

Chapter 6

Request for Comments

6.1.1 Notice of Request for Comments – Proposed Amendments to OSC Rule 31-502 – Proficiency Requirements for Registrants, OSC Rule 31-505 – Conditions of Registration and OSC Rule 35-502 – Non-Resident Advisers

NOTICE OF REQUEST FOR COMMENTS

PROPOSED AMENDMENTS TO RULE 31-502 – PROFICIENCY REQUIREMENTS FOR REGISTRANTS AND RULE 31-505 – CONDITIONS OF REGISTRATION AND RULE 35-502 – NON-RESIDENT ADVISERS

Substance and Purpose of Proposed Amendments

Representatives of the investment adviser industry have raised concerns about the proficiency requirements for compliance officers of firms registered as advisers under Rule 31-502 – *Proficiency Requirements for Registrants* (Rule 31-502) and also with respect to the requirements for designated compliance officers and their delegates under Rule 31-505 – *Conditions of Registration* (Rule 31-505) and Rule 35-502 – *Non-Resident Advisers* (Rule 35-502; together, the Rules). The proposed amendments to the Rules are intended to provide alternative proficiency requirements for compliance officers of advisers and clarify the roles assigned to individuals involved in the supervision of advisers' regulatory compliance. The Commission also proposes to make two minor clarifications to Rule 31-502 that are not limited to matters concerning compliance officers. The proposed amendment to Rule 35-502 will remove the requirement for an international adviser to designate a compliance officer.

Summary of the Proposed Amendments

Under Rule 31-502, an adviser's designated compliance officer is required to have the same proficiency as an officer, partner or representative of the adviser. Under the proposed amendments, Rule 31-502 will provide alternatives which recognize practical expertise in compliance matters.

Under Rule 31-505, an adviser is required to designate a compliance officer who will be responsible for certain prescribed duties and is permitted to delegate certain of those duties to another individual who has the same proficiency as the designated individual. Under the proposed amendments, this will be replaced for advisers with a system whereby a senior officer assumes ultimate responsibility for the compliance function, while day-to-day supervision of the compliance function is undertaken by an operating officer whose proficiency is determined in accordance with the amended requirements under Rule 31-502. The operating officer will be free to determine what responsibilities and skills are appropriate for any subordinates working in a compliance capacity. A single individual may undertake both roles if he or she meets the requirements of both.

Section 1.2 of Rule 31-502 permits individuals who have completed required courses or examinations more than three years previously to be registered or reinstated in a registration category, provided that the individual was registered in Ontario in that category during the preceding three-year period. Individuals who have been continuously registered in equivalent categories in other provinces or territories of Canada are thus unable to avail themselves of section 1.2 in applying for registration in Ontario. The Commission proposes to amend subsection 1.2 to recognize equivalent registration in other Canadian jurisdictions. If the proposed amendment receives final approval, Staff Notice 32-702 – *Applications for Exemptions from the Time Limits on Completion of Courses and Previous Registrations* will be withdrawn.

Subsection 3.3(3) of Rule 31-502 provides that "An investment counsel or portfolio manager that employs an associate representative, associate partner or associate officer shall designate a representative, partner or officer that is not an associate representative, associate partner or associate officer to approve advice given by an associate representative, associate partner or associate officer". Subsection 3.3(4) sets out further specifications concerning the designated supervisor. For greater certainty, the Commission proposes to specify that the designated supervising representative, partner or officer referred to in these two subsections is required to be a registrant.

The Commission proposes to amend Rule 35-502 to remove the requirement for international advisers to designate a compliance officer, which serves no regulatory purpose in view of the restricted activities international advisers are permitted to undertake and limited requirements applicable to their activities.

Authority for Proposed Amendments

The following provisions of the Act provide the Commission with authority to make the Rules and as such, to amend them: Paragraph 143(1)1 of the *Securities Act* (the Act) authorizes the Commission to make rules prescribing requirements in respect of applications for registration and the renewal, amendment, expiration or surrender of registration. Paragraph 143(1)2 of the Act authorizes the Commission to make rules prescribing the conditions of registration or other requirements for registrants or any category or sub-category of registrant. Paragraph 143(1)3 of the Act authorizes the Commission to make rules extending any requirements prescribed under paragraph 143(1)2 to unregistered directors, partners, salespersons and officers of registrants.

Alternatives Considered

The Commission considered maintaining the status quo but concluded that the concerns raised by the industry are serious enough to merit remedial action. The Commission also considered relying on the Director's authority to grant exemptive relief to address these issues, but felt that the exercise of the Director's discretion is a mechanism intended to provide extraordinary relief, while the concerns are common to most if not all advisers. As such, it would be inappropriate and wasteful of the resources of both advisers and the Commission to rely on exemptions.

Unpublished Materials

In proposing the amendments to the Rules, the Commission has not relied on any significant unpublished study, report, decision or other written materials.

Anticipated Costs and Benefits

Staff believes that the proposed amendments will permit advisers to establish more effective compliance systems without incurring new costs.

Regulations Revoked or Amended

The proposed amendments do not require any regulations to be revoked or amended.

Comments

Interested parties are invited to make written submissions with respect to the proposed amendments. Submissions received by March 31, 2003 will be considered.

Submissions should be sent to:

John Stevenson, Secretary
Ontario Securities Commission
20 Queen Street West
19th Floor, Box 55
Toronto, Ontario M5H 3S8
jstevenson@osc.gov.on.ca

If you are not sending your comments by e-mail, please send us two copies of your letter, together with a diskette containing your comments (in either Word or Wordperfect format). As the Act requires that a summary of the written comments received during the comment period be published, confidentiality of submissions cannot be maintained.

Questions may be referred to:

Christopher Jepson
Legal Counsel
Ontario Securities Commission
(416) 593-2379
cjepson@osc.gov.on.ca

Proposed Amendments

The text of the proposed amendments follows.

December 10, 2002.

Proposed Amendments

Amendments to Rule 31-502 — Proficiency Requirements For Registrants

1. Subsection 1.2(1) is amended by the addition of “or its equivalent in any other province or territory of Canada” after “previously registered in the relevant category”.
2. The title of section 3.1 is amended by the deletion of “and Compliance Officers”, which is replaced with “, Chief Compliance Officers and Ultimately Responsible Persons”.
3. Subsection 3.1(2) is re-designated subsection 3.1(3) and amended by the deletion of “as the compliance officer under section 1.3 of Rule 31-505 Conditions of Registration or”.
4. Section 3.1 is amended by the substitution of the following in place of the former subsection 3.1(2):

“3.1 (2) An individual shall not be designated by a securities adviser as the chief compliance officer under section 1.3 of Rule 31-505 Conditions of Registration unless the individual

 - (a) has been granted registration previously as a representative, partner or officer of a securities adviser, investment counsel or portfolio manager;
 - (b) has
 - (i) obtained professional designation as a lawyer or Chartered Accountant in a Canadian jurisdiction or the equivalent in a foreign jurisdiction and is in good standing with the appropriate self-regulatory body or regulatory agency;
 - (ii) completed the Canadian Securities Course and the Partners, Directors and Senior Officers Qualifying Examination; and
 - (iii) either
 - (A) been employed for three years by a registered dealer or a registered adviser; or
 - (B) been providing professional services to the securities industry for three years and employed by a registered dealer or registered adviser for one year; or
 - (c) has
 - (i) completed the Canadian Securities Course and the Partners, Directors and Senior Officers Qualifying Examination; and
 - (ii) either
 - (A) been employed for five years by a registered dealer or a registered adviser, including three years under the supervision of the designated or chief compliance officer of a registered dealer or a registered adviser; or
 - (B) been employed for five years by a financial intermediary regulated by the federal Office of the Superintendent of Financial Institutions in a compliance capacity relating to portfolio management and employed by a registered dealer or registered adviser for one year;

provided that an individual designated as chief compliance officer pursuant to paragraph (b) or (c) shall not act as an adviser.”
5. The title of section 3.2 is amended by the deletion of “and Compliance Officers”, which is replaced with “, Chief Compliance Officers and Ultimately Responsible Persons”.
6. Subsection 3.2(2) is re-designated subsection 3.2(3) and amended by the deletion of “as the compliance officer under section 1.3 of Rule 31-505 Conditions of Registration or”.

7. Section 3.2 is amended by replacement of the former subsection 3.2(2) with the following:
- “3.2 (2) An individual shall not be designated by an investment counsel or portfolio manager as the chief compliance officer under section 1.3 of Rule 31-505 Conditions of Registration unless the individual
- (a) has been granted registration previously as a representative, partner or officer of an investment counsel or portfolio manager, other than in reliance on section 3.3 or under a registration subject to terms and conditions requiring the individual’s advising activities to be supervised, or as an investment counsel or portfolio manager;
 - (b) has
 - (i) obtained professional designation as a lawyer or Chartered Accountant in a Canadian jurisdiction or the equivalent in a foreign jurisdiction and is in good standing with the appropriate self-regulatory body or regulatory agency;
 - (ii) completed the Canadian Securities Course and the Partners, Directors and Senior Officers Qualifying Examination; and
 - (iii) either
 - (A) been employed for three years by a registered dealer or a registered adviser; or
 - (B) been providing professional services to the securities industry for three years and employed by a registered dealer or registered adviser for one year; or
 - (c) has
 - (i) completed the Canadian Securities Course and the Partners, Directors and Senior Officers Qualifying Examination; and
 - (ii) either
 - (A) been employed for five years by a registered dealer or a registered adviser, including three years under the supervision of the designated or chief compliance officer of a registered dealer or a registered adviser; or
 - (B) been employed for five years by a financial intermediary regulated by the federal Office of the Superintendent of Financial Institutions in a compliance capacity relating to portfolio management and employed by a registered dealer or registered adviser for one year;
- provided that an individual designated as chief compliance officer pursuant to paragraph (b) or (c) shall not act as an adviser.”

8. Subsection 3.3(3) is amended by the addition of the word “registered” after “shall designate a”.

9. Subsection 3.3(4) is amended by the addition of the word “registered” after “the designated”.

10. Part 3 is amended by the addition of the following section 3.4:

“3.4 New Entrants Equivalency – In this Part, an individual may meet a requirement to complete the Canadian Securities Course by completion of the New Entrants Examination and the U.S. Series 7 Examination.”

Amendments to Rule 31-505 — Conditions Of Registration

11. The title of section 1.3 is amended by the addition of “or Chief Compliance Officer and Ultimately Responsible Person” after “Compliance Officer”.
12. Subsection 1.3(1) is re-designated paragraph 1.3(1)(a) and amended by the deletion of “or adviser”, which appears twice.

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13. Subsection 1.3(2) is re-designated paragraph 1.3(1)(b) and amended by the deletion of “or adviser” and the deletion of “and supervising advice provided to each client”.
14. Subsection 1.3(3) is re-designated paragraph 1.3(1)(c) and amended by the deletion of “or an officer in the same category of registration as the adviser,” and the deletion of “in each case” and the replacement of the references to “subsections (1) and (2)” with references to “paragraphs (a) and (b)”.
15. Section 1.3 is amended by the addition of the following subsection 1.3(2):
 - “1.3(2) (a) A registered adviser shall designate an executive officer as the individual who is ultimately responsible for discharging the obligations of the registered adviser under Ontario securities law.
 - (b) “Executive officer” means for purposes of paragraph (a) a registered partner or registered officer who is,
 - (i) president, chief executive officer, chief financial officer, secretary, general counsel or general manager of the registered adviser or any other individual who performs functions for it which are similar to those normally performed by an individual occupying any such office, or
 - (ii) one of the five highest paid partners or officers of the registered adviser.
 - (c) The ultimately responsible person designated under paragraph (a) shall ensure that policies and procedures for the discharge of the obligations of the registered adviser under Ontario securities law are developed and implemented.
 - (d) A registered adviser shall also designate a partner or officer as the chief compliance officer who shall either be the same individual as the ultimately responsible person designated under paragraph (a) or shall report to that individual.
 - (e) The chief compliance officer designated under paragraph (d) shall supervise the registered adviser’s adherence to the policies and procedures referred to in paragraph (c) and shall also be responsible for supervising the opening of each new account and supervising advice provided to each client or, if a branch manager is designated under subsection 1.4(1), for supervising the branch manager’s conduct of the activities specified in subsection 1.4(2).
 - (f) The ultimately responsible person designated under paragraph (a) shall report directly to the board of directors or partnership annually concerning the discharge of the obligations of the registered adviser under Ontario securities law and shall have a right to directly access the board of directors or partnership at such other times as he or she may deem necessary or advisable.
 - (g) An applicant for registration or reinstatement of registration as an adviser shall deliver to the Commission, with the application, written notice of the name of the person or persons proposed to be designated under paragraphs (a) and (c).”
16. Subsection 1.4(2) is amended by the deletion of “section 1.3” and its replacement with “subsection 1.3(a) in the case of a dealer and the chief compliance officer designated under subsection 1.3(b) in the case of an adviser.”

Amendments to Rule 35-502 – Non-Resident Advisers

17. Part 3 is amended by the addition of the following section 3.14:

“Partial Exemption from Rule 31-505 – An international adviser is exempt from subsection 1.3(2) of Rule 31-505.”