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**BULLETIN #0452 – M**  
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# MFDA Bulletin

## Member Information

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

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### **Changes regarding the MFDA Investor Protection Corporation**

#### **1. Background**

The MFDA issued a bulletin on June 17, 2010 (see Bulletin #0437-M), which advised of proposals by the MFDA Investor Protection Corporation (“IPC”) regarding changes to its fund size and assessment base. The bulletin also described the formation by the MFDA of the MFDA IPC Issues Committee (“IPCIC”) to consider the proposals. The bulletin outlined the IPCIC's proposed recommendations to the MFDA Board of Directors and other issues for consideration with respect to the IPC and invited Member comment.

The recommendations proposed and issues identified by the IPCIC contemplated a three stage, phased-in approach to the changes relating to the IPC.

#### **2. Member Consultation Process**

Members were invited to submit comments on the recommendations proposed and issues outlined in Bulletin #0437-M by September 1, 2010. Consultation with Members was also conducted through an in-person meeting open to all Members, held on July 15, 2010, and a meeting with the Investment Funds Institute of Canada and the Federation of Mutual Fund Dealers on July 28, 2010.

A summary of the written comments received and minutes of the in-person meetings can be accessed under the IPC section of the MFDA's website.

#### **3. Agreement by the MFDA to IPC Changes**

The changes proposed by the IPC to its fund size and its assessment base are required to be made with the agreement of the MFDA. The IPCIC consulted with the IPC during the course of its

deliberations, and the IPC participated in the Member consultation above. The IPC was also kept apprised of the development of the IPCIC's recommendations to the MFDA Board, which were presented at its meeting on September 30, 2010. The changes to the fund size and period for accumulation of the incremental funds have been agreed between the MFDA and IPC.

### **3.1 Stage 1 Recommendations: Fund Size**

The stage 1 proposed recommendations of the IPCIC related to whether the size of the IPC fund should increase and, if it should, how related matters of timing and minimum assessments should be addressed.

#### Increase the IPC Fund to \$50 Million

The MFDA Board of Directors agreed with the IPC proposal to increase the size of the fund to \$50 million.

Many Members were not convinced of the merits of the IPC proposal to increase the fund size to \$50 million. Some Members expressed their disagreement by questioning the need and value of the fund in the first place, while others questioned the information provided and reasons given in the support of the increase. However, the MFDA and IPC are satisfied that insolvency risk does exist for MFDA Members and their customers and the IPC fund must increase as the risk of insolvency of Members increases.

#### Recommendation to Implement Increase over Seven Years with Transition Period

The assessment period proposed by the IPC for raising the additional \$20 million for the fund will be increased from five years to seven years, and the assessment period for raising the additional funds will begin on July 1, 2011.

During the comment period, several Members requested that, should the fund size be increased, the time frame for raising the additional \$20 million be extended beyond five years (as initially proposed) to lessen the burden on Members.

Having regard to the comments received, the MFDA and IPC are of the view that extending the assessment period to seven years is reasonable. In addition, providing Members with a transition period until July 1, 2011 before collecting assessments will provide sufficient time for business and budget planning by Members.

#### Recommendation to Reduce Minimum Assessment by Proportionate Reduction in Member Fees

The Member assessments for the seven years, commencing July 1, 2011, will be substantially less than the current annual assessment (the new amounts will be approximately 55% of the prior year's assessment). The minimum assessments charged to Members will be reduced by the proportional reduction in Member assessments.

### **3.2 Stage 2 and 3 Recommendations: Issues for Further Study and Consideration**

The stage 2 and 3 proposed recommendations of IPCIC related respectively to aligning the IPC assessment base with the customer property protected and the introduction of risk-based assessment measures and other means of protection not relying as much on pre-funding.

During the consultation period, many comments were received on these subjects including the incorporation of risk measures into the assessment formula for the IPC, such as consideration of the flow of funds into and out of trust accounts of Members, the value of assets held in client name versus nominee name, and the financial strength of the Member. In addition, Members suggested that consideration be given to the use of insurance products as an alternative or additional source of IPC funding. It was also noted that there are other products, including financial institution bonds and errors and omissions insurance, which mitigate the risks of calls upon the IPC fund.

The MFDA Board accepted the principle of aligning the IPC scope of product coverage with the IPC assessment base but decided that the matter required further consideration. Accordingly, MFDA staff has been asked to work with the IPC to consider and analyze, by October 1, 2011, the practical implications and desirability of changes. With respect to risk-based assessment methodologies and the use of insurance products by either IPC or Members to mitigate risks, it was also determined that further information and analysis was required. The IPC has been asked, with the support of MFDA staff, to consider and provide to the MFDA such information and analysis by January 1, 2012.

### **4. Next Steps**

The response of the MFDA Board to the IPC proposals was considered by the IPC Board of Directors at its meeting on October 4, 2010. The IPC will be implementing the proposals relating to the increase of the fund size to \$50 million as modified. MFDA staff will consider and analyze with the IPC the issues related to the IPC assessment base and risk-based assessment methodology and other issues, as outlined above, and within the specified timelines.

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