members Only site is able to accept such submissions electronically. Any questions with respect to the reporting of branch information should be directed to the MFDA Membership Services Department.

## **Client Mobility**

MFDA By-laws and Rules require individuals to be registered and in compliance with securities legislation. The new client mobility provisions contained in NI 31-103 will not be added to the MFDA Rulebook. However, Members should be aware of and comply with the new client mobility requirements in NI 31-103.

National Instrument 11-101 *Principal Regulator System* has been rescinded and replaced with NI 31-103. Sections 2.2 and 8.30 of NI 31-103 allow an Approved Person and a Member,

respectively, to maintain “eligible clients” (as defined in the instrument) in each jurisdiction without requiring registration in the jurisdiction subject to conditions. An Approved Person is allowed up to 5 eligible clients and a Member is allowed up to a total of 10 eligible clients in each jurisdiction. In order to rely on the exemption, Members and Approved Persons must not act beyond the scope of their registration in their principal jurisdiction (for example, acting as an adviser for discretionary managed accounts) and must be in compliance with their regulatory obligations to clients (for example, KYC, suitability and client reporting obligations). Before acting for the eligible client, the Member must advise the client in writing that it is exempt from registration in the relevant jurisdiction and is not subject to requirements applicable under local securities legislation. The Member must also submit a completed form 31-103F3 *Use of Mobility Exemption* to the local jurisdiction as soon as possible after relying on the exemption.

Members are expected to institute controls and procedures to comply with the conditions in NI 31-103 and to prevent the opening of new accounts in jurisdictions where the conditions of the exemption cannot be satisfied or where the exemption is not relied on. Where a Member does not rely on the exemption or if the exemption conditions cannot be met (for example where the Member or Approved Person has exceeded the eligible client limits), the Member must:

- Freeze accounts in the relevant jurisdiction where the Member is not registered from further purchase or switch transactions (except for transactions made pursuant to an automatic contractual plan); and either
- Immediately advise the client in writing that:
  - The Member is not registered in the jurisdiction;
  - The Member is not able to process further purchase or switch transactions for the account; and
  - The client must transfer his or her account to another dealer; or
- Immediately apply for registration in the relevant jurisdiction.

### **Referral Arrangements**

MFDA Rule 2.4.2 currently limits who a Member can enter into a referral arrangement with. Further, any referral for securities related business, the sale of investment products or financial services must be conducted through the Member. MFDA Rules currently allow Approved Persons to enter into referral arrangements on their own accord provided the referrals do not involve securities related business, the sale of investment products or financial services and such activity is in compliance with MFDA Rule 1.2.1(d) relating to dual occupations.

NI 31-103 does not impose limits as to who a registrant can enter into referral arrangements with. However, NI 31-103 requires all referral arrangements of Approved Persons to be conducted through their Member firm. NI 31-103 also provides more detail regarding the disclosure required to be provided to clients than is outlined in Rule 2.4.2. MFDA Rules will be amended to harmonize with the requirements of NI 31-103.

Members will have 6 months from September 28, 2009 to comply with the new requirements for referral arrangements. This includes referral arrangements entered into prior to NI 31-103 coming into effect.

### **Investment Fund Managers (“IFMs”)**

IFM is a new registration category and will only apply to a limited number of MFDA Members. Those Members who are operating as an IFM will have 12 months from September 28, 2009 to apply for registration as an IFM in their principal jurisdiction and 24 months to apply for IFM registration in the other jurisdictions in which they operate. MFDA Members with IFM registration will also have to separately submit financial filings and subordinated loan agreements to the MFDA and provincial securities regulatory authority in their principal jurisdiction in compliance with the different filing requirements of each regulator.

### **Trade Confirmations for Automatic Plans**

For automatic payment plans, MFDA Rule 5.4.2 requires a trade confirmation to be sent for the initial trade only. Under NI 31-103, trade confirmations for automatic plans are required to be sent semi-annually. MFDA Rule 5.4.2 will be amended to conform to NI 31-103.

### **Account Statements**

#### **Frequency**

NI 31-103 requires dealers to deliver account statements to clients at least once every 3 months for both client name and nominee name accounts. This requirement will result in an increase to the frequency of account statement delivery by Members operating in client name as such Members currently send account statements annually as required by MFDA Rule 5.3.1. MFDA Members who hold only a mutual fund dealer license will have 24 months from September 28, 2009 to comply with the quarterly statement requirement. Currently, there is no transition period for MFDA Members who hold an EMD license. EMDs are required to send quarterly account statements at the September 28, 2009 effective date. MFDA is aware that, at least in Ontario and Newfoundland, consideration is being given for a transition period for client account statements for EMDs. Should there be further developments regarding such a transition period, MFDA will issue a bulletin to Members.

#### **Content**

NI 31-103 requires account statements to disclose information regarding client positions for client name and nominee name accounts. MFDA Rule 5.3.3(b) does not require, but does not prohibit, disclosure of client positions for client name accounts. Given the new requirements of NI 31-103, MFDA Rule 5.3.3 will be amended to require disclosure of client positions regardless of whether the assets are held in nominee name or client name.

## **Outsourcing Account Statements and Trade Confirmations**

Under NI 31-103, dealers are responsible for sending account statements and trade confirmations to clients. MFDA Rules 5.3.1(c) and (d) and 5.4.1 allow for instances where a dealer may rely on another party to send account statements or trade confirmations on its behalf. Based on discussions with the CSA, the MFDA understands that Rules 5.3.1(c) and (d) and 5.4.1 do not require amendment to comply with NI 31-103, as such instances would be considered “outsourcing arrangements”. The NI 31-103 Companion Policy notes that Members are responsible and accountable for all functions that they outsource to a service provider. Outsourcing arrangements should be subject to a binding agreement, in writing, stating that due-diligence should be conducted prior to engaging third party service providers and that the firm, its auditors and regulators should have the same access to the work product of such service providers as they would if the firm performed the activities itself.

## **Exempt Market Dealers (“EMDs”)**

This is a new category of registration for entities in the business of dealing in exempt securities. The introduction of the EMD category of registration does not impact the scope of the MFDA’s regulatory oversight as Members and Approved Persons selling exempt securities are currently required to conduct such activity through the MFDA Member. MFDA Rule 1.1.1 requires all securities related business to be carried on for the account and through the facilities of the Member. Securities related business includes trading and advising in exempt securities. While the EMD category may be new, Members and Approved Persons are still not permitted to sell exempt securities through any other entity or refer clients to another party to purchase exempt securities.

## **Dealer Registration**

MFDA Members who wish to continue selling exempt securities after September 28, 2009 will be required to obtain EMD registration in all applicable provinces and territories. In Ontario and Newfoundland, Members with LMD registration will not have to apply for an EMD license as LMD registration will convert automatically to EMD registration. In the other provinces and territories, Members will have to apply for EMD registration. In the provinces and territories other than Ontario and Newfoundland, Members who have been actively selling exempt securities prior to September 28, 2009 will have 12 months to apply for the EMD license. Those Members who have not been actively selling exempt securities prior to September 28, 2009 and new MFDA Members after September 28, 2009 will have to apply for and obtain an EMD license prior to selling exempt securities.

## **Non-Prospectus Qualified Mutual Funds**

Mutual fund dealers are licensed to sell “mutual funds” as defined under the various provincial *Securities Acts*. “Mutual funds” are not limited to those that are prospectus qualified. Certain non-prospectus qualified investment funds may also meet the definition of a “mutual fund” and therefore would not require additional EMD registration to distribute.

## **New EMD Proficiency Requirements**

Salespersons of an EMD must pass either:

- the Canadian Securities Course Exam;
- the Exempt Market Products Exam; or
- satisfy the requirements of an advising representative for a portfolio manager.

CCOs of an EMD selling exempt securities must pass the PDO exam and either:

- the Canadian Securities Course Exam;
- the Exempt Market Products Exam; or
- satisfy the requirements of a CCO for a portfolio manager.

**It is important to note that the previous Mutual Fund Officers, Partners and Directors course and the new Mutual Fund Dealers Compliance Exam do not satisfy the proficiency requirements of a CCO of an EMD.**

## **EMD Proficiency Transition Period**

In Ontario and Newfoundland, the CCO and salespersons of a Member with an existing LMD license have 12 months from September 28, 2009 to obtain the above proficiency. In the other provinces and territories, if the firm is active in selling exempt securities, the CCO and salespersons have 12 months to obtain the above proficiency. If the Member is not active in selling exempt securities prior to September 28, 2009 or obtains membership in the MFDA after September 28, 2009, the Member must obtain an EMD license and individuals must satisfy the above proficiency prior to selling exempt securities.

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