

VIA E-MAIL

September 28, 2010

British Columbia Securities Commission
Alberta Securities Commission
Saskatchewan Financial Services Commission
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
New Brunswick Securities Commission
Registrar of Securities, Prince Edward Island
Nova Scotia Securities Commission
Superintendent of Securities, Newfoundland and Labrador
Registrar of Securities, Northwest Territories
Registrar of Securities, Yukon Territory
Registrar of Securities, Nunavut

Delivered to:

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Dear Sirs/Mesdames:

**Re: Canadian Investor Protection Fund
Proposed Amendments to National Instrument 31-103
National Instrument 33-109 and
Ontario Securities Commission Rule 33-506**

Canadian Investor Protection Fund ("CIPF") is pleased to provide its comments in respect of the Notice and Request for Comments ("Notice") relating to the Instruments and Rule referred to above. Our comments are restricted to National Instrument 31-103 ("NI 31-103"). In particular, CIPF wishes to comment on:

1. **Fair value.** The proposed amendments to Section 14.14 of NI 31-103 (and related amendments in Form 31-103F1) requiring account statements to include "fair value" information with respect to client holdings; and



2. **Client name securities.** The proposal being considered with respect to Section 14.14 of NI 31-103 to include client name securities in client account statements and Questions 1 and 6 posed in the Notice.

CIPF is sponsored by the Investment Industry Regulatory Organization of Canada ("IIROC") and is the only compensation fund approved by the Canadian Securities Administrators for IIROC Dealer Members. All IIROC Dealer Members are CIPF Members.

Fair Value

The proposed amendments to Section 14.14 of NI 31-103 relate to the accounting amendments which are part of the International Financial Reporting Standards ("IFRS") including replacement of the term "market value" with the term "fair value" as defined in IFRS. As indicated above, CIPF provides protection in respect of IIROC Dealer Members and, accordingly, works closely with respect to IIROC and its Dealer Members in providing coverage according to both client holdings and risk management assessments based on the financial condition of Dealer Members. The matter of the valuation of client holdings is critical to CIPF in that regard and CIPF relies on financial reporting by Dealer Members, including valuation of client-held inventories, and it is important that such reporting be based on clear and workable accounting standards and requirements. CIPF is aware of the submissions to be made by IIROC to the CSA in respect of Section 14.14 of NI 31-103 and shares the concern that the adoption of IFRS for Dealer Member regulatory reporting and client statement reporting can only be supported with some departures from IFRS. In particular, we support the view that the valuation process to determine fair value should permit an assignment of "value not determinable" where one of the IFRS modelling approaches other than the current market price is not reliable. Application of IFRS valuation methodology otherwise is not practical for IIROC Dealer Members.

Apart from the practical difficulties of determining fair value as indicated above and in the submissions of IIROC, the use of fair value for IIROC Dealer Members and in client account statements raises more fundamental concerns in the context of an IIROC Dealer Member insolvency. CIPF's primary mandate is the protection of client assets held by Dealer Members in the event of an insolvency and its role in that regard is reflected in (and co-ordinated with) the provisions of Part XII of the *Bankruptcy and Insolvency Act* (Canada) ("BIAC"). In summary, the provisions of Part XII of BIAC outline the terms on which an insolvent securities dealer will be liquidated with preferential treatment to clients of dealers who hold assets at the dealer. In the event of a dealer insolvency a trustee in bankruptcy is required to determine the assets and liabilities of the estate and calculate the net equity for each customer, being the "net dollar value of the account or accounts, equal to the amount that would be owed by a securities firm to the customer as a result of the liquidation by sale or purchase at the close of business of the securities firm on the date of bankruptcy of the securities firm, of all security positions of the customer in each securities account..." The amount which is the difference between an eligible customer's net equity and the value of the assets held by the dealer (as at the date of insolvency and usually determined according to customer statements) is the

amount of compensation CIPF would pay. CIPF would normally return to customers the securities in an account if they are available. If they are not available, CIPF would provide cash to the equivalent value and, therefore, the matter of certain valuation of securities is important.

Based on the foregoing requirements of BIAC, it is likely that the basis on which net equity is calculated will differ from the financial position of an IIROC Dealer Member reported using fair value as required by IFRS. As a practical matter, the prompt and efficient liquidation of the estate of a securities dealer and compensation payments to be made by CIPF are based on the account statements of customers of IIROC Members. This circumstance may have several consequences. For the purposes of these submissions, however, we believe that the method of inventory valuation proposed by IIROC will result in a more consistent approach for determining net equity. Further, and of arguably more importance, the alignment of the expectation of customers according to their account statements with what may be expected to be recovered from the insolvency of their Dealer Member may be distorted by the adoption of fair value reporting standards.

Client Name Securities on Account Statements

The Notice indicates that the CSA is "considering amending Section 14.14 [of NI 31-103] to clarify whether client statements only need to include securities held or controlled by a firm or whether they need to also include client name securities". In respect of this consideration, the Notice poses a number of questions of which questions 1 and 6 are particularly relevant to CIPF and on which we have commented below. In summary, CIPF would not support the inclusion of client name securities on client statements. Such a change would not benefit clients and would, in fact, add considerably to client confusion and concern.

With respect to question 1, one of the primary benefits for customers in respect of account reporting is the communication as to who is responsible for the property of the customer. This information is of critical importance to customers in that the expectations of customers for protection are usually defined by their account statements. Under the current Canadian SRO Rules of IIROC, the distinction is clear and is relied upon by CIPF. In addition, bankruptcy officials such as trustees in bankruptcy rely on such statements as evidence of client entitlement in a liquidation. This speeds up the process of claims payments. A change to the current rules to include client name positions on customer accounts would not appear to us to be of benefit to customers and would add confusion, rather than clarity, to customer reporting and slow up the payment process considerably if a determination as to nominee and client name holdings would be required. In the context of CIPF and customer protection in the event of the insolvency of an IIROC Dealer Member, customers would have to be aware of the fact that client name securities are not protected by CIPF and nor do they benefit from the customer pool preference provided by Part XII of BIAC. As a matter of understanding, it is difficult to explain in layperson terms the differences between nominee and client name holdings. Such explanations are necessarily technical, confusing and to the

extent that they implicitly endorse some financial products over others, consumer choice and buying decisions may be skewed.

With respect to question 6, the matter of when a client relationship with a dealer starts and ends is of relevance and concern to CIPF. CIPF assumes financial responsibility for the protection of persons who are clients of a dealer in the sense of the dealer having an account with the person and holding assets for his or her account. The provisions of Part XII of BIAC described above are based on the same principles. The prospect of including client name positions on Dealer Member client statements is of concern to CIPF because the implicit expectation would be that protection would continue after any conventional client relationship had terminated. This would increase exposure to CIPF and the Dealer Members who sponsor it in a manner that would be unfair and unwarranted. To the extent that account statements only include nominee name positions, the expectation of CIPF protection and actual coverage are aligned. If a client transfers property out of an account, it is clear and understood that CIPF's coverage ceases.

We will be pleased to provide any further information and answer any questions in connection with the comments above.

Yours very truly,

CANADIAN INVESTOR PROTECTION FUND



Rozanne Reszel
President & Chief Executive Officer

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