OSC

ONTARIO SECURITIES COMMISSION

Annual Summary Report for Dealers, Advisers and Investment Fund Managers

Compliance and Registrant Regulation

OSC Staff Notice 33-749

August 23, 2018

CONTENTS

Director's message

The Ontario Securities Commission (**OSC**, the **Commission**) expects strong compliance by registered firms and individuals (collectively, **registrants**) and articulates its expectations through its oversight, guidance and outreach. To assist registrants with meeting these regulatory expectations, we have redesigned one of our main outreach tools, the Annual Report for Dealers, Advisers and Investment Fund Managers (**Annual Report**). Our aim is to create a versatile report for registrants to reference when developing, implementing and maintaining an effective compliance system.

A key change to this year's Annual Report is the grouping of deficiencies by topic instead of registration category. Since firms are often registered in multiple categories and because deficiencies can apply equally across categories, we think registrants will find it beneficial to focus on deficiencies by topic. Also, relevant regulatory resources have been organized into dedicated sections for ease of reference. We continue to include topic specific guidance to help registrants understand how to comply with both the explicit regulatory requirements and the spirit of the requirements. For example, we have included a sample flowchart to assist firms with evaluating compliance with section 5.6 of National Instrument 81-105 *Mutual Fund Sales Practices* (**NI 81-105**). Finally, we provide summaries of the Director's Decisions since these decisions evidence the compliance–enforcement continuum. We hope that registrants find this report informative and use it as a self-assessment tool.

Over the past year, the Compliance and Registrant Regulation (**CRR**) staff have been proactively meeting with registrants, completing reviews, approving registration applications, evaluating developments in the financial technology space and working on policy projects. You will find much of this work detailed in this report. One point that I would like to emphasize is that, when conducting our reviews, we continue to focus on evaluating the effectiveness of a registrant's compliance system. Part 11 of National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* (**NI 31-103**) and accompanying guidance provides the framework for establishing an effective compliance system. To meet this obligation, registrants should continually monitor, test and revise their compliance system to keep up-to-date with the evolution of their business practices, products and risks. When assessing how a registrant

maintains the effectiveness of its compliance system, CRR staff find it useful to review the Chief Compliance Officer's (**CCO**) annual report to the board of directors or similar governance body. A well written report documents how the firm proactively evaluated the effectiveness of its compliance system and explains how the firm addressed, or intends to address, any identified weaknesses in the compliance system.

Looking forward, our compliance reviews will focus on the following areas:

- section 5.6 of NI 81-105 which governs the provision of promotional items and business promotion activities,
- conflicts of interest created by compensation practices,
- firms that participated in the 'Registration as the First Compliance Review' program and have been in operation for greater than one year,
- assessing the accuracy of responses from firms completing the 2018 Risk Assessment Questionnaire (**RAQ**), a tool that is issued every two years that gathers information about our registrants' operations, and
- high risk registrants identified through the 2018 RAQ process.

In addition to this report, we continue to provide useful tools to assist registrants in strengthening their compliance function. Our Registrant Outreach program includes educational seminars and we update the **Topical Guide for Registrants** periodically. This tool provides links to guidance for over 100 topic areas.

The CRR Branch encourages continuous and open lines of communication with registrants. We invite registrants to discuss regulatory policy, compliance practices and matters impacting their business models with us, so do not hesitate to call or email us. Our contact information is included at the end of this report.

We look forward to engaging with our registrants in the upcoming year.

Debra Foubert
Director, Compliance and
Registrant Regulation

Introduction

Who we are

The CRR Branch of the OSC is responsible for regulating firms and individuals who are in the business of trading in, or advising on, securities or commodity futures and firms that manage investment funds in Ontario. The OSC's mandate is to:

- provide protection to investors from unfair, improper or fraudulent practices,
- foster fair and efficient capital markets, and
- contribute to the stability of the financial system by making and monitoring compliance with rules governing the securities industry in Ontario.

CRR's activities are integral to the OSC's goal of being an effective and responsive securities regulator.

The purpose of this report

This Annual Report prepared by staff of the CRR Branch is designed to assist registrants with information on the following:

- **Education and registration outreach**
  Part 1 of this report provides links and information to the registration and ongoing educational resources and outreach opportunities available to current and prospective registrants.

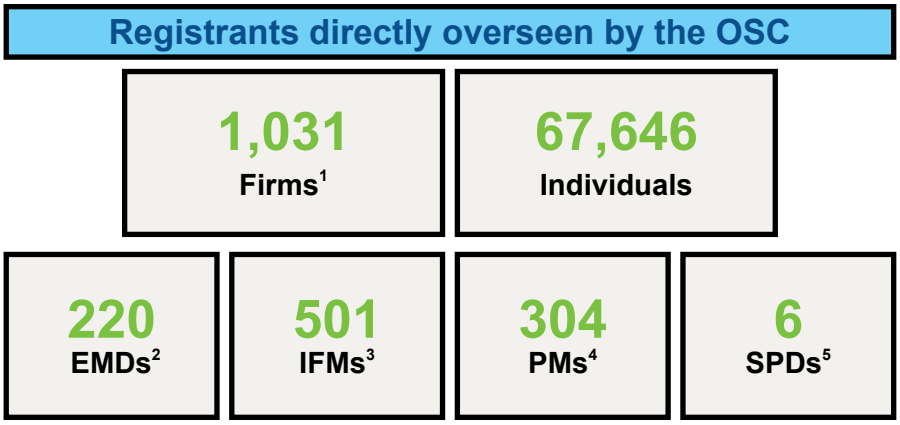
- **Regulatory oversight activities and guidance**
  Part 2 of this report should be used by registrants as a self-assessment tool to strengthen compliance with Ontario securities law and, as appropriate, to make changes to enhance their systems of compliance, internal controls, and supervision.

- **Impact of upcoming policy initiatives**
  Part 3 of this report provides insights into some of the new and proposed rules and other regulatory initiatives that may impact a registrant's operations.

- **Regulatory conduct activities**
  Part 4 of this report is intended to enhance a registrant's understanding of our expectations and our interpretation of regulatory requirements. This section also provides insight into the types of regulatory actions the CRR Branch may take to address non-compliance.

Who this report is relevant to

This Annual Report provides information for registrants that are directly regulated by the OSC. These registrants primarily include exempt market dealer (**EMDs**), investment fund managers (**IFMs**), portfolio managers (**PMs**) and scholarship plan dealers (**SPDs**).



In general, firms must register with the OSC if they conduct any of the following activities in Ontario:

- are in the business of trading in, or advising on, securities. This is referred to as the 'business trigger' for registration,
- act as an underwriter or as an IFM, or
- conduct trading and advising activities involving commodity futures contracts or commodity futures options.

Individuals must register if they trade, advise or underwrite on behalf of a registered dealer or adviser, or act as the Ultimate Designated Person (**UDP**) or CCO of a registered firm.

There are seven dealer and adviser categories for firms trading in or advising on securities:

- EMDs,
- SPDs,
- restricted dealers,
- PMs,
- restricted portfolio managers,
- investment dealers (**IDs**), who must be members of the Investment Industry Regulatory Organization of Canada (**IIROC**), and
- mutual fund dealers (**MFDs**), who must, except in Quebec, be members of the Mutual Fund Dealers Association of Canada (**MFDA**).

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[1] This number excludes firms registered as MFDs or firms registered solely in the category of ID or other registration categories (commodity trading manager, futures commission merchant, restricted PM, and restricted dealer).

[2] This number includes firms registered as sole EMDs and EMDs also registered in other registration categories.

[3] This number includes firms registered as sole IFMs and IFMs also registered in other registration categories.

[4] This number includes firms registered as sole PMs and PMs also registered as EMDs, and in other registration categories.

[5] This number includes firms registered as sole SPDs and SPDs also registered as IFMs.

There are four dealer and adviser categories for firms trading in or advising on commodity futures:

- commodity trading adviser,
- commodity trading counsel,
- commodity trading manager, and
- futures commission merchant.

The OSC also registers firms and individuals in the category of MFDs and dealing representatives, and firms in the category of IDs, however, these firms and their registered individuals are directly overseen by the self-regulatory organizations (**SROs**) the MFDA and IIROC, respectively. Although this report focuses primarily on registered firms and individuals directly overseen by the OSC, firms directly overseen by the SROs should review Part 2 of the Annual Report as certain information would be applicable to them as well.

Although applications for registration are reviewed by CRR staff, we remind firms seeking registration in the category of ID, MFC or futures commission merchant to also apply separately for membership with the relevant SRO.

Part 1 OUTREACH TO REGISTRANTS

1.1 Registrant Outreach program and resources

Registrant Outreach since inception

54
In-person and webinar seminars held

4,055
Web replays viewed

10,407
Individuals that have attended in-person outreach sessions

95
E-mail blasts sent to registrants

We continue to interact with our stakeholders through our Registrant Outreach program, which was launched in 2013. The objectives of our Registrant Outreach program are to strengthen communication with Ontario registrants that we directly regulate and with other industry participants (such as lawyers and compliance consultants) to promote stronger compliance practices and to enhance investor protection.

- **Interested in attending an upcoming Registrant Outreach seminar?**
  Click here for our calendar of upcoming events.
- **Looking for information about regulation matters?**
  Take a look at our Registrant Outreach webpage or our Topical Guide for Registrants for help with key compliance issues and policy initiatives.
- **Want to be informed about newly released guidance?**
  Register to receive our e-mail blasts here.
- **Looking for a listing of recent e-mail blasts and links to each?**
  Refer to the OSC Compliance Reports, Staff Notices & E-mail blasts webpage.
- **Interested in reading previously published Director's Decisions?**
  Refer to the Director's Decisions webpage.

If you have questions related to the Registrant Outreach program or have suggestions for seminar topics, please send an e-mail to RegistrantOutreach@osc.gov.on.ca

1.2 Registration initiatives

Guide to completing and filing a firm application

To assist firms and individuals with navigating the registration process, the OSC's website was updated in 2017 to provide additional information with respect to getting registered with the OSC (http://www.osc.gov.on.ca/en/Dealers_getting-registered_index.htm) including a section outlining the process for submitting initial registration applications for firms and individuals (http://www.osc.gov.on.ca/en/Dealers_applying_index.htm).

Applicants are encouraged to review the Guide to Completing and Filing a Firm Application prior to submitting a registration application with the OSC. The guide also provides references to certain links that may assist the applicant during the application process.

Background checks

As of June 21, 2018 the OSC has commenced a United States (**U.S.**) background check procedure in partnership with Sterling Talent Solutions (**Sterling**), a provider of background screening products. This procedure will affect individual registration applications where an applicant has been resident in the U.S. at any time in the last 10 years prior to the date of the application.

In order to initiate this procedure, an individual applicant will be required to provide express consent to Sterling to conduct background checks. While Form 33-109F4 *Registration of Individuals and Review of Permitted Individuals* (**Form 33-109F4**) provides consent for the OSC to collect personal information, including contacting "private bodies or agencies, individuals, corporations and other organizations for information" about an applicant, part of Sterling's security and privacy policies require that all applicants provide express consent directly to Sterling.

Applicants will receive an e-mail from Sterling within 48 hours of filing their application on the National Registration Database (**NRD**). This e-mail will contain a secure link to an intuitive and user-friendly online portal where the consent may be provided.

Applicants are not required to consent to a U.S. background check, however not doing so may impact their ability to become registered in a timely manner, or in some cases, at all.

We are confident that this arrangement will assist us in conducting timely due diligence, thereby minimizing impact to registrants.

1.3 OSC LaunchPad

"OSC LaunchPad is committed to innovation for the long-term and we look forward to continuing our work with fintech businesses."

Pat Chaukos, Deputy Director

Our recent LaunchPad initiative is an example of developing a collaborative approach to respond to emerging issues. These actions are essential to reach solutions that balance the inclusion of innovation and competition in the marketplace while maintaining appropriate investor safeguards.

OSC Statement of Priorities 2018-2019

What we do

The pace of fintech innovation continues to accelerate and is a disruptive force in the financial services industry. Our goal is to keep regulation in step with digital innovation.

Since October 2016, OSC LaunchPad has actively engaged with novel fintech businesses to provide support in navigating regulatory requirements. OSC LaunchPad provides a forum to discuss proposed approaches, raise questions and educate fintech businesses about the regulatory requirements for which registration and/or exemptive relief may be needed.

OSC LaunchPad strives to achieve the following:

- Greater use of creative regulatory approaches (for example, limited registration and other exemptive relief) that provide an environment for innovators to test their products, services and applications.
- With the **CSA Regulatory Sandbox**, support the development of novel business models and facilitate more timely registration and exemptive relief processes for emerging firms.
- Provide a positive and supportive environment for fintech innovation and ensure investors are protected.

With a small, dedicated **core team** focused exclusively on fintech and an extended team with expertise from the various branches at the OSC, the OSC LaunchPad team focuses on three areas:

Engage with the fintech community	Offer eligible fintech businesses direct support in navigating regulatory requirements	Take learnings and apply them to similar businesses going forward

Are you eligible for support?

You are a fintech business that has not yet started operations or is in the process of applying to the OSC for registration or exemptive relief. ✔

You have a new innovation or significantly different product, service or application from those currently available. ✔

Your innovation will likely provide identifiable benefits to investors. ✔

You understand the necessity of investor protections and will invest time and energy in understanding and addressing them. ✔

For more information on **how to apply for direct support**, as well as the types of support we offer, please visit OSC LaunchPad's **dedicated site**.

OSC LAUNCHPAD

Key accomplishments in fiscal 2017-2018

242	Meetings held with fintech businesses and stakeholders
156	Requests for support received and direct support provided to fintech businesses
55	Events that OSC LaunchPad has hosted or participated in
25	Collaborative reviews with the CSA Regulatory Sandbox of novel business models that want to operate across Canada

Guidance & investor resources

- Working with the CSA Regulatory Sandbox, OSC LaunchPad published **CSA Staff Notice 46-307 *Cryptocurrency Offerings*** (August 2017), which provides guidance on how securities law requirements may apply to initial coin and token offerings, cryptoasset investment funds and cryptoasset trading platforms.

- We also published **CSA Staff Notice 46-308 *Securities Law Implications for Offerings of Tokens*** (June 2018), which provides additional guidance on the applicability of securities laws to offerings of coins and tokens, including ones commonly referred to as “utility tokens”.

- Through Canadian Securities Administrators (**CSA**) investor alerts, we remind investors of the **inherent risks associated with cryptoasset futures contracts** and the **need for caution when investing with cryptoasset trading platforms**.

- OSC LaunchPad continues to support our Investor Office in the publication of guidance to investors, as well as research studies, on relevant topics:
  - **Get Smarter About Money: Cryptocurrency Offerings**
  - **Ontarians and Cryptocurrencies: A First Look**
  - **Get Smarter About Money: Cryptocurrency Basics**
  - **Taking Caution: Financial Consumers and the Cryptoasset Sector**

Trends & decisions

Complexity driven by financial innovation offers many potential benefits and risks to the market. Fintech is leveraging new technology and creating new business models in the financial services industry such as providing new product offerings (blockchain-based cryptoassets) and disrupting service channels (online advisers).

After an initial focus on online advisers, online lenders and crowdfunding portals, industry focus has largely shifted to cryptoasset-related businesses, including:

- Initial coin and token offerings
- Cryptoasset investment funds
- Traditional financial service businesses utilizing blockchain technology
- Cryptoasset trading platforms

We are also seeing many businesses seeking to provide RegTech services, technology-based compliance solutions and data analytics services. In the past fiscal year, OSC LaunchPad has worked with the CSA Regulatory Sandbox to approve a variety of innovative products and services, including:

- Initial coin and token offerings
- Cryptoasset investment funds
- Algorithmic trading platform
- New product offering by an online adviser

The **full list** of approved novel products and services can be found on OSC LaunchPad's **dedicated site**.

International co-operation highlights

The OSC, together with the CSA, entered into co-operation agreements with the **Abu Dhabi Global Market Financial Services Regulatory Authority** and the **France Autorité des Marchés Financiers** concerning co-operation and information sharing between authorities regarding their respective innovation functions. This adds to similar agreements entered into with the **Australian Securities and Investments Commission** and the **U.K. Financial Conduct Authority**.

Part 2 INFORMATION FOR DEALERS, ADVISERS AND INVESTMENT FUND MANAGERS

"The foundation of a strong culture of compliance begins with a commitment of resources and a tone from the top."

Felicia Tedesco, Deputy Director

Protect investors and foster confidence in our markets by upholding strong standards of compliance with our regulatory framework.

OSC Statement of Priorities 2018-2019

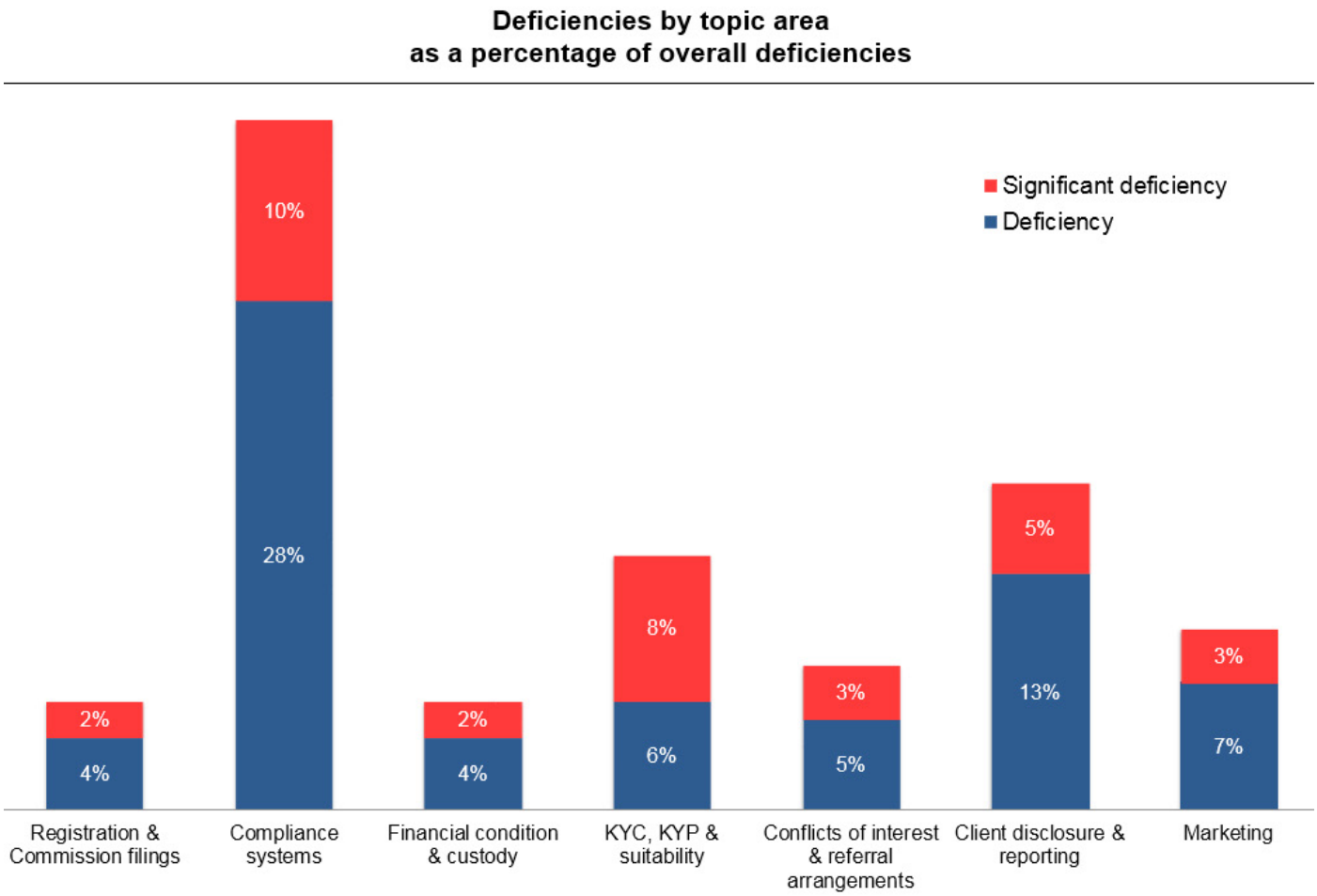
How to navigate Part 2 of the Annual Report

Section 2.1 - Annual highlights

Part 2 of the Annual Report provides an overview of the key findings and outcomes from compliance reviews conducted during the 2017/2018 fiscal year. Section 2.1 provides information specific to registered dealers, advisers and IFMs and discusses, at a high level, some of the key compliance reviews completed during the fiscal year.

Section 2.2 - Registration and compliance deficiencies

In contrast to prior versions of the annual report, this year's report categorizes our guidance for all registrant categories into 7 topic areas. The following chart illustrates the focus areas of our compliance reviews during fiscal 2017/2018, noting common deficiencies identified within each of the 7 topic areas, including those considered significant.



Which guidance applies to me?

The highlights section in 2.1 provides readers with a direct link between the key compliance reviews conducted, the guidance issued as a result of our findings and a list of the registration categories that the guidance applies to. In addition, in section 2.2, registration categories are listed beside each deficiency heading to indicate the information is relevant to firms registered in this capacity.

Registrants also have the option of navigating through section 2.2 of the Annual Report by topic area. Scroll over and click each of the topic areas listed below to access information on that topic.

Sections 2.2.1 to 2.2.7 discuss the most commonly identified deficiencies, suggested best practices (and unacceptable practices) and specify applicable legislation and guidance to assist firms in addressing each of the deficiency topic areas.

We encourage registrants to review all the information set out in Part 2 of this report as the guidance presented may be helpful to registration categories other than those listed.

2.1 Annual highlights

a) Senior suitability review

b) Client Relationship Model Phase 2 (CRM2) review

c) Expenses charged to investment funds review

d) Sales practices review

e) Scholarship plans review

f) Inappropriate capital raising activity by registrants

g) Excessive fees cases

h) Protection from reprisals review

i) Registration as the first compliance review

j) Targeted reviews

WHAT WE DID	GUIDANCE	REGISTRANTS

a) SENIOR SUITABILITY REVIEW

In 2017, we conducted a sweep of 20 PM and 10 EMD firms that provided investment advisory services or sales of products to a significant proportion of clients over the age of 60. We wanted to determine if registered firms had an appropriate compliance system and supervisory controls that were designed to effectively address the particular needs of older investors with the objective of protecting them from potential financial harm.

As part of the OSC Seniors Strategy, more detailed guidance will be developed to assist firms and their representatives to effectively manage their relationship with senior clients.

- section 2.2.2 (page 36)
- section 2.2.4 (page 48)

✔ PM

✔ EMD

✔ SPD

b) CRM2 REVIEW

The CRM2 review focused on assessing a firm's policies and procedures on client reporting and reviewing a sample of client statements, reports on charges and other compensation and investment performance reports. Registered firms selected for the desk review included 10 PMs, 5 EMDs and 15 registered firms maintaining registration under multiple categories.

- section 2.2.2 (page 38)
- section 2.2.6 (page 64)

✔ PM

✔ EMD

✔ SPD

"We engage with our PM registrants on a continuous basis, striving to provide them with appropriate flexibility to develop and adapt their business models while fostering best practices in compliance."

Elizabeth Topp, Manager
Portfolio Manager Team

WHAT WE DID	GUIDANCE	REGISTRANTS

c) EXPENSES CHARGED TO INVESTMENT FUNDS REVIEW

In 2017, we conducted a review of fees and expenses charged to investment funds by IFMs (the **expense desk review**). We selected 20 IFMs to participate in the expense desk review.

The expense desk review focused on assessing whether an IFM had properly developed, implemented and disclosed adequate policies and procedures to validate that the investment funds they managed were only charged fees and expenses related to the daily operation of the investment fund. We had previously conducted a similar review in 2014 as reported in OSC Staff Notice 33-743 *Guidance on sales practices, expense allocation and other relevant areas developed from the results of the targeted review of large investment fund managers* (**OSC Staff Notice 33-743**). The notice provides guidance on acceptable types of fees and expenses that can be allocated to investment funds.

- section 2.2.2 (page 43)
- OSC SN 33-743

✔ IFM

d) SALES PRACTICES REVIEW

In 2017, we continued to work with the Enforcement Branch to reach settlement agreements with registrants regarding the sales practices of industry participants in connection with the distribution of publicly offered mutual funds. Our work focused on sales practices that could be perceived as inducing dealers and their representatives to sell mutual fund securities on the basis of incentives they were receiving, rather than on the basis of what was suitable for and in the best interests of their clients.

- section 2.2.5 (page 56)

✔ IFM

✔ SPD

✔ MFD

✔ ID

WHAT WE DID	GUIDANCE	REGISTRANTS

e) SCHOLARSHIP PLANS REVIEW

We conducted compliance reviews of a sample of firms registered as SPDs as well as the affiliated IFMs of the scholarship plans. Areas of concern identified from the recent reviews include but are not limited to:

- the use of misleading or inaccurate marketing materials,
- inadequate branch oversight,
- inadequate insurance coverage,
- inadequate designation of trust accounts and commingling of investment fund assets,
- inadequate oversight of service providers,
- charging inappropriate expenses to investment funds, and
- inadequate interaction with and execution of Independent Review Committee (**IRC**) duties and obligations.

We are in the process of reporting the findings from these reviews to each firm. As is our normal process, depending on the deficiencies identified during a review, we may consider further regulatory action to remediate the deficiencies.

- section 2.2.2 (page 41-44)
- section 2.2.3 (page 45-47)
- section 2.2.5 (page 54-55)
- section 2.2.7 (page 66)

✔ IFM

✔ SPD

"We encourage an open dialogue with registrants and invite them to reach out to us to discuss current issues and developing trends."

Dena Staikos, Manager
Dealer Team

WHAT WE DID	GUIDANCE	REGISTRANTS
f) INAPPROPRIATE CAPITAL RAISING ACTIVITY BY REGISTRANTS We implemented additional review procedures when reviewing a registrant's financial statements filed with us. The objective of the additional procedures are to identify potentially problematic capital raising activities such as registrants issuing shares or debt of themselves to retail investors directly or indirectly through the investment funds they manage. Areas of concern include: • unsuitable investments, posing the risk of investor harm • prohibited distributions to investors (when no prospectus exemption is available)	• section 2.2.3 (page 45)	✔ IFM ✔ PM ✔ EMD ✔ SPD
g) EXCESSIVE FEES CASES We continued to work with the Enforcement Branch to reach no-contest settlements related to certain registrant practices that resulted in excessive fees being charged to clients over an extended period of time.	This initiative was discussed in detail in section 3.1(c)(vii) of OSC Staff Notice 33-748 *Annual Summary Report for Dealers, Advisers and Investment Fund Managers* (OSC Staff Notice 33-748)	✔ IFM ✔ PM ✔ EMD ✔ SPD

WHAT WE DID	GUIDANCE	REGISTRANTS

h) PROTECTION FROM REPRISALS REVIEW

We completed desk reviews of 30 registered firms to assess compliance with the provisions in section 121.5 - *No Reprisals* of the *Securities Act* (Ontario) (the **Act**). We identified a number of employee agreements that contained inappropriate language.

- section 2.2.2 (page 35)

- ✔ IFM
- ✔ PM
- ✔ EMD
- ✔ SPD

i) REGISTRATION AS THE FIRST COMPLIANCE REVIEW

As part of our review of initial firm registration applications or proposals to change a registered firm's business, we conducted 52 in-person meetings or calls with firms this year.

The purpose of these reviews is to facilitate mutual understanding of:

- the business model the firm plans to adopt,
- some of the key compliance issues a new firm might face, especially if planning to offer an online platform, and
- resources the OSC makes available to new firms, pre and post-registration.

- section 1.2 (page 10)

- ✔ IFM
- ✔ PM
- ✔ EMD
- ✔ MFD
- ✔ ID

"As gatekeepers, the Registration team operationalizes the registration regime by evaluating initial and ongoing fitness for registration based on the principles outlined in section 2.1 of the Act."

Louise Brinkmann, Manager
Registration Team

WHAT WE DID	GUIDANCE	REGISTRANTS

j) TARGETED REVIEWS

We conducted targeted compliance reviews of registered IFMs, PMs and EMDs using a risk-based approach and identified additional areas requiring guidance on registration and compliance issues including:

- not-for-profit organizations distributing securities,
- incorrect calculation of participation fees by registered firms,
- inadequate delivery of offering documents under the offering memorandum exemption,
- non-disclosure of outside business activities,
- inadequate compliance system,
- inadequate policies and procedures,
- inappropriate use of IFM registration,
- inadequate oversight of related party service providers,
- inadequate assessment of conflicts of interest,
- misleading marketing materials,
- inadequate working capital and/or insurance,
- inadequate relationship disclosure information, and
- inadequate control over the safeguarding of client assets.

- section 2.2.1 (page 27)
- section 2.2.2 (page 34)
- section 2.2.3 (page 45)
- section 2.2.4 (page 48)
- section 2.2.5 (page 53)
- section 2.2.6 (page 64)
- section 2.2.7 (page 66)

- ✔ IFM
- ✔ PM
- ✔ EMD
- ✔ SPD

"The IFM team is committed to helping fund managers succeed in meeting their obligations as registrants."

Vera Nunes, Manager
Investment Fund Manager Team

2.2 Registration and compliance deficiencies

2.2.1 Registration & Commission filings

2.2.2 Compliance systems

2.2.3 Financial condition & custody

2.2.4 Know your client (KYC), Know your product (KYP), & suitability

2.2.5 Conflicts of interest & referral arrangements

2.2.6 Client disclosure & reporting

2.2.7 Marketing

2.2.1 Registration & Commission filings

The registration requirements under securities law help to protect investors from unfair, improper or fraudulent practices by participants in the securities markets. In general, firms must register with the OSC if they:

- are in the business of trading in, or advising on, securities. This is referred to as the 'business trigger' for registration,
- act as an underwriter or as an IFM, or
- conduct trading and advising activities involving commodity futures contracts or commodity futures options.

a) Issuers directly offering securities (pre-registration)

We remind entities that offer their own or an affiliate's securities to continually reassess whether they are in the business of trading or advising and thus require registration. This activity does not have to be the entity's sole or even primary endeavour for it to be considered in the business of trading in, or advising on, securities.

Some of the factors we review to determine if the business trigger has been met include:

- how frequently Form 45-106F1 *Report of Exempt Distribution* filings are filed without reference to a registered dealer, since this raises the concern that trading activity is being conducted with repetition, regularity or continuity,
- entities that appear to be directly soliciting by advertising their securities offerings to prospective investors,
- using the internet, including public websites and discussion boards, to reach a large number of potential investors,
- employees of an entity actively soliciting the public for the purpose of selling that entity's securities, possibly with employees dedicated to the role of capital-raising,
- entities that raise large sums of capital from the general public through the distribution of securities.

More information about the factors that we consider to be relevant in determining whether an individual or entity is trading in, or advising on, securities for a business purpose and, therefore, subject to the dealer or adviser registration requirements, is set out in section 1.3 of NI 31-103CP.

The distribution of securities may also be subject to the prospectus requirements unless a prospectus exemption is available. When relying on a prospectus exemption, the issuer is responsible for determining whether the terms of the prospectus exemption are met at the time of the trade and that adequate supporting documentation to support the availability of the prospectus exemption is retained.

Legislative reference and guidance

- NI 31-103
- Companion Policy 31-103CP *Registration Requirements, Exemptions and Ongoing Registrant Obligations* (NI 31-103CP)
- Section 1.9 of National Instrument 45-106 *Prospectus Exemptions* (NI 45-106)
- Companion Policy 45-106CP *Prospectus Exemptions* (NI 45-106CP)

b) Not-for-profit organizations distributing securities (pre-registration)

We are aware of several not-for-profit organizations that, on a regular basis, directly solicit and sell investment opportunities to community members associated with the organization, including retail investors. These financing activities are sometimes done through a separate corporate entity that may or may not be organized as a not-for-profit entity. In particular, we have considered requests for exemptive relief from certain not-for-profit organizations that continually raise and pool capital, which is subsequently used to provide mortgages for the acquisition, construction, or renovation of houses of worship, homes for their leaders, and other places for their organization's activities such as schools, camps, and other similar programs. We encourage other not-for-profit organizations engaging in similar financing activities and their counsel to contact us to discuss the issues discussed below and potential options, including applying for exemptive relief.

i) Business model and financing activities

It is our understanding that not-for-profit organizations have established investment programs to provide these mortgage services because their borrowers (who are usually affiliated with the not-for-profit organization) generally have difficulty accessing financing at reasonable rates, if at all, from banks and other commercial lenders. The primary source of capital used by these organizations to fund mortgages or loans is selling securities to their community members. Typically, donations are not solicited or used to fund the mortgages or loans.

The activities of these organizations are not targeted to a specific project (e.g., a single faith group fundraising for the renovation of their own house of worship) but involve more general capital raising programs (e.g., for the provincial or national community). These more general capital raising investment programs are similar to those of mortgage investment entities that pool capital raised from investors and use that capital to provide loans to borrowers who are unable to access conventional mortgage financing. These organizations typically originate and administer these loans or mortgages and they earn a spread between the interest charged to borrowers and the interest paid to investors. This spread or profit is often used to pay for the organization's expenses from operating this program and the excess may be used for various purposes, including funding more mortgages, establishing a reserve fund for possible mortgage defaults, returning monies to current borrowers in the mortgage pool, or funding other programs of the organization.

We have been working with several of these organizations to ensure compliance with securities law requirements, including: (i) their or the separate corporate entity's registration as dealers and (ii) their reliance on available prospectus exemptions or discretionary relief. As an example, see the decision *In the Matter of Pentecostal Financial Services Group Inc., Pentecostal Securities Corp. and The Pentecostal Assemblies of Canada, (2017) 40 OSCB 8504*.

ii) Investor protection concerns

While acknowledging that these not-for-profit organizations may wish to engage in certain general capital raising activities through offering securities to their community members, Staff are concerned that, in certain circumstances, these activities are not being undertaken in compliance with applicable securities law (both registration and prospectus requirements) and may raise potential investor protection concerns, including the following:

- Investors may be provided with limited information about the securities being sold and the marketing materials provided may be overly promotional.

b) Not-for-profit organizations distributing securities (cont'd)

- Investors may not be provided with any disclosure of conflicts of interest.
- There may not be an assessment of whether the investment is suitable for the investor, and if there is such an assessment, it may not be adequate.
- Selling persons may lack proficiency as they may not have taken any securities related courses and may not have any securities related experience.
- Investors may not be experienced investors (i.e., very limited or no investing experience).
- Investors may be asked to invest based on appeals to support the mission of the not-for-profit organization, which raises the possibility for affinity fraud.

iii) Registration as dealers

When these organizations have formal or sophisticated capital raising and securities distribution programs, originate or administer loans or mortgages as part of these programs, and pool capital to invest in opportunities that do not necessarily directly benefit the community members that are solicited to invest (e.g., not raising funds necessarily for the camp that the investors' children will be attending that summer), we typically are of the view that they require registration as dealers because they are in the business of trading in securities.

For example, these organizations solicit investors (often retail) through word-of-mouth, webpages and/or community brochures, and carry on their capital raising and lending activities (which are similar to other registered firms) with repetition and regularity. As noted in section 1.3 of NI 31-103CP, the following factors, among others, are relevant to the registration business purpose analysis:

- having the capacity or ability to carry on the organization's activities to produce profit,
- the various sources of income for the organization,
- the amount of time the organization spends on the activities associated with the trading activity,
- soliciting investors or potential investors, and
- expecting to be remunerated or compensated.

Any one of the above factors on its own is not determinative of whether an individual or firm is in the business of trading securities.

Although not-for-profit organizations are not established for the purposes of earning a profit, a not-for-profit organization may engage in activities that result in income or profit and may carry on a business similar to "for profit" organizations. However, as a not-for-profit entity, the income or profits must only be used to carry out the goals and objectives of the organization and may not be paid to or made available for the personal benefit of any of its members or securityholders. Being a not-for-profit entity does not prevent the organization from being in the business of trading in securities.

There is no available exemption from the dealer registration requirement for these not-for-profit organizations. Further, if these organizations are not registered as dealers, there is no available exemption from the adviser registration requirement in respect of any incidental advice provided by the organization in connection with a trade in its securities.

However, depending on the organization's business model, we may consider exemptive relief from certain requirements, if they are not appropriate for this type of business model and if our concerns can otherwise be adequately addressed.

b) Not-for-profit organizations distributing securities (cont'd)

iv) Availability of not-for-profit issuer prospectus exemption

Given the extent and sophistication of the capital raising programs run by these not-for-profit issuers, Staff view these organizations' financing activities to likely be beyond the scope and intent of the not-for-profit issuer prospectus exemption in section 2.38 of NI 45-106 because this exemption requires that, among other things, issuers be organized exclusively for educational, benevolent, fraternal, charitable, religious or recreational purposes and not for profit. That is, to use this exemption, issuers must be organized exclusively for one or more of the listed purposes and use the funds for these purposes.

The guidance in section 4.8 of NI 45-106CP indicates that if one of the not-for-profit organization's mandates is to provide an investment vehicle for its members, or if over time an organization that was initially organized for a listed purpose devotes more and more of its efforts to lending money or other capital raising activities, then the not-for-profit organization may be unable to rely upon section 2.38 of NI 45-106.

In considering whether a not-for-profit organization may appropriately rely on the exemption in section 2.38 of NI 45-106, we may not consider an issuer's status as a registered charity to be determinative and the following factors may also be considered:

- The extent, frequency and scope of the issuer's capital raising activities to its community members and whether such activities extend beyond its community.
- The nature of the securities offered and whether these securities are offered with an investment purpose or are held in registered accounts (e.g., RRSPs, RRIFs, etc.).
- The stated purposes of the issuer in their articles of incorporation, charter or other organizational documents, in particular, whether capital raising or providing financing to other persons is a listed purpose of the issuer.
- Whether the issuer is established solely to lend money or to carry on a business, even if for an educational, benevolent, fraternal, charitable, religious or recreational motive.

The presence of any or a combination of these factors may suggest an issuer is not organized exclusively for educational, benevolent, fraternal, charitable, religious or recreational purposes and, consequently, the issuer's activities would not fall within the intended scope of the prospectus exemption in section 2.38 of NI 45-106.

Under these circumstances, we are of the view that these organizations fall outside of the scope of the exemption in section 2.38 of NI 45-106 and should instead rely on other available prospectus exemptions to offer securities, such as:

- the accredited investor exemption (set out in section 73.3 of the Act and section 2.3 of NI 45-106),
- the offering memorandum exemption (set out in section 2.9 of NI 45-106), and
- the friends, family and business associates exemption (set out in section 2.6.1 of NI 45-106).

Issuers may also apply for discretionary exemptive relief to accommodate the use of a restricted dealer to conduct suitability assessments in connection with the investment limits for eligible investors under the offering memorandum exemption or to otherwise accommodate the issuer's specific business model.

c) Calculation of participation fees paid by registered firms (IFM / PM / EMD / SPD)

Over the last year, we have seen a number of registered firms improperly deducting certain amounts from their "specified Ontario revenues" when determining their participation fees under OSC Rule 13-502 *Fees* (the **Fee Rule**).

A registered firm is required to remit, by December 31 of each year, the participation fee shown in Appendix B to the Fee Rule opposite the firm's "specified Ontario revenues" for the previous financial year of the firm.

Although a registered firm is permitted to deduct certain revenues not attributable to "capital markets activities", as defined in the Fee Rule, we have seen a number of registered firms deducting fees that fall within the definition of capital markets activities, such as origination fees and renewal fees paid to a registered firm in connection with mortgage financings.

We remind registered firms that the term "capital markets activities", as defined in the Fee Rule, means activities for which registration is required, or activities for which an exemption from registration is required under the Act or under the *Commodity Futures Act* (Ontario), or would be so required if those activities were carried out in Ontario.

Although subsection 35(4) of the Act and section 8.12 of NI 31-103 include an exemption from the registration requirement in respect of a trade in a mortgage on real property in Canada by a person or company registered or licensed under mortgage broker legislation in Canada, to the extent a registered firm engages in such activities, these activities would be considered capital markets activities. Accordingly, a registered firm is not permitted to deduct any revenues paid in connection with such activities.

We remind all registered firms to validate that all "specified Ontario revenues" from "capital markets activities" are being appropriately captured in their calculation for participation fees, as prescribed within the Fee Rule.

d) Outside business activities (IFM / PM / EMD / SPD)

Registrants must notify the Commission of updates to Item 10 of Form 33-109F4, including outside business activities (**OBAs**). Section 4.1(1)(b) of NI 33-109 requires a registered or permitted individual to notify the Commission of changes to information previously submitted in a Form 33-109F4, within 10 days of the change, including the information in Item 10 of Form 33-109F4. Item 10 requires a list and description of all current business and employment activities, including all officer or director or equivalent positions.

Item 10 also requires disclosure with respect to positions of influence, which can include religious roles, teaching roles, medical or personal care roles, as well as acting as a coach for national or elite-level athletes. We sometimes receive filing updates from registrants that include OBAs for coaching recreational or "house league" sports. This is generally not required to be reported and is generally not viewed to be a position of influence.

d) Outside business activities (cont'd)

We have met with certain registered firms during the year to discuss registration-related matters, including discussion of the types of activities and positions required to be disclosed for Item 10. Based on these discussions and trends identified in the year, firms should be aware of the following:

- failure to meet the filing deadlines set out in NI 33-109 can result in the firm incurring significant late fees, and
- certain OBAs may require terms and conditions be placed on the registrant.

Legislative reference and guidance

- National Instrument 33-109 *Registration Information* (**NI 33-109**)
- Companion Policy **33-109CP** *Registration Information*
- Annual Summary Reports for Dealers, Advisers and Investment Fund Managers from prior years (**2011 - 2017**)

e) Inappropriate outsourcing of IFM responsibilities (IFM)

During the course of our reviews, we identified instances of registered firms inappropriately entering into an arrangement with other unrelated registered firms (i.e. EMDs, IIROC dealer members, MFDA member firms) responsible for the distribution of investment funds managed by the IFM. The following issues resulted from this arrangement:

- the IFM performed limited activity while the dealer took numerous actions directing the business, operations and affairs of the investment funds including, but not limited to:
    - preparing the offering memorandum in conjunction with external legal counsel,
    - directly providing seed capital for the investment funds,
    - indirectly making decisions on fund investments and managing the status of the investments,
    - having and exercising signing authority over the bank accounts of the investment funds,
    - engaging the service providers for the daily fund administration of the investment funds,
    - engaging an auditor to prepare the year-end audited financial statements of the investment funds, and
    - collecting the majority of the fees related to an investment in the investment fund.

The distributing dealer appeared to be the mind and management of the investment funds directing the business activities and operations of the funds.

Per subsection 1(1) of the Act, an investment fund manager is defined as a person or company that directs the business, operations or affairs of an investment fund.

e) Inappropriate outsourcing of IFM responsibilities (cont'd)

IFMs should:

- be involved in every aspect of the daily operations of an investment fund they manage. This includes, but is not limited to:
  - engaging service providers required to fulfill the key responsibilities of an investment fund,
  - establishing and implementing policies and procedures to actively oversee all service providers,
  - overseeing the service providers to confirm that all duties and responsibilities outsourced to them are conducted in accordance with securities law,
  - drafting and approving any legal documentation relating to the investment funds, and
  - reviewing and approving all aspects regarding fund administration.
- validate that each party involved with the investment fund is adequately executing their duties and responsibilities within the parameters of their registration category.

IFMs should not:

- allow other firms that are not registered as the IFM of the investment funds (i.e. EMD or other dealers (IIROC or MFDA) involved in the distribution of the investment funds, or PMs engaged to manage and execute trades in relation to the assets of the investment fund), to direct the business, operations or affairs of an investment fund it manages, and
- outsource the responsibility of overseeing the fund administration activities of an investment fund that it manages to another entity.

Legislative reference and guidance

- Part 11 - *Division 1 Compliance* of NI 31-103 and related NI 31-103CP
- Definition of investment fund manager per subsection 1(1) of the Act

2.2.2 Compliance systems

A registered firm must have a system of controls and supervision to provide reasonable assurance that the firm, and individuals acting for it, comply with securities law and prudently manage the risks associated with its business. An effective compliance system establishes, maintains and applies policies and procedures to ensure that a system of supervisory controls is in place.

a) Inadequate compliance system (IFM / PM / EMD / SPD)

We continue to have concerns that some registered firms are not establishing an adequate compliance system, based on the types of significant deficiencies we identify. We also continue to identify instances where a firm's UDP and/or CCO are not adequately meeting their stated regulatory obligations.

There are serious consequences when registered firms have deficiencies of this nature. In addition to requiring the registered firm to correct its deficiencies, we may also take further regulatory action, including:

- requiring the registered firm to hire an external compliance consultant to correct the deficiencies and to strengthen the firm's compliance system,
- requiring the registered firm to replace its CCO and/or UDP,
- requiring the registered firm to stop accepting new clients, new investments from existing clients and/or creating new investment funds,
- referring the matter to the Enforcement Branch, and/or
- suspending the firm's registration.

Registered firms should:

- create a compliance system that:
  - is appropriately tailored to the nature, size and risk of the firm's operations,
  - uses a risk-based approach to monitor and test compliance with the firm's policies and procedures,
  - proactively identifies and promotes the timely correction of non-compliance,
  - documents results and actions taken in compliance activities,
  - identifies and manages key risks, including risks related to new products or services, new locations, technology changes and changes to regulatory obligations, and
  - requires periodic self-assessments of compliance with securities law and acts to improve internal controls, monitoring, supervision and policies and procedures when necessary.

Legislative reference and guidance

- Part 11 - *Division 1 Compliance* of NI 31-103 and related NI 31-103CP
- Section 4.1.2 of OSC Staff Notice 33-742 *2013 OSC Annual Summary Report for Dealers, Advisers and Investment Fund Managers* (OSC Staff Notice 33-742)
- OSC E-mail blast (May 2012) - *Concerns about inadequate compliance systems and Chief Compliance Officers not adequately performing responsibilities*
- Registrant Outreach seminar (June 2015) - *Elements of an effective compliance system*

b) Protection from reprisals (IFM / PM / EMD / SPD)

We conducted a desk review of registered firms to review their compliance with provisions in section 121.5 of the Act, which came into force on June 28, 2016. The objective of the review was to identify restrictive provisions in employment contracts, severance agreements, confidentiality agreements and other related documents, which seek to preclude or purport to preclude employees from reporting violations of securities law to the OSC, SROs or law enforcement agencies. We selected a sample of 30 registered firms with a larger number of registered individuals, including firms registered as IFMs, PMs, and EMDs.

Overall, we found that a significant portion of the firms reviewed had employment agreements that contained inappropriate language. Specifically, we identified language that may inhibit possible disclosure to the OSC, SROs or law enforcement agencies. Furthermore, certain registered firms' policies and procedures, as well as other agreements and documents, contained provisions which preclude or purport to preclude whistleblowers from coming forward.

Registered firms should:

- review employment contracts, severance agreements, confidentiality agreements and other related documents to confirm that they do not contain provisions which preclude or purport to preclude whistleblowers from reporting securities law violations, including language that:
    - allows disclosure "only as required by law",
    - limits the types of information that an employee may report,
    - prohibits any and all disclosure of information, without an exception for reporting potential violations of securities law,
    - requires representations that an employee has not assisted in any investigation involving their employer,
    - requires notification or consent from an employer prior to reporting information, and
    - permits disclosure only for "good faith" reports but is silent as to how the firm will assess that a report is made in good faith.
- conduct appropriate remediation efforts in the event agreements containing provisions which preclude or purport to preclude whistleblowers from coming forward are identified. Remediation efforts may include:
    - the revision of agreements and other documents on a prospective basis to clarify that they will not prohibit employees from voluntarily communicating with the OSC, an SRO, a law enforcement agency, or from receiving a whistleblower award,
    - the distribution of general notices to employees who signed restrictive agreements, to inform them of their rights to contact the OSC, an SRO, a law enforcement agency, or to receive a whistleblower award,
    - contacting former employees who signed restrictive agreements to inform them that they are not prohibited from communicating with the OSC, an SRO, a law enforcement agency, or from receiving a whistleblower award.
- establish policies and procedures for reviewing and approving any and all such agreements to confirm that they do not contain provisions which preclude or purport to preclude whistleblowers from coming forward.

b) Protection from reprisals (cont'd)

Registered firms should (cont'd):

- review their internal compliance systems to determine whether a culture of compliance is being fostered. As part of this exercise, firms may also want to assess the availability and appropriateness of employee reporting channels to encourage potential whistleblowers to report misconduct internally and to allow the organization to investigate and remediate as appropriate.

c) Inadequate policies and procedures

(i) Senior investors (PM / EMD / SPD)

Staff conducted a focused sweep and approximately 90% of the firms reviewed did not have any written policies and procedures for dealing with seniors and vulnerable investors (for example investors with diminished capacity, severe or long term illness, mental or physical impairment, language barrier). Although the majority of firms were aware of the challenges associated with servicing senior clients, they had not established any written procedures or guidelines nor provided any training programs to their staff on how to identify and address issues such as potential financial abuse, diminished mental capacity and the misuse of a power of attorney (**POA**). As well, the firms did not have a clear definition of what they considered to be a senior or vulnerable client.

While we do not expect firms and their staff to be experts in identifying clients with suspected financial abuse or cognitive impairment issues, they should have adequate procedures and oversight controls to address these issues as they arise. When developing policies and procedures surrounding the sharing of client information with third parties, we remind firms to be cognizant of the potential implications of privacy legislation and develop controls to minimize the risk.

Through our discussions with the firms' CCOs and advising representatives, a small number of them indicated they had experienced difficulty when servicing clients that had suffered from diminished capacity or suspected financial abuse. In each case, they exercised their professional judgment and took appropriate steps to protect their clients such as consulting with their compliance staff or legal counsel and acting in a manner consistent with their obligations to deal fairly, honestly and in good faith with their clients.

Most advising representatives that we interviewed have known their senior clients, including their family members, for a long period of time. As such, they also maintain records of an emergency contact person on file. However, some of them expressed concerns about the difficulty in detecting clients with potential cognitive impairment issues or who may be victims of financial abuse. At times, they also found it challenging to share sensitive information with the clients' family members given existing privacy legislation.

c) Inadequate policies and procedures (cont'd)

(i) Senior investors (cont'd)

PMs, EMDs and SPDs should:

- develop policies and procedures specific to senior investors that:
  - define a senior or vulnerable investor,
  - provide training to staff on how to:
    - communicate with senior investors and document any verbal discussions,
    - recognize signs of financial abuse and cognitive impairment,
    - respond to identified issues of financial abuse and cognitive impairment,
    - interact with clients who show signs of diminished capacity or financial abuse,
    - identify the potential misuse of a POA and how to document the suspected misuse,
  - provide staff with a list of red flags that may suggest potential diminished capacity, financial abuse or the misuse of a POA,
  - instruct staff on how to escalate issues about a client with potential diminished capacity, financial abuse or the misuse of a POA to the CCO,
  - identify how, in the case of a client with potential diminished capacity, financial abuse or the misuse of a POA, the account will continue to be managed,
  - identify cases where it may be appropriate or necessary that the firm seek legal advice when dealing with an escalated issue,
  - describe when a POA may be necessary, and
  - outline how to verify the existence of a POA document and how to maintain an up-to-date version of the document.

Legislative reference and guidance

- Sections 13.2 *Know your client* and 13.3 *Suitability* of NI 31-103 and related NI 31-103CP
- CSA Staff Notice 31-336 *Guidance for Portfolio Managers, Exempt Market Dealers and Other Registrants on the Know-Your-Client, Know-Your-Product and Suitability Obligations* (CSA Staff Notice 31-336)

c) Inadequate policies and procedures (cont'd)

(ii) Cyber security (IFM / PM / EMD / SPD)

In the fall of 2016, CRR staff, along with staff from other CSA jurisdictions, sent a survey to gather detailed information about the cyber security and social media practices of firms. In October 2017, the CSA published the results of the survey, along with high level guidance for registered firms, in CSA Staff Notice 33-321. During compliance reviews, CRR staff continue to review the cyber security preparedness of firms relating to potential cyber-attacks and other cyber security incidents.

Registered firms should:

- have policies and procedures to identify which information and systems the firm needs to protect and outline the ways they are protected,
- train employees on the firm's cyber security policies and procedures as employees are often the first line of defense against an attack,
- have an incident response plan to respond to and escalate a cyber security incident that details what steps a firm will take when it is attacked, and
- review the cyber security policies and procedures of third party service providers used by the firm.

Legislative reference and guidance

- Section 11.1 - *Compliance system* of NI 31-103 and related NI 31-103CP
- CSA Staff Notice 33-321 *Cyber Security and Social Media*
- CSA Staff Notice 11-332 *Cyber Security*
- CSA Staff Notice 11-326 *Cyber Security*

(iii) CRM2 (IFM/ PM / EMD / SPD)

In 2017, and into 2018, staff conducted a focused desk review to assess compliance with the client reporting requirements in Part 14 *Handling client accounts - firms* of NI 31-103. We identified inadequate or no policies and procedures for client reporting in addition to ineffective internal controls over client reporting.

c) Inadequate policies and procedures (cont'd)

(iii) CRM2 (cont'd)

Registrants should:

- develop tailored policies and procedures covering the following areas, if applicable:
  - method of determining market value of different types of securities,
  - method of determining security position cost,
  - preparation of:
    - trade confirmations,
    - account statements,
    - additional statements,
    - report on charges and other compensation, and
    - investment performance reports,
  - if a SPD, the preparation of scholarship plan dealer statements,
  - if a PM, procedures relating to PM-IIROC dealer-member service arrangements,
  - if an IFM, the preparation of security holder statements, and
  - if an IFM, the duty to provide information to dealers and advisers.

Legislative reference and guidance

- Section 11.1 - *Compliance system* of NI 31-103 and related NI 31-103CP
- Part 14 *Handling client accounts - firms* of NI 31-103 and related NI 31-103CP
- CSA Staff Notice 31-345 *Cost Disclosure, Performance Reporting and Client Statements - Frequently Asked Questions and Additional Guidance*
- CSA Staff Notice 31-347 *Guidance for Portfolio Managers for Service Arrangements with IIROC Dealer Members* (CSA Staff Notice 31-347)

(iv) Best execution (PM / EMD)

Registered firms must meet the requirements of section 4.2 of NI 23-101 which states that a dealer and an adviser must make reasonable efforts to achieve best execution when acting for a client. As defined in section 1.1 of NI 23-101 the term "best execution" means the most advantageous execution terms reasonably available under the circumstances.

Section 4.1 of NI 23-101CP further describes the obligation to achieve best execution. A dealer or an adviser should be able to demonstrate that it has abided by policies and procedures designed to meet its best execution obligations.

c) Inadequate policies and procedures (cont'd)

(iv) Best execution (cont'd)

PMs and Dealers should:

- have written best execution policies and procedures tailored to their business that:
  - outline the process they have designed toward the objective of achieving best execution,
  - describe how the firm evaluates whether best execution was obtained, and
  - adequately identify and address conflicts of interest arising from trading activities, such as using an affiliated dealer.
- provide training to employees on the firm's best execution policies and procedures,
- review the policies and procedures regularly and vigorously to confirm they are still designed to reasonably achieve best execution on behalf of client trades,
- periodically evaluate, on a sufficiently timely basis, whether best execution was achieved for client trades,
- maintain adequate books and records to demonstrate:
  - the steps taken to evaluate whether best execution was achieved for client trades, and
  - that policies and procedures were reviewed and updated as necessary.
- consider factors for achieving best execution to be considered by dealers if directly accessing a marketplace for a client trade.

PMs and Dealers should not:

- provide misleading or inaccurate disclosure to clients regarding the firm's processes to achieve best execution,
- rely on a dealer's best execution obligation or policies and procedures when executing client trades to satisfy their own best execution obligation, and
- unnecessarily interpose another party between the PM and the dealer or marketplace through which best execution can be achieved for client trades, for example, by directing commissions to a dealer not involved in executing the trade to compensate them for referred clients.

Legislative reference and guidance

- Sections 1.1 and 4.2 of NI 23-101 *Trading Rules*
- Sections 1.1.1 and 4.1 of the Companion Policy 23-101CP *Trading Rules*
- Section 3.3 b) iii) of OSC Staff Notice 33-748
- Section 3.2 a) of OSC Staff Notice 33-734 *2010 Compliance and Registrant Regulation Branch Annual Report*
- Director's Decision (26 September 2017) *In the Matter of Staff's Recommendation To Impose Terms and Conditions on the Registration of Acker Finley Asset Management Inc.*

d) Oversight of related party service providers (IFM)

Some IFMs have outsourced fund administration functions (for example, fund accounting and transfer agency) of their IFM operations to related parties. In limited instances, we noted that some IFMs performed limited or no oversight of the functions outsourced to related service providers.

NI 31-103 requires IFMs to establish a system of controls and supervision to ensure compliance with securities legislation and to manage their business risks in accordance with prudent business practices. Part 11 of NI 31-103CP, under the heading *General business practices - outsourcing*, states that registered firms are responsible and accountable for all functions that they outsource to a service provider.

IFMs should:

- have a system of controls for monitoring the service provider to meet their regulatory obligations,
- implement and follow the same level of oversight for both related and unrelated service providers,
- in some cases, where an IFM is part of a global conglomerate and using a related party service provider to allow for common compliance resources, take a modified approach to oversee the related party service provider. In these cases, IFMs must at a minimum:
    - maintain a service level agreement with the affiliate that clearly lists each party's roles and responsibilities,
    - implement a formal line of reporting between the affiliate and the registrant,
    - have officers/directors of the affiliated service provider attend and report to committees within the registrant's organization (including but not limited to the Risk Management Committee and Valuation Committee),
    - tailor oversight procedures to the IFM's business and the outsourcing arrangement to meet their regulatory obligations, and
    - compare the fees charged by a related service provider to those charged by third parties to confirm that the selection of the service provider is in the best interests of the investment funds, with referral of the matter to the IRC, if applicable, for consideration.

IFMs should not:

- rely solely on the related service provider and assume that all obligations under securities law are met since the service provider is related.

d) Oversight of related party service providers (cont'd)

Legislative reference and guidance

- Part 11 - *Division 1 Compliance* of **NI 31-103** and related **NI 31-103CP**
- Part V of **OSC Staff Notice 33-743**
- Section 4.4.1 of **OSC Staff Notice 33-742**
- **Registrant Outreach seminar (June 2017)** - *Effective Oversight of Service Providers and Modernization of Investment Fund Product Regulation - Alternative Funds*

e) Inadequate branch audits conducted by registered firms (EMD / SPD)

During our reviews of EMDs and SPDs, we noted several instances where firms did not establish and maintain systems of controls and oversight to effectively supervise and monitor the firm's dealing representatives at their various branch office locations. Specifically, we reviewed the branch audit programs and branch audit testing results conducted by several firms of their branch office locations and noted one or more of the following deficiencies:

- branch audit methodologies, procedures and results were inadequately documented,
- branch audit programs did not adequately cover all areas of operations, business risks and securities legislation at the respective branch office locations,
- branch audit programs did not adequately address the product knowledge of the dealing representatives being examined, and
- there was a lengthy delay between the completion of the branch audit and the issuance of the audit report to the branch manager.

Registrants are required to establish, maintain and apply policies and procedures that establish a system of controls and supervision to ensure compliance with securities legislation and manage the firm's business risks in accordance with prudent business practices. Firms should have an appropriate audit framework and methodology in place to effectively audit branch office locations and address any significant concerns identified. A firm's audit framework should cover all relevant aspects of securities legislation and validate that branch audits are effectively being performed, reviewed and approved.

e) Inadequate branch audits conducted by registered firms (cont'd)

Dealers should:

- thoroughly document the firm's audit methodology including, where applicable, any metrics considered, timing, resource requirements, audit scope, materiality and sampling techniques,
- develop an audit program that is sufficiently detailed and covers areas relevant to each branch office location's business operations, as well as all aspects of securities legislation, including the firm's business risks,
- document all audit procedures performed including the results and any deficiencies identified,
- validate that branch audit results are communicated to dealing representatives and branch managers in a timely manner after the completion of the audit,
- follow-up on branch audits conducted to make certain that deficiencies identified are appropriately remediated in a timely manner (for example, confirm that dealing representatives with identified product knowledge deficiencies have received subsequent training, etc.), and
- confirm that branch audits are effectively being performed, reviewed and approved.

Dealers should not:

- use a template of a branch audit program provided by another firm or a consultant without reviewing and tailoring the template to the firm's operations and securities law obligations, and
- conduct branch audits using a "tick the box" approach without documenting in detail the results and findings of the audit procedures performed.

Legislative reference and guidance

- Subsection 32(2) of the Act
- Part 11 - *Division 1 Compliance* of NI 31-103 and related NI 31-103CP

f) Expenses charged to investment funds (IFM)

CRR staff performed a desk review on fees and expenses charged to investment funds by IFMs. The expense desk review focused on assessing an IFM's process to disclose and charge fees and expenses to the investment funds it manages. The most common deficiency we noted involved IFMs charging investment funds with various expenses related to the portfolio management function over and above a management fee charged to the funds, which already included an advisory fee paid to the PM. Examples of these expenses included costs incurred for research and analysis, portfolio management software and due diligence fees. We consider these examples to be expenses of executing the portfolio management function of an investment fund. As such, we expect that the portion of the management fee paid to the PM as an advisory fee will cover all the expenses of executing the portfolio management function and that additional portfolio management expenses should not be separately charged to the investment funds.

f) Expenses charged to investment funds (cont'd)

Other noted deficiencies were as follows:

- the use of an inappropriate methodology for allocating expenses between investment funds,
- inadequate disclosure of fees and expenses in offering documents,
- other inappropriate expenses charged to investment funds such as:
  - investment level penalties,
  - upfront fees charged upon the creation of the funds to subsidize future expenses of the funds,
  - a reimbursement to the IFM to compensate the IFM for subsidizing certain expenses of an investment fund in prior periods,
- overcharging performance fees, and
- no documentation to support expenses charged to the investment fund.

IFMs should:

- review the nature and type of expenses charged to each investment fund managed to confirm that expenses charged are attributable to the daily operation of the investment fund,
- use a fair allocation methodology to allocate expenses that includes cost drivers directly related to the type of expense being allocated,
- review the costs relating to termination, restructuring and mergers to assess if these costs are being charged to the investment funds and if so, if it is appropriate,
- have written policies and procedures in place that relate to expenses and fees to ensure consistency with the IFM's practice,
- communicate with the IRC on fees, expenses and costs arising from the termination, restructuring or merger of investment funds,
- provide adequate and accurate disclosure about fees and expenses, and
- review the performance fee charged to each investment fund managed to confirm that the calculation is accurate and any changes to the high watermark are reasonable and appropriately disclosed.

Legislative reference and guidance

- Section 19 of the Act
- Section 116 of the Act
- Part 11 - *Division 1 Compliance* of NI 31-103 and related NI 31-103CP
- OSC Staff Notice 33-743

2.2.3 Financial condition & custody

Solvency is considered one of three key pillars in assessing a firm's fitness for initial and ongoing registration. Registered firms must maintain solvency by adequately meeting their capital and insurance requirements at all times. In addition, to mitigate investor assets from the risk of misappropriation or insolvency, firms must use a qualified custodian to hold client and/or investment fund cash or securities.

a) Financial condition (IFM / PM / EMD / SPD)

Some registered firms are not adequately meeting their excess working capital and insurance coverage obligations. These are common deficiencies identified and previously reported in prior CRR annual reports. Registered firms must meet their capital and insurance requirements to maintain their registration in good standing.

Legislative reference and guidance

- Part 12 - *Division 1 Working Capital* of NI 31-103 and related NI 31-103CP
- Part 12 - *Division 2 Insurance* of NI 31-103 and related NI 31-103CP
- OSC Staff Notice 33-742 - Section 4.1.2 - *Inaccurate calculations of excess working capital*
- OSC Staff Notice 33-745 - *Annual Summary Report for Dealers, Advisers and Investment Fund Managers* (OSC Staff Notice 33-745) - Section 4.1(c)(iii) - *Inadequate insurance coverage*
- OSC Staff Notice 33-748 - Section 2.1(b) - *Review of insurance requirements*

b) Fund financial statements (IFM)

IFMs prepared financial statements for investment funds they managed in accordance with Accounting Standards for Private Enterprises (**ASPE**), but did not maintain documentation to support the appropriateness of these accounting standards.

In cases where NI 81-106 does not apply to a fund, IFMs are:

- required to refer to the preface to the CPA Canada Handbook – Accounting (**Handbook**) to determine which accounting standards are permitted for each fund that they manage, and
- only permitted to use ASPE for a fund's financial statements if the fund does not meet the definition of a publicly accountable enterprise (**PAE**).

IFMs should:

- if securities regulation does not specify a required accounting framework:
  - assess whether a fund meets the definition of a PAE as noted in the Handbook,
  - prepare a fund's financial statements in accordance with International Financial Reporting Standards (**IFRS**) if it meets the definition of a PAE,
  - prepare a fund's financial statements in accordance with IFRS, or ASPE, if a fund does not meet the PAE definition, and
  - maintain documentation to support the appropriateness of the accounting framework used if a fund's financial statements are not prepared in accordance with IFRS.

b) Fund financial statements (cont'd)

IFMs should not:

- prepare a fund's financial statements using a basis of accounting that is contrary to what is prescribed by securities regulation, and
- where securities regulation does not prescribe an accounting framework, fail to:
  - assess whether a fund meets the PAE definition, and
  - maintain documentation to support the basis of that determination.

Legislative reference and guidance

- Preface to the CPA Canada Handbook - Accounting
- NI 81-106 *Investment Fund Continuous Disclosure* (NI 81-106)
- Section 11.5 - *General requirements for records* of NI 31-103

c) Holding client assets (IFM)

We continued to note instances where IFMs were not complying with the requirement to hold investment fund assets separately and apart from firm assets, despite previously issued guidance in prior versions of the Annual Report. We remind registered firms that deficiencies of this nature raise serious violations of Ontario securities law and may result in regulatory action. Section 14.6 of NI 31-103 requires IFMs to hold client assets:

- separate and apart from the registrant's own property,
- in trust for the registrant's clients, and
- in the case of cash, held in a designated trust account at a Canadian financial institution, a Schedule III bank, or an IIROC member firm.

Amendments to the custody requirements came into force on June 4, 2018. We advise each IFM to review these amendments to assess applicability to the operation of their investment funds and apply the changes accordingly. Please refer to section 3.4 for additional details on these changes.

Legislative reference and guidance

- Part 14 - *Division 3 Client assets and investment fund assets* of NI 31-103 and NI 31-103CP
- Section 3.4 (a)(ii) of OSC Staff Notice 33-748

d) Safeguarding client assets (IFM)

We noted instances where IFMs did not have adequate controls in place through a segregation of duties to safeguard client assets. In particular, certain IFMs performing the trust accounting function in-house, lacked proper segregation of duties and an independent review and approval process, which as a result, exposed client assets to increased risk. We identified activities where:

- the trust accounting function was executed by a single employee who was responsible for:
  - reconciling the trust accounts, and
  - disbursing monies from the trust accounts,
- the trust account was not reviewed or approved by someone other than the employee responsible for reconciling the account, and
- a single employee was able to issue cheques and wire disbursements from the trust account without any secondary authorization or review.

We remind registered firms that deficiencies of this nature raise serious violations of Ontario securities law and may result in regulatory action.

IFMs should:

- establish, maintain and apply policies and procedures that establish a system of controls and supervision to ensure compliance with securities legislation and manage their business risks in accordance with prudent business practices. These include:
  - ensuring that reconciliations, and the corresponding activity within trust accounts, are reviewed, signed and dated by an individual independent of the preparer, and
  - requiring that disbursements from the trust accounts are authorized by multiple approved persons, and
- implement adequate compensating controls to address the increased risks present when there is a lack of segregation of duties.

IFMs should not:

- accept client assets without having clearly documented policies and procedures regarding the handling of client assets.

Legislative reference and guidance

- Part 11 - *Division 1 Compliance* of NI 31-103 and related NI 31-103CP
- Part 14 - *Division 3 Client assets and investment fund assets* of NI 31-103 and NI 31-103CP
- Part 11 - *Commingling of Cash* of National Instrument 81-102 *Investment Funds* (NI 81-102)

2.2.4 Know your client (KYC), Know your product (KYP) & suitability

Securities laws impose a duty on registrants to deal fairly, honestly and in good faith with clients. Part 13 *Dealing with clients - individuals and firms* of NI 31-103 sets out the principal KYC, KYP, and suitability obligations for registrants. These obligations work together and are an extension of the duty to deal fairly. More specifically, the suitability obligation requires a registrant to know the client, know the product that is the subject of the proposed recommendation or client order, and to form an opinion as to whether the product is suitable in light of the client's investment needs and objectives.

The purpose of the KYC obligation is to establish the client's identity, establish the suitability of the proposed transaction and, if applicable, to determine whether the prospectus exemption relied upon is available in the circumstances. Without adequate and timely KYC information, a firm cannot meet its suitability obligation to clients. Section 13.3 *Suitability* of NI 31-103 requires a registrant to take reasonable steps to ensure that before it makes a recommendation to, or accepts an instruction from a client to buy or sell a security, or makes a purchase or sale of a security for a client's managed account, the registrant must determine if the purchase or sale is suitable for the client. We remind firms of the importance of maintaining adequate documentation to demonstrate compliance with their suitability obligation.

a) Inadequate KYC and suitability assessment for senior investors (PM / EMD / SPD)

i) Inadequate collection and documentation of client KYC information

From our senior suitability sweep, approximately 57% of the firms reviewed did not collect and document sufficient KYC information, including information relating to risk tolerance, time horizon and investment knowledge, for some of their clients. This is one of the common deficiencies that we continue to find in our reviews of firms. While most of the firms and their representatives were able to demonstrate that these were documentation issues rather than a general lack of understanding of their senior clients' investment needs and objectives, we remind firms to maintain adequate and up-to-date KYC information to support their compliance with the KYC and suitability obligations.

In addition, we generally found that firms adopted the same KYC process as was used for other clients when servicing senior clients. For instance, the frequency of the KYC update and the type of KYC information collected were the same regardless of the client's age. However, some firms were more proactive in discussing the potential use or existence of a POA and obtaining the names and contact information of family members or other third party representatives (for example, lawyers or accountants) during the onboarding process, even though their clients did not appear to have any mental capacity or health related issues.

a) Inadequate KYC and suitability assessment for senior investors (cont'd)

We also observed that certain firms established a policy whereby they increased the frequency of contacting their senior clients (where possible, through face-to-face meetings) once they suspected any issues relating to diminished capacity or financial abuse. These firms also documented the outcome of their discussions after each meeting to further support the selected investment strategies and suitability determination. These firms believed that frequent interaction with senior clients assisted them in identifying early signs of diminished capacity or suspected financial abuse so that appropriate protective measures could be taken in a timely manner.

ii) Inadequate documentation to support suitability determination

Further, from our senior suitability sweep, we also noted approximately 23% of the firms reviewed did not maintain adequate documentation to support suitability determinations. Although in most cases the firms were able to provide staff with additional information to support their suitability assessments, such information was not documented on file at the time of our reviews. In one review, we noted some of the firms' senior clients invested more than 10% of their net financial assets in a related issuer product which raised concerns as to whether the investments were suitable given the level of investment concentration in that product. There was no documentation to support why the firm considered these trades to be suitable. It was also unclear whether the firm had explained to their senior clients the risk of holding such a concentrated position in their portfolios.

With respect to the review procedures for senior clients, they were generally the same as for other clients; we did not observe any different practices in terms of supervision and review procedures for senior or vulnerable clients when compared to a firm's other clients. We expect firms to heighten their reviews of senior and vulnerable client accounts, particularly when they have identified signs of issues such as diminished capacity and financial abuse, to make sure that their client's portfolio holdings or trades remain aligned with their investment needs and objectives.

PMs, EMDs and SPDs should:

When communicating with seniors and gathering up-to-date KYC information:

- obtain and collect additional KYC information such as future plans, health conditions, liquidity needs, sources of income, risk tolerance (financial capacity and willingness to accept risk) and time horizon including a breakdown of their expenses such as health care, nursing home etc. and consider the potential increases of such costs over time when developing the investment plan,
- explain whether a client's investments are generating sufficient income to meet their retirement needs or maintain their current lifestyle,
- be proactive and engage with clients to prepare for future life event changes which may affect their ability to make investment decisions,
- budget more time for meeting with senior clients,
- assist clients in evaluating the use of different tools (for example, the use of a POA or trusted contact person (**TCP**)) to address issues in the event of a loss of capacity,

a) Inadequate KYC and suitability assessment for senior investors (cont'd)

PMs, EMDs and SPDs should (cont'd):

- increase the frequency of contact with senior and vulnerable clients to assist with the identification of early signs of diminished capacity or financial abuse,
- provide a list of red flags to staff to assist them in identifying potential mental capacity and financial abuse issues when interacting with older investors,
- maintain more frequent contact if the firm identifies signs of diminished capacity or financial abuse and maintain documentation of discussions with clients and/or family members. Keep the CCO apprised of any new developments,
- establish a process to confirm and check the validity of an existing POA and how to make sure that the POA on file remains current,
- verify any trade or withdrawal of funds request received from the POA holder, where appropriate, with the clients,
- use plain language and avoid financial jargon when interacting with senior clients. Encourage them to ask questions during meetings, and
- provide a written summary of any discussions including any decisions that were agreed upon with the clients.

When preparing documentation to support suitability determinations:

- flag accounts of senior and vulnerable clients with potential suitability issues such as concentrated positions (for example, illiquid securities, high risk products or complex products) and patterns of unusual trading activity for further review and suitability assessments,
- enhance the oversight review of a client account when there are signs of mental capacity issues or financial abuse,
- document in the client file any suitability assessments and discussions with the TCP on how the account was managed in light of the client's issues,
- maintain adequate documentation to support the review process and suitability determination,
- confirm KYC is up-to-date, and
- make sure that any issues, such as diminished capacity, have been escalated and addressed appropriately with documentation to support all actions taken.

When performing portfolio management activities:

- monitor concentration issues in client portfolios, and
- monitor liquidity requirements of the account to validate the portfolio generates sufficient income for the senior investors.

a) Inadequate KYC and suitability assessment for senior investors (cont'd)

PMs, EMDs and SPDs should not:

- ignore the red flags of diminished capacity or financial abuse and continue to service their clients in the same manner,
- avoid discussion with clients regarding topics such as diminished capacity and financial abuse for fear of offending the clients, and
- invest senior clients in high risk and/or illiquid products if the clients rely on their investment principal, or income generated from it, to fund their retirement expenses.

Legislative reference and guidance

- Sections 13.2 *Know your client* and 13.3 *Suitability* of NI 31-103 and related NI 31-103CP
- CSA Staff Notice 31-336
- Section 3.1(b)(i) of OSC Staff Notice 33-747 *Annual Summary Report for Dealers, Advisers and Investment Fund Managers* (2016)
- Section 4.3(a)(iii) of OSC Staff Notice 33-746 *Annual Summary Report for Dealers, Advisers and Investment Fund Managers* (2015)

b) Offering memorandum exemption – delivering offering documents (EMD)

The person relying on a prospectus exemption is responsible for determining whether the terms and conditions of the prospectus exemption are met at the time of the trade. For an issuer to rely on the offering memorandum exemption (the **OM exemption**), among other things, a dealer must have delivered to the investor (where the issuer has not) an offering memorandum (**OM**) in the prescribed form at the same time or before the purchaser signs the agreement to purchase the security.

There is no prescribed method for the delivery of an OM, however, a dealer must be able to demonstrate that an OM has been delivered.

We have identified some concerns with electronic delivery of an OM. Some dealers are making an electronic version of an OM available on their websites or online platforms, but are not providing the recipients with separate notice of its availability. Other dealers are delivering an OM in electronic format (for example, as a compact disk), without taking reasonable steps to ensure that the electronic access to the OM, in this type of format, is not burdensome or overly complicated for recipients. Further, certain dealers are not maintaining any documentation of how and when an OM was delivered to the investor.

NP 11-201 sets out guidance for dealers and other industry participants who want to use electronic delivery to fulfill delivery requirements in securities legislation. When providing documents to investors through electronic delivery, it is important that investors are made aware of the electronic document, are able to open the electronic document and are provided access to the electronic document at any point in time.

b) Offering memorandum exemption – delivering offering documents (cont'd)

EMDs should:

- implement appropriate policies and procedures to provide reasonable assurance of compliance with the requirements for delivery of an OM,
- document the reasonable steps taken to deliver the OM to an investor and when it was delivered, and
- provide training to dealing representatives on the requirements to deliver an OM and the dealer's policies and procedures surrounding the process.

EMDs should not:

- process a transaction in reliance on the OM exemption when the investor has not received an OM,
- rely solely on the posting of an OM on a website or online platform, etc., as delivery, and
- allow dealing representatives to determine themselves how and when an OM will be delivered to an investor.

Legislative reference and guidance

- Paragraph 2.9(2.1)(c) of **NI 45-106**
- Section 1.9 of **NI 45-106CP**
- **National Policy 11-201** *Electronic Delivery of Documents*

2.2.5 Conflicts of interest & referral arrangements

A registered firm is responsible for having a compliance system that promotes compliance by the firm and its individuals with securities law, including when individuals of the firm encounter conflict of interest situations during their daily operational activities. A registered firm is also responsible for meeting the requirements applicable to referral arrangements prior to entering into any such arrangements.

On June 21, 2018 the CSA published for comment detailed proposed amendments (**Client Focused Reforms**) to certain obligations of registered firms and individuals that would require registrants to, among other things, address conflicts of interest in the best interest of the client. In addition, the Client Focused Reforms propose to amend the obligations of registered firms that enter into referral arrangements. We remind registrants that the proposed rules and guidance recommend significant enhancements to a registrant's obligations when dealing with conflicts of interest and referral arrangements. As such, in addition to reviewing the following guidance, we encourage registrants to review the Client Focused Reforms which are accessible using the following link:

https://www.osc.gov.on.ca/documents/en/Securities-Category3/rule_20180621_31-103_client-focused-reforms.pdf

a) Assessing & addressing conflicts of interest (IFM / PM / EMD / SPD)

Registered firms are responsible for identifying and appropriately responding to any conflicts of interest under Part 13 - *Dealing with clients - individuals and firms* of NI 31-103. Conflicts of interest that arise for registered firms when dealing with their clients include (but are not limited to):

- *competing firm and client interests* – where the interests of the registered firm are not aligned with the interests of its clients, and
- *competing client interests* – where the interests of a client of the registered firm are not aligned with the interests of another client of the registered firm.

Registered firms must:

- have written policies and procedures to address conflicts of interest,
- have a process in place to identify existing conflicts of interest and new conflicts as they arise,
- adequately assess and document the level of risk that the conflicts of interest raise,
- avoid the situation giving rise to a conflict of interest if the risk of harming a client or potential harm to the integrity of the markets is too high,
- document the steps taken to manage a conflict of interest,
- provide disclosure to clients, if appropriate, that:
  - clearly describes, in plain language, the situation giving rise to the conflict,
  - explicitly identifies the situation as a conflict of interest, and
  - explains how the conflict of interest could affect the service the client is being offered.
- provide registered individuals and other relevant staff adequate training so they are aware, and understand the nature of, any material conflicts of interest inherent in the firm's business model and the importance of avoiding, managing and/or disclosing them.

a) Inadequate assessment & addressing conflicts of interest (cont'd)

Registered firms must not:

- assume that disclosure alone, which identifies and explains a conflict of interest, is sufficient to respond to it,
- give partial disclosure about a conflict of interest that could mislead clients,
- present conflicts of interest disclosure in an obscure or confusing manner, such as in lengthy and complex documents, and
- ask a client to waive receiving conflicts of interest disclosure.

Legislative reference and guidance

- Part 13 - Division 2 *Conflicts of Interest* of NI 31-103 and related NI 31-103CP
- OSC Staff Notice 33-745 - Section 4.1(f)
- CSA Staff Notice 31-343 *Conflicts of interest in distributing securities of related or connected issuers*

b) Ineffective use of Independent Review Committee (IFM)

A key finding from our ongoing compliance reviews of IFMs relates to conflicts of interest. We noted several scenarios where IFMs were not adequately meeting their conflict of interest obligations in executing their responsibilities in relation to the daily operations of the investment funds they manage. In particular, this section summarizes significant deficiencies raised regarding an IFM's use of an IRC, for reporting issuer investment funds.

The requirement to establish an IRC belongs to the IFM. Once the IRC is established, both the IFM and the IRC have obligations to comply with securities law requirements as set out in NI 81-107.

We noted instances where IFMs did not meet their obligations under NI 81-107. Specifically, some IFMs did not have, or did not adhere to, written policies and procedures in place in relation to the IRC, including but not limited to the following:

- not identifying and referring conflict of interest matters to the IRC for review, recommendation or approval,
- not obtaining standing instructions where conflict of interest matters were identified in the normal course of operations,
- not submitting sufficient information to assist the IRC in its determination to issue or approve standing instructions in relation to conflict of interest matters, and
- not submitting a written report to the IRC describing each instance that the IFM acted in reliance on a standing instruction.

b) Ineffective use of Independent Review Committee (cont'd)

IFMs should:

- have written policies and procedures in place regarding the IRC,
- provide, for any conflict of interest matter identified by the IFM and referred to the IRC, information sufficient to enable the IRC to adequately assess the conflict of interest matter and to determine whether standing instructions should be issued, and
- not engage in a conflict of interest matter before the IRC's assessment of the matter has been completed and communicated.

IRCs should:

- have a written charter which specifies its mandate, responsibilities, functions, and the policies and procedures it will follow when executing its functions,
- meet, at least annually, to comply with its annual reporting obligations,
- review and assess, at least annually:
  - the adequacy and effectiveness of the IFM's written policies and procedures,
  - any standing instructions it has provided to the IFM, and
  - both the IFM's and the funds' compliance with any conditions imposed by the IRC relating to previous recommendations or approvals provided to the IFM, and
- engage in 'reasonable inquiry' when an IFM refers a conflict of interest matter to the IRC for its recommendation or approval, as appropriate.

Legislative reference and guidance

- National Instrument 81-107 *Independent Review Committee for Investment Funds* (NI 81-107)
- Companion Policy 81-107CP *Independent Review Committee for Investment Funds* (NI 81-107CP)
- OSC Staff Notice 81-713 *Focused Disclosure Review*
- CSA Staff Notice 81-317 *Frequently Asked Questions on National Instrument 81-107 Independent Review Committee for Investment Funds*

c) Sales practices (IFM)

We continued to work closely with the Enforcement Branch to reach Commission approved settlement agreements related to our focused compliance reviews of sales practices relating to section 5.2 of NI 81-105 that governs the organization and presentation of mutual fund sponsored conferences. The compliance reviews, which began in December 2015, included a sample of 20 IFMs and focused on mutual fund sponsored conferences organized and presented between 2013 and 2015. In total, we reviewed 63 mutual fund sponsored conferences organized by 13 IFMs that engaged in this type of sales practice under Part 5 of NI 81-105.

The purpose of the focused compliance reviews was to:

- determine if there had been improvement in sales practice compliance resulting from the publication of OSC Staff Notice 33-743,
- review and assess an IFM's policies, procedures and practices relating to sales practices and, specifically, to the organization and presentation of mutual fund sponsored conferences,
- determine and assess involvement by an IFM's compliance staff in the organization and execution of mutual fund sponsored conferences, and
- assess and identify areas where additional guidance to industry participants may be needed.

One or more of the following significant deficiencies were noted in the reviews of registered firms referred to the Enforcement Branch:

- the process followed to select representatives of participating dealers (representatives) – IFMs were targeting their 'top producers' and directing wholesale staff to invite these representatives to mutual fund sponsored conferences,
- the payment of prohibited costs – payment of travel, accommodation and personal incidental expenses of representatives attending the conferences,
- the reasonableness of the conference costs – conference costs and in particular costs associated with meals, entertainment and the provision of non-monetary benefits were excessive, extravagant and not in keeping with the spirit of the NI 81-105.

As a result of certain findings from these compliance reviews, the Enforcement Branch expanded their investigations of sales practices to include business promotion generally between IFMs and participating dealers and their representatives.

We encourage IFMs to assess and take appropriate steps to improve their sales practices and related policies and procedures considering the guidance summarized here and in the settlement agreements. OSC staff will continue to monitor and test registrant compliance with all parts of NI 81-105 through various compliance initiatives.

Part 5 of NI 81-105

Part 5 of NI 81-105 regulates the sales practices of industry participants in connection with the distribution of publicly offered securities of mutual funds to safeguard the interests of investors. The companion policy to NI 81-105 (**NI 81-105CP**) states that NI 81-105 was adopted in order to discourage sales practices and compensation arrangements that could be perceived as inducing dealers and their representatives to sell mutual fund securities on the basis of incentives they were receiving rather than on the basis of what was suitable for and in the best interests of their clients.

c) Sales practices (cont'd)

The purpose of NI 81-105 is to provide a minimum standard of conduct to ensure that investor interests remain uppermost in the actions of mutual fund industry participants when they are distributing mutual fund securities and that conflicts of interest arising from sales practices and compensation arrangements are minimized. Specific provisions under Part 5 of NI 81-105 must be considered in the context of this guiding principle.

Non-compliant sales practices

We previously issued guidance on sales practices in OSC Staff Notice 33-743. We have interacted with many IFMs through our various compliance initiatives that demonstrated their understanding of this previously issued guidance and that have implemented sales practices policies and procedures that comply with Part 5 of NI 81-105 and its guiding principle. However, we continue to see similar non-compliant sales practice issues with some IFMs.

We strongly encourage IFMs to use the information from the three recent sales practices settlement agreements dated March 31, 2017, April 4, 2018 and April 19, 2018 respectively, OSC Staff Notice 33-743 and the December 2016 Investment Funds Practitioner, to enhance their systems of compliance, internal controls and supervision in relation to sales practices. Many aspects of securities law that an IFM must comply with are not prescriptive but rather require the exercise of judgement. Compliance with NI 81-105 is not different in this respect. As such, it is the responsibility of the IFM to exercise judgement when interpreting and implementing securities law through the creation and application of an adequate compliance system.

A. IFM provision of non-monetary benefits

Non-monetary benefits are provided by IFMs to participating dealers and representatives through promotional items and activities. To avoid providing non-monetary benefits that could pose a risk of non-compliance with Part 5 of NI 81-105, IFMs must consider a number of factors. Please refer to the flowchart included at the end of this section entitled "Example framework to assess compliance of the provision of a non-monetary benefit with section 5.6 of NI 81-105". This framework is an example of a process that may be used by an IFM to assist in assessing compliance of the provision of a non-monetary benefit with NI 81-105.

i) Promotional items

The types of promotional items of minimal value contemplated under section 5.6 of NI 81-105 include examples of reminder advertising as outlined in section 7.6 of NI 81-105CP such as pens, calendars, t-shirts, hats, coffee mugs, paperweights and golf balls. Furthermore, Staff's view is that in order for an item to be considered promotional in nature, the IFM's logo must be prominently displayed directly on the item itself.

We have noted through our compliance initiatives that IFMs have expanded the types of items that they consider to be a promotional item of minimal value. We have seen the provision of items that are clearly not compliant with the spirit of NI 81-105. The items provided by IFMs as promotional items that are referenced in the settlement agreements referred to above are examples of items that are not promotional in nature, not of minimal value, excessive and therefore not in compliance with Part 5 of NI 81-105.

c) Sales practices (cont'd)

The following table lists some of the promotional items provided by IFMs to representatives that Staff noted during compliance initiatives to be compliant and also items provided as promotional items by IFMs that were non-compliant for which deficiencies were raised and references included in the settlement agreements.

Compliant: promotional items that are of minimal value, prominently display an IFM's logo, are not extensive and/or frequently provided.

- luggage tags
- embroidered basic bags (i.e. back packs)
- water bottles
- insulated coffee mugs
- notebooks and notepads
- USB keys
- umbrellas
- passport holders
- business card holders
- mobile telephone cases

Non-compliant: items that are not of minimal value, do not prominently display the IFMs logo, are extensive and/or frequently provided.

- electronic items - BOSE soundlink speakers or wireless music systems, activity trackers, Sony digital cameras
- computers or tablets - iPad minis, Samsung Galaxy Tablets
- alcohol - Dom Pérignon champagne, expensive bottles of wine
- designer brand jewellery - Tiffany & Co. earrings
- custom made clothing - men's dress shirt, sports jacket
- household appliances and gadgets - Nespresso espresso machine
- luxury sporting goods - expensive golf putters and golf shoes, Nike golf bags, BUSHNELL Neo-ghost golf GPS
- gifts for life events - baby gifts, wedding, anniversary, retirement, funeral, etc.

ii) Business promotion activities

An IFM is permitted to engage in reasonable business promotion activities under Part 5 of NI 81-105. Section 7.6 of NI 81-105CP provides examples of reasonable business promotion activities including occasional meals or drinks, tickets to sporting events, the ability to participate in events such as golf tournaments and other comparable entertainment. The purpose of these activities is to provide an opportunity outside of a business environment to discuss and promote an IFM's funds.

For an activity to be considered promotional in nature, a representative of the IFM must attend the activity, for the entire duration of the event, along with the representative(s) of the participating dealer to whom the IFM is providing the activity. There should also be a reasonable number of IFM representatives attending the activity in relation to the number of dealing representatives that attend.

c) Sales practices (cont'd)

We have noted through our compliance initiatives, that IFMs have expanded the type of activities that they consider to be a "reasonable promotional activity". Staff's view is that promotional activities must not be extravagant or excessive or be an activity that would be out of reach, based either on cost or access, for an average person.

The following table summarizes promotional activities provided by IFMs to representatives that Staff noted during compliance initiatives to be compliant and also activities provided as promotional activities by IFMs that were non-compliant for which deficiencies were raised and references included in the settlement agreements.

 **Compliant:** promotional activities which a representative of the IFM attended, that were not extensive or frequent.	 **Non-compliant:** activities for which a representative of the IFM did not attend and/or were extensive and frequent.
rounds of golf at golf courses with reasonable green fees	the opportunity to play at a golf course with expensive green fees or golf followed by a reception including cocktails, dinner and non-promotional gifts not of minimal value that in aggregate made the cost of the day excessive – e.g., Eastern township golf events, golf green fees in excess of $600 per representative
tickets to sporting events at a reasonable cost per ticket (e.g. - regular season sporting tickets for MLB, NBA, NHL, etc. and no floor seats, no box seats, etc.)	major league sporting event play-off tickets or tickets to sporting events that include expensive catering and bar service or meals and drinks and non-promotional gifts (i.e. team jerseys, hats, and other non-promotional sport paraphernalia) – e.g., Vancouver Canucks and Montreal Canadiens hockey games with a total benefit of more than $700 per representative
breakfast, lunch or dinners at costs that were not excessive and not held at extravagant venues	after business hour activities at conferences held at extravagant venues, including excessive cocktails, dinner receptions and entertainment – e.g., approximately $1,500 per representative for dinner and activities held at a luxury resort, approximately $700 per representative for dinner and activities held at the Bacara Resort, approximately $500 per representative for dinners at various exclusive venues
tickets to city attractions at mutual fund sponsored conferences (e.g. - Empire State building, the city zoo, etc.)	tickets to popular celebrity concerts and/or sporting events for a representative and their family members at excessive costs - e.g., Madonna concert, Tears for Fears concert
keynote speakers that do not have celebrity status at conferences or seminars	the opportunity to listen and meet celebrity keynote speakers such as sports athletes – e.g., Magic Johnson as the keynote speaker at a mutual fund sponsored conference

c) Sales practices (cont'd)

iii) Value of promotional items and business promotion activities attributed to participating dealers and representatives

When assessing the value of the promotional item/activity provided to a participating dealer and/or representative, an IFM must consider the retail value of items and activities. This is the value it would cost an individual that does not have special access to purchase the item or pay for the activity on their own. If an IFM is able to obtain tickets to an event or an item at a wholesale price or a deep discount, the non-discounted value is the cost of the non-monetary benefit that should be attributed per ticket or item, per attending representative for purposes of assessing compliance with NI 81-105.

- For example, if an IFM purchases a season ticket package to a sporting event, tickets provided to representatives must be allocated based on the retail value of the ticket and not the weighted average cost based on the value of the entire package.

It is not enough for an IFM to set dollar limits and assume compliance with Part 5 of NI 81-105 as long as spending remains within the set internal parameters. An IFM must also apply a qualitative analysis when assessing a non-monetary benefit to confirm compliance with the spirit of NI 81-105.

- For example, the provision of tickets to a national or major league play-off sporting event is considered a type of event that would not normally be available to the average person. The cost of the tickets, which can vary from one Canadian city to another, is irrelevant. The provision of the non-monetary benefit is the same regardless of where the sporting activity occurs.

Some IFMs are also combining individual internal limits for non-monetary benefits that can be provided under different categories, such as food, promotional activities and promotional items to provide a combined event to representatives. In order to make the event comply with Part 5 of NI 81-105, these IFMs are treating each component of the event separately when assessing reasonableness of the event. In some instances, the combination of the limits has resulted in the provision of excessive and extravagant non-monetary benefits. Promotional activities that combine limits for different sales practice components should not only be assessed individually against internal limits but also considered collectively when assessing compliance with Part 5 of NI 81-105.

Staff noted that some IFMs do not have adequate internal controls to track all non-monetary benefits provided to representatives and participating dealers. Any non-monetary benefits that IFMs provide must be categorized into one of the sections of Part 5 of NI 81-105. IFMs must have policies and procedures that include a process to confirm that all non-monetary benefits are tracked and allocated to participating dealers and/or representatives as permitted by Part 5 of NI 81-105.

- For example, non-monetary benefits provided to guests of representatives attending a mutual fund sponsored conference under section 5.2 of NI 81-105 represent non-monetary benefits for the representative. The cost of these non-monetary benefits should be attributed to the attending representative.

c) Sales practices (cont'd)

B. Prohibited solicitation by participating dealers and representatives

We remind participating dealers and their representatives that section 2.2 of NI 81-105 restricts a participating dealer and its representatives from soliciting or accepting from an IFM, in connection with the distribution of securities of a mutual fund, among other requirements, the provision of a non-monetary benefit. The only exemptions available to section 2.2 of NI 81-105 are:

- a participating dealer can solicit and accept a non-monetary benefit as permitted by Part 5 of NI 81-105, and
- a representative of a participating dealer can only accept a non-monetary benefit as permitted by Part 5 of NI 81-105. No solicitation by representatives is permitted.

We understand that, in some cases, the provision of prohibited spending and non-monetary benefits is being driven by:

- participating dealers soliciting IFMs to pay for expenses of their dealer events that do not fall within allowable sections of Part 5 of NI 81-105, and
- representatives soliciting IFMs to provide non-monetary benefits. Examples include:
    - tickets for sporting events and concerts,
    - gaming consoles,
    - golf equipment such as golf putters, and
    - cases of alcohol solicited by providing an IFM representative with an invitation to holiday parties.

If a non-monetary benefit is solicited by a representative of a participating dealer, it is deemed to be non-compliant. If a non-monetary benefit solicited or accepted by a participating dealer does not fall within the allowable categories of Part 5 of NI 81-105, it is non-compliant, as discussed in further detail below.

C. Prohibited categories of spending

As a result of the prohibition included in section 2.2 of NI 81-105, participating dealers are prohibited from soliciting funding and non-monetary benefits from IFMs, and IFMs are prohibited from providing funding and non-monetary benefits to participating dealers and their representatives, for categories not included in Part 5 of NI 81-105.

- For example, providing funding for non-educational dealer events and then tracking the spending per representative of a participating dealer under section 5.6 of NI 81-105 is not a compliant practice. Monetary support for participating dealer events can only fall within section 5.5 of NI 81-105 and these types of events do not qualify under this section. In addition, this is not the type of spending on promotional items and activities originally contemplated when NI 81-105 and section 5.6 was adopted, and is not within the spirit of the rule.

c) Sales practices (cont'd)

Example framework to assess compliance of the provision of a non-monetary benefit with section 5.6 of NI 81-105

IFMs may choose to use this example framework as a tool to help assess compliance of the provision of a non-monetary benefit.

This example framework can also be used to assess compliance of the provision of a non-monetary benefit outside of section 5.6 of NI 81-105. For example, if an IFM is providing a non-monetary benefit through an item or activity during a conference or seminar organized under section 5.2 of NI 81-105, the framework can be used to assess compliance with the requirement to ensure the reasonableness of the cost of the item or activity being provided. Section 7.3 of NI 81-105CP states that the term "reasonable" costs pertaining to paragraph 5.2(e) of NI 81-105 would not include gifts or entertainment provided to attendees other than as permitted by section 5.6 of NI 81-105.

Staff's view is that any exceptions to an IFM's internal policies and procedures on sales practices would constitute non-compliance with NI 81-105 and are therefore, not permissible. Unintended or unforeseen exceptions should be documented and escalated for resolution.

Example framework to assess compliance of the provision of a non-monetary benefit with section 5.6 of NI 81-105		
Step	**Promotional item**	**Business promotion activity**
	IFM decides to provide a non-monetary benefit through a promotional item.	IFM decides to provide a non-monetary benefit through a business promotion activity.
#1	Was the item solicited by a representative?	Was the activity solicited by a representative?
	No – proceed to step #2	
	Yes – the IFM cannot provide the item/activity	
#2	Is the item promotional - does it prominently display the IFM's logo?	Is the activity promotional - will a representative of the IFM attend the activity as well?
	Yes – proceed to step #3	
	No – the IFM cannot provide the item/activity	

#3	Execute a quantitative analysis: Assess if the cost of the promotional item is of minimal value and if the cost of the promotional activity is reasonable to ensure compliance with the parameters of section 5.6 of NI 81-105 and the IFM's internal policies and procedures.
	Consider the following factors when executing a quantitative analysis:
	• Does the cost fit within the IFM's internally set limits?
	  ◦ limit per item,
	  ◦ limit per activity,
	  ◦ limit per representative/participating dealer per quarter and per annum,
	  ◦ frequency limit,
	  ◦ other limits set by the IFM's internal policies and procedures.
	• Does the item fall within the non-compliant examples included in this report?	

	Is the cost of the item of minimal value?	Is the cost of the activity within the parameters of section 5.6 of NI 81-105?
	Yes – proceed to step #4	
	No – the IFM cannot provide the item/activity	
#4	Execute a qualitative analysis: Assess the nature of the item/activity to determine reasonability within the parameters of Part 5 of NI 81-105 and the IFM's internal policies and procedures. Consider the following factors when executing a qualitative analysis: • Does the item/activity comply with the spirit of the rule? • Would the activity be out of reach for an average person? • Does the item/activity fit within the IFM's internal policies and procedures established to help with a qualitative analysis? • How would an independent third party react to the provision of the non-monetary benefit? Would they consider it to be extravagant? • What would be the reputational impact to the IFM if the non-monetary benefit was made public, for example in a news article? • Does the item/activity fall within the non-compliant examples included in this report?	
	Is the nature of the item reasonable?	Is the nature of the activity reasonable?
	Yes – the IFM can provide the item/activity	
	No – the IFM cannot provide the item/activity	

2.2.6 Client disclosure & reporting

Division 2 of Part 14 *Handling client accounts - firms* of NI 31-103 sets out disclosure requirements for registered firms. Sections 14.2, 14.2.1 and 14.4 explain the content and frequency of disclosure to clients including: relationship disclosure information, pre-trade disclosure of charges and disclosure when the firm has a relationship with a financial institution.

Division 5 of Part 14 *Handling client accounts - firms* of NI 31-103 sets out client reporting requirements for registered firms including, where applicable, the requirement to send account statements and additional statements (collectively, **client statements**), the report on charges and other compensation (**compensation reports**) and the investment performance report (**performance reports**).

a) Relationship disclosure information (IFM / PM / EMD / SPD)

We continue to raise a number of deficiencies related to relationship disclosure information as a result of:

- the document(s) provided to clients not containing all of the required disclosure,
- the document(s) provided to clients containing incorrect or outdated information, or
- in some instances, no document or disclosure being provided.

Legislative reference and guidance

- Part 14 - *Division 2 Disclosure to Clients* of **NI 31-103** and related **NI 31-103CP**
- **CSA Staff Notice 31-334** *CSA Review of Relationship Disclosure Practices*
- Section 5.1.2 - *Inadequate relationship disclosure information* of **OSC Staff Notice 33-738** *2012 OSC Annual Summary Report for Dealers, Advisers and Investment Fund Managers*
- **Registrant Outreach seminar (November 2016)** - *Communicating with clients in a compliant manner* and accompanying slides 28-37

b) Inadequate client statements and reports (PM / EMD / SPD)

During our CRM2 review, we noted that some firms were not delivering the required client statements, compensation reports and performance reports. Examples of these firms include:

- EMDs that hold client assets,
- EMDs that do not hold client assets, but receive trailing commissions related to the client's ownership of the securities they purchased for clients, and
- PMs that believed they had met their statement delivery obligation because their clients' custodian(s) were carrying out these tasks (we remind PMs to refer to CSA Staff Notice 31-347).

b) Inadequate client statements and reports (cont'd)

We also noted the following common deficiencies in the client statements, compensation reports and performance reports reviewed:

Client statements:

- were provided on a consolidated basis, combining all accounts owned by a client or family group

Compensation reports:

- did not include adequate disclosure about the operating and/or transaction charges when clients with multiple accounts (for example, TFSA and RRSP accounts) had designated one account to pay for all the fees incurred
- were consolidated inappropriately (for example, for a family group) or without obtaining written client consent

Performance reports:

- were missing information (for example, the definition of total percentage return and associated notification)
- did not include text, tables and charts to illustrate the contents of the report
- included inadequate disclosures when presenting benchmarks
- were consolidated inappropriately (for example, for a family group) or without obtaining written client consent

Legislative reference and guidance

- Appendix D *Annual Charges and Compensation sample report* of **NI 31-103CP**
- Appendix E *Performance Report sample* of **NI 31-103CP**
- Appendix F *Part 14 Client reporting requirements and sole EMDs* of **NI 31-103CP**
- Sections 14.17, 14.18 and 14.19 of **NI 31-103** and related **NI 31-103CP**
- Questions 36-45 of **CSA Staff Notice 31-345** *Cost Disclosure, Performance Reporting and Client Statements - Frequently Asked Questions and Additional Guidance*
- Section 3.1 b) ii) of **OSC Staff Notice 33-748**
- **CSA Staff Notice 31-347**

2.2.7 Marketing

a) Misleading or inaccurate marketing materials (IFM / PM / EMD / SPD)

Registered firms must validate that all marketing materials are accurate and free of misleading statements or unsubstantiated claims. This is important in order to meet obligations under securities law, including the obligation to deal fairly, honestly and in good faith with clients. Registered firms should establish procedures to conduct an adequate review and obtain approval of all marketing materials prior to dissemination in order to provide both meaningful and accurate marketing materials to existing and prospective clients.

We have identified concerns with the marketing materials provided to prospective clients. Some examples include:

- the use of hypothetical performance data, without first determining whether the use of the hypothetical performance data is fair and not misleading,
- sales presentations that are not fair and balanced as they do not include information on key features such as commissions, fees and risks, thus exaggerating the benefits of the investment or plan, and
- unsubstantiated statements in marketing and promotional materials that are not supported by evidence to verify the claims.

Registered firms should:

- present actual performance returns for clients of the firm where available,
- consider relevant factors to determine whether the use of hypothetical performance data is permitted, fair and not misleading,
- substantiate all claims made in marketing materials, and
- adequately reference information supporting claims so that investors can easily assess the merits of claims made.

Registered firms should not:

- provide sales presentations to prospective clients which understate commissions or fees, and do not adequately communicate the risks associated with an investment.

Legislative reference and guidance

- Subsection 2.1(1) of OSC Rule 31-505 *Conditions of Registration*
- CSA Staff Notice 31-325 *Marketing Practices of Portfolio Managers*

Part 3

KEY POLICY INITIATIVES IMPACTING REGISTRANTS

3.1 Derivatives regulation

CRR staff have been working with the Derivatives Branch to develop a number of rules relating to the regulation of derivatives, including proposed rules that will set out the principal business conduct and registration requirements and exemptions for derivatives dealers and derivatives advisers (collectively, **derivatives firms**), and a rule that prohibits the advertising, offering, selling or otherwise trading of binary options to or with individual investors. In addition, CRR staff continue to work with the Derivatives Branch on the implementation of other rules relating to derivatives, including conducting compliance reviews of derivatives market participants in connection with their compliance with OSC Rule 91-507 *Trade Repositories and Derivatives Data Reporting*.

Derivatives business conduct and registration rules

On April 4, 2017, the CSA published for comment Proposed **National Instrument 93-101 *Derivatives: Business Conduct*** and a related companion policy (collectively, **the Proposed Business Conduct Rule**). The Proposed Business Conduct Rule sets out the principal business conduct obligations and exemptions for derivatives firms and certain of their representatives and will apply to a derivatives firm, regardless of whether the derivatives firm is registered or exempted from the requirement to be registered under Ontario securities law.

Similarly, on April 19, 2018, the CSA published for comment Proposed **National Instrument 93-102 *Derivatives: Registration*** and a related companion policy (collectively, **the Proposed Registration Rule**) for a 150-day comment period. We considered comments received on the April 2017 publication of the Proposed Business Conduct Rule in developing the Proposed Registration Rule.

On June 14, 2018 the CSA published a revised version of the Proposed Business Conduct Rule for a second comment period. The comment period coincides with the comment period for the Proposed Registration Rule. This gives stakeholders the opportunity to consider both of the proposed instruments when making their comments. Comments should be submitted in writing on or before September 17, 2018.

The CSA has developed the Proposed Business Conduct and the Proposed Registration Rule to help protect investors, reduce risk, improve transparency and accountability, and to implement a comprehensive regime for the regulation of persons or companies that are in the business of trading derivatives and in the business of advising on derivatives. Many of the requirements in the Proposed Business Conduct and the Proposed Registration Rule are similar to existing market conduct and registration requirements applicable to registered dealers and advisers under NI 31-103 but have been modified to reflect the different nature of derivatives markets and their participants.

Prohibition on the offer or sale of binary options to individuals

CRR staff have also been working with the Derivatives Branch, Enforcement Branch and the Investor Office in developing a number of strategies to respond to investor complaints over binary options fraud.

These strategies include the development and adoption of a new rule, **Multilateral Instrument 91-102 *Prohibition of Binary Options*** (the **Binary Options Rule**), that prohibits advertising, offering, selling or otherwise trading of binary options to or with individual investors.

The firms and individuals involved in binary options trading platforms are often located overseas. Many of these products and the platforms selling them have been identified as vehicles to commit fraud. We emphasize that no offering of these products, including by a broker, dealer or platform, has been authorized in Canada. All current offerings in Canada are therefore illegal, with only limited and narrow exceptions for transactions with highly sophisticated investors. Nevertheless, some persons are using misleading information to promote these products as legal and legally offered.

The Binary Options Rule came into force in Ontario on December 12, 2017 and is available on the OSC website at the following link: **http://www.osc.gov.on.ca/en/54014.htm**

In addition, over the last year, CRR staff have assisted Enforcement Branch staff in a number of enforcement proceedings involving unregistered offshore platforms that have victimized Canadian investors. Lastly, CRR staff have also worked with the Investor Office in developing investor warning materials about the risks of binary options, including the materials at: **http://www.binaryoptionsfraud.ca**.

Before making a decision to invest, investors should visit **aretheyregistered.ca** to check the registration of a person or company offering the investment. There are no registered individuals or firms permitted to trade binary options in Canada.

3.2 Syndicated mortgages

On March 8, 2018, the CSA published a notice and request for comment for proposed amendments to both NI 45-106 and NI 31-103 relating to syndicated mortgages (the **Proposed Amendments**).

The purpose of the Proposed Amendments is to introduce additional investor protections related to the distribution of syndicated mortgages and to increase harmonization regarding the regulatory framework for syndicated mortgages across all CSA jurisdictions.

At present, the Act provides that mortgages sold by persons registered or exempt from registration under mortgage brokerage legislation are exempt from the registration and prospectus requirements in Ontario. These exemptions currently include syndicated mortgages, which are defined as mortgages in which two or more persons participate, directly or indirectly, as the mortgagee.

The Proposed Amendments include changes to the prospectus and registration exemptions available for the distribution of syndicated mortgages, and in particular:

- remove the prospectus and registration exemptions for trades in syndicated mortgages in the CSA jurisdictions where the exemptions are available (in Ontario, the Act will be similarly amended),
- introduce additional requirements to the OM exemption under section 2.9 of NI 45-106 that apply when the exemption is used to distribute syndicated mortgages, and
- amend the private issuer prospectus exemption under section 2.4 of NI 45-106 so that it is not available for the distribution of syndicated mortgages.

The comment period for this notice ended on June 6, 2018. CSA staff are reviewing the comments received and anticipate that the final amendments will be published shortly.

3.3 OBSI Joint Regulators Committee (JRC)

On March 29, 2018, the CSA, IIROC, and MFDA jointly published the fourth annual report of the JRC (the **JRC Annual Report**), see ***CSA Staff Notice 31-353 OBSI Joint Regulators Committee Annual Report for 2017***.

The JRC Annual Report:

- provides an overview of the JRC's mandate and its major activities during the year,
- details steps to strengthen OBSI's ability to secure redress for investors by considering a regulatory framework to facilitate binding decisions, and
- describes the JRC's ongoing monitoring of:
  - complaint volumes,
  - the types of investment issues raised in complaints, and
  - cases where the amount compensated by the registered firm was below the OBSI recommendation.

The JRC is comprised of representatives from the CSA, IIROC and MFDA. It meets regularly with OBSI to discuss governance and operational matters and other significant issues that could influence the effectiveness of the dispute resolution system. For more information on the JRC, please see the **JRC web page** on the OSC's website.

Publication of joint notice

On December 7, 2017, the CSA, IIROC and MFDA released a joint notice ***CSA Staff Notice 31-351, IIROC Notice 17-0229, MFDA Bulletin #0736-M Complying with requirements regarding the Ombudsman for Banking Services and Investments (OBSI)***.

The notice highlights concerns about some registered firms' complaint handling systems and participation in OBSI's services, and sets out potential regulatory responses. The notice also highlights regulators' concerns regarding the use of an internal "ombudsman" as part of complaint handling systems.

We expect registered firms to participate in OBSI's dispute resolution process in a manner consistent with their obligation to deal fairly, honestly and in good faith with their clients and to respond to each customer complaint in a manner that a reasonable investor would consider fair and effective.

3.4 Custody requirements for IFMs and PMs

On June 4, 2018, the amendments to NI 31-103 that enhance the custody requirements (the **Custody Amendments**) came into force. The related guidance in NI 31-103CP became effective on the same date.

The Custody Amendments apply to investment fund managers, advisers and dealers (with certain exceptions, including those described below). These amendments (i) address potential intermediary risks when registered firms are involved in the custody of client assets, (ii) enhance the protection of client assets, and (iii) codify existing custodial best practices of registered firms.

Generally, the Custody Amendments:

- require registered firms to ensure that a "qualified custodian" (as defined in NI 31-103) is used to hold securities and cash of a client or an investment fund in certain circumstances,
- with limited exceptions, prohibit self-custody by registered firms and prohibit the use of a custodian that is not functionally independent of the registered firm,
- require registered firms to confirm that the securities and cash of a client or an investment fund are being held by a qualified custodian, and that the custodian's records show that the client or investment fund beneficially owns these assets, with limited exceptions, and
- require registered firms to disclose to clients where and how client assets are held or accessed, and any associated risks and benefits.

The Custody Amendments do not apply to certain firms, clients, investment funds, or assets. These exceptions are typically based on whether another custodial regime applies, there is no (or limited) intermediary risk, or the client has a certain level of sophistication. For example, exceptions exist for the following:

- investment funds subject to NI 81-102 or National Instrument 41-101 *General Prospectus Requirements*,
- customer collateral subject to custodial requirements under National Instrument 94-102 *Derivatives: Customer Clearing and Protection of Customer Collateral and Positions*,
- registered firms that:
    - are members of IIROC or the MFDA, and
    - comply with the custodial provisions of IIROC and the MFDA, respectively,
- securities recorded on the books of a security's issuer, or the transfer agent of that issuer, only in the name of the client or investment fund,
- permitted clients that are not individuals and not investment funds, and
- mortgages under certain conditions.

Future proposals to revise the Custody Amendments (including the terminology and the exemptions) may follow as a consequence of the CSA's ongoing policy work in respect of both the modernization of investment fund product regulation under NI 81-102 and derivatives.

For more information see NI 31-103, NI 31-103CP, and the related CSA notice of amendments published on July 27, 2017 at: **http://www.osc.gov.on.ca/en/SecuritiesLaw_20170727_31-103_amendments.htm**.

3.5 Amendments to NI 31-103 to clarify restrictions on EMD participation in prospectus offerings & brokerage activities

On December 4, 2017, certain amendments to NI 31-103 that impact the EMD category of registration came into force. These amendments, among other things, make it clear that an EMD is not permitted to act as a dealer or underwriter in a distribution of securities being qualified by a prospectus. This restriction includes:

- acting as a "selling group member" in a prospectus distribution, or
- acting as an agent in a special warrant transaction.

The ID category or, in the case of a mutual fund prospectus distribution, the MFD category, are the appropriate dealer registration categories for prospectus distributions. However, the amendments do not have any impact on the ability of an EMD to participate in a distribution by an issuer, including a reporting issuer, under a prospectus exemption.

In addition, the amendments further clarify the existing restriction on EMDs participating in brokerage activities involving listed securities.

An overview of the amendments to NI 31-103 that impact the EMD category of registration may be found in the Registrant Outreach Session on EMDs, available at the following link:

http://www.osc.gov.on.ca/documents/en/Dealers/ro_20171121_exempt-market-dealers.pdf

Part 4 ACTING ON REGISTRANT MISCONDUCT

Registration is a privilege and not a right, that is granted to individuals and firms that have demonstrated their suitability for registration. (*Re Sterling Grace & Co. Ltd. and Casale, (2014) 37 O.S.C.B. 8298, 8331*)

Elizabeth King, Deputy Director

The OSC is committed to improving the efficiency and effectiveness of its compliance, supervision and enforcement processes and will protect the interests of investors by taking action against firms and individuals who do not comply with Ontario securities law. These activities help to deter misconduct and non-compliance by registrants and market participants.

OSC Statement of Priorities 2018-2019

4.1 Annual highlights and trends

The Registrant Conduct Team within the CRR Branch is responsible for investigating conduct issues involving individual and firm registrants, recommending regulatory action where appropriate, and conducting OTBH proceedings before the Director. Potential registrant misconduct comes to our attention through compliance reviews, applications for registration, disclosures on NRD, and by other means such as complaints, inquiries or tips.

Registrants must also remain alert and monitor for potential misconduct by enacting and implementing appropriate policies and procedures and ensuring that controls are in place to detect and address instances of misconduct.

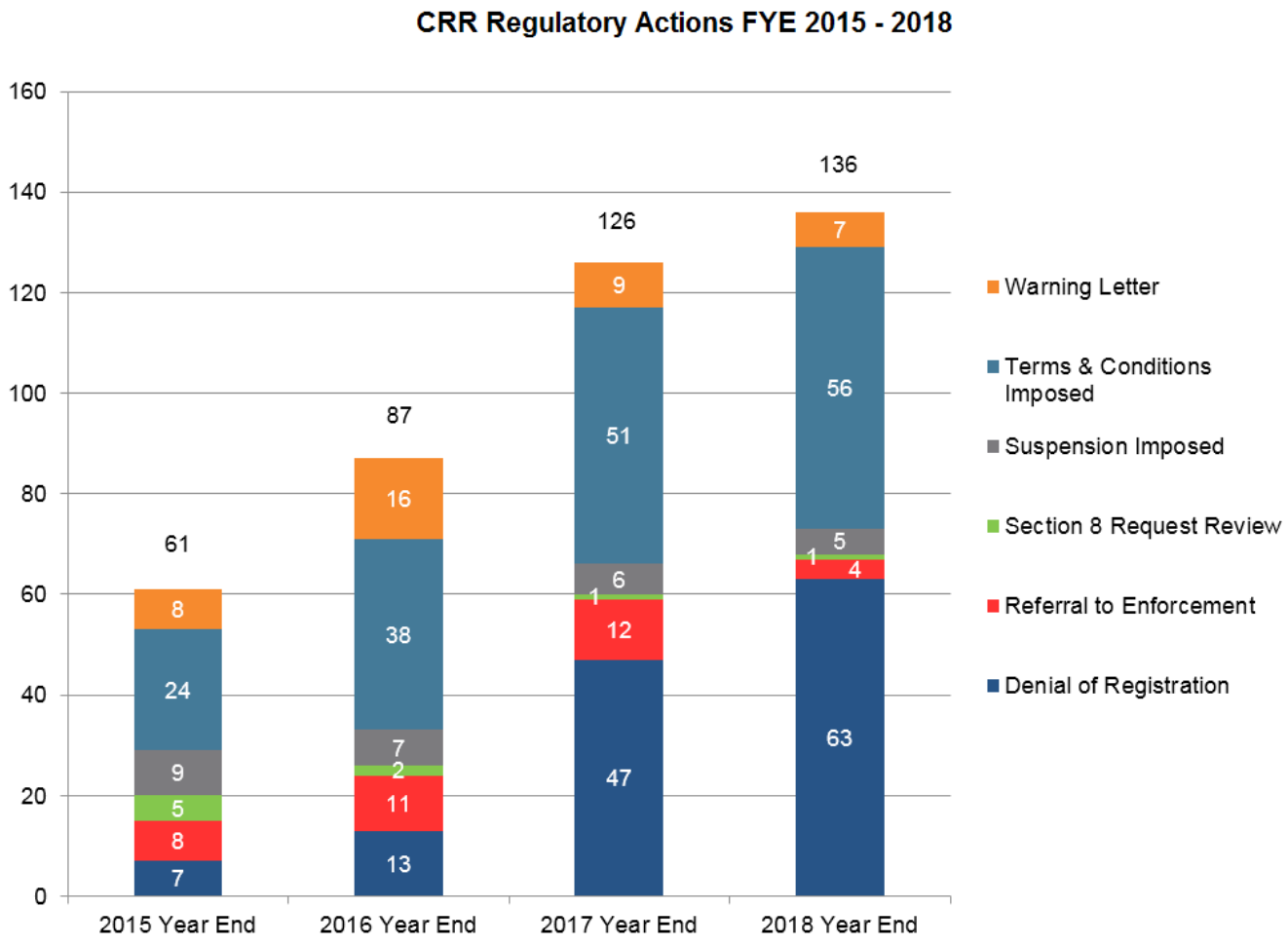
As our Director recently stated:

> "Investors place a great deal of trust in registrants' ability to assist them with financial matters. Registrants help clients evaluate their financial needs and objectives, assist with developing a plan to meet those objectives and recommend products that are suitable for the client. Clients expect registrants to have high standards of fitness and business conduct and act honestly and responsibly."

"We need to deal promptly and effectively with registrant misconduct to be fair to registered firms and individuals who do their best to comply with Ontario securities law."

Michael Denyszyn, Manager
Registrant Conduct Team

The following chart summarizes the regulatory actions taken by CRR staff against firms or individuals engaged in registrant misconduct or serious non-compliance with Ontario securities law.



The chart illustrates that CRR makes use of regulatory actions along the compliance-enforcement continuum, the action being commensurate with the magnitude of the misconduct or non-compliance in a given situation. Terms and conditions, denials of registration, and suspensions of registrations are all tools available to CRR staff to address serious non-compliance. Referrals are made to the Enforcement Branch in cases where the appropriate tool is a power that can only be exercised by the Commission.

CRR is continually improving our information tools, which is having the intended effect of identifying high risk registrants and applicants for registration. This has resulted in an increase in regulatory actions over the past four years. Sources of information include background and solvency checks on individual registrants or individual applicants, responses to the RAQ, external contacts received directly and indirectly from the Contact Centre, and referrals from SROs and other organizations.

The Registrant Conduct Team continues to investigate instances of the significant and recurring issue of false or misleading applications for registration, the consequences of which may include regulatory action.

CSA Staff Notice 33-320 The Requirement for True and Complete Applications for Registration was published on July 13, 2017 to remind applicants of their obligation to provide true and complete information in their applications, and to encourage firms to self-assess their existing policies and procedures relating to the due diligence they must exercise to ensure the truth and completeness of applications they sponsor. The guidance in the notice is equally applicable to registrants and all registration-related documents and information updates they are required to deliver pursuant to their ongoing obligations under NI 33-109 and NI 31-103.

4.2 Opportunity to be Heard (OTBH) process

Prior to a Director of the OSC imposing terms and conditions on registration, refusing an application for registration, or suspending a registration, an applicant or registrant has the right under section 31 of the Act to request an OTBH before the Director. There were 11 OTBH decisions from fiscal 2017/2018.

A registrant or applicant may also request a hearing and review by the Commission of a Director's decision under section 8 of the Act. A section 8 review was requested once this fiscal year.

DIRECTOR'S DECISIONS

Director decisions on OTBH proceedings are published in the OSC Bulletin and on the OSC website at **Director's Decisions**, where they are presented by topic and by year. Director decisions can be used as an important resource for registrants and their advisers, as they highlight matters of concern to the OSC, as well as the regulatory action that may be taken as a result of misconduct and non-compliance.

4.3 Cases of interest

CONTESTED OTBH DECISIONS AND SETTLEMENTS BY TOPIC

The following matters came before the Director this year.

i) Appointing a UDP

Registrant and date of Director's decision	Description
Hanane Bouji June 22, 2017	Hanane Bouji, already a director of two affiliated firms and registered as a dealing representative, applied to amend her registration by adding the category of UDP. Bouji's father, who was the former UDP of the firms and the sole shareholder, was the subject of significant sanctions due to past misconduct, including a prohibition on acting as an officer or director. Staff argued that the amended registration would be objectionable in light of evidence that the applicant's father remained active in directing the affairs of the firms despite the prohibitions, and in light of the non-independent applicant acquiescing in this misconduct while acting as the Chair of the Board of Directors for the firms. Following an OTBH, the Director agreed and refused to amend the registration. Bouji requested a hearing and review under section 8 of the Act, and the Commission confirmed the Director's decision, citing the applicant's role in the firms' failure to appropriately restrict the applicant's father's role in their respective businesses.

ii) Best execution

Registrant and date of Director's decision	Description
Acker Finley Asset Management Inc. September 26, 2017	Acker Finley Asset Management Inc. is a registered PM and IFM. The firm provides discretionary management services to a number of individual accounts, and advises and manages two investment funds. A compliance review by Staff found that the firm had been placing many of its trades through its affiliated ID, and that the firm had no policies or procedures in place as to how it would assess compliance with its best execution obligation when it directed its trades to its affiliated dealer. Following an opportunity to be heard, the Director concluded that the firm had failed to comply with its obligations:

ii) Best execution (cont'd)

	• to make reasonable efforts to achieve best execution, • to make a good faith determination that its clients receive a reasonable benefit from the use of client brokerage commissions, and • to respond to a material conflict of interest in an effective manner. As a result, the Director imposed some (but not all) terms and conditions that had been recommended by Staff. Specifically, the terms and conditions imposed by the Director required the firm to retain a compliance consultant to assist the firm in rectifying the issues that had been identified by Staff through its compliance review.

iii) Compliance with securities laws of foreign jurisdictions

Registrant and date of Director's decision	Description
Pierre Prieur November 7, 2017	Pierre Prieur was registered as a mutual fund dealing representative. Prieur resides in Quebec, and therefore his principal regulator was the Autorité des marchés financiers in Québec (**AMF**). On September 28, 2017, the Chambre de la sécurité financière ordered that Prieur's registration under Quebec securities law be suspended for two months following his admission that he had forged a client's signature on two discretionary management agreements. On November 3, 2017, and at Staff's request, Prieur consented to a suspension of his registration in Ontario. In requesting his consent to this suspension, Staff informed Prieur that it was of the view that it would be objectionable for him to be registered in Ontario during such time as his registration in Quebec was suspended.
Hugh Smilestone November 10, 2017	Hugh Smilestone filed an application for registration in an additional jurisdiction to reinstate his registration in Ontario. Staff recommended that Smilestone's Ontario registration as a mutual fund dealing representative be subject to terms and conditions that mirrored terms and conditions imposed on Smilestone's registration by Nova Scotia, his principal regulator. Smilestone had been registered as a mutual fund dealing representative in Nova Scotia for approximately 14 years, when, in March 2010 some of his conduct became the subject of an investigation of the MFDA. In a 2013 settlement agreement with the MFDA, Smilestone admitted that he had engaged in conduct in violation of MFDA rules, including, among other things, falsifying client signatures on account documents and engaging in unauthorized discretionary trading. Smilestone was fined and prohibited from conducting securities related business for two years.

iii) Compliance with securities laws of foreign jurisdictions (cont'd)

	In 2015 the Nova Scotia Securities Commission approved Smilestone's application for registration in Nova Scotia subject to certain customized supervisory terms and conditions. When Mr. Smilestone reapplied for registration in Ontario, Staff recommended terms and conditions on his Ontario registration which included strict supervision of his trading activity, requirements concerning disclosure of his outside business activities and other customized terms and conditions that were consistent with those imposed on his registration in Nova Scotia, which Smilestone consented to.
Bonwick Capital Partners, LLC November 27, 2017	A registered firm, whose principal regulator is the AMF, failed to pay its annual fees or deliver its annual audited financial statements to the AMF. The firm has also previously had its FINRA membership in the U.S. cancelled for, among other reasons, non-payment of fees. After the AMF suspended the firm's registration and in light of late fees owing to the OSC, Staff recommended that the firm's registration also be suspended in Ontario. The firm did not request an opportunity to be heard, and the Director accepted Staff's recommendation to suspend the firm's registration.

iv) False client documentation

Registrant and date of Director's decision	Description
Christopher Aqui March 28, 2017	Christopher Aqui applied for a reactivation of registration on April 8, 2016. A review of Aqui's application revealed that he had been terminated from his previous firm for material violations of the firm's policy concerning the use of blank signed forms, making false representations on an annual compliance questionnaire regarding the use of blank signed forms, and non-compliance with the firm's policy regarding deferred sales charges (**DSC**). Specifically, the review found that Aqui had obtained at least 90 pre-signed forms for 15 different clients, and most of those forms had been used for securities transactions. In one case, pre-signed forms had been used to facilitate discretionary trading. Aqui also had at least 27 forms for 17 clients where he had altered the document without having the client initial the change. During his employment, Aqui had completed annual compliance questionnaires from his firm in which he represented that he did not obtain or use pre-signed forms. Finally, from time to time Aqui would transfer his clients' assets from one DSC mutual fund to another, thereby restarting the DSC schedule and generating a sales commission for himself. Although Aqui believed he verbally informed his clients that their DSC schedule would restart, he did not provide them with any written disclosure to that effect.

iv) False client documentation (cont'd)

	Consequently, Staff identified concerns relating to Aqui's suitability for registration. In March 2017, Staff and Aqui signed a settlement agreement in which Aqui agreed: • to withdraw his application and not to reapply for 15 months from the date of the application under consideration, • he would successfully complete the Conduct and Practices Handbook Course before reapplying, and • that if his registration was reactivated it would be subject to supervisory terms and conditions for a period of not less than one year.

v) Financial condition

Registrant and date of Director's decision	Description
R. Alan Filer November 13, 2017	R. Alan Filer, a mutual fund dealing representative, invested in tax shelters over a 15 year period. The Canada Revenue Agency (**CRA**) denied the deductions associated with these tax shelters and imposed penalties and interest on the taxes owing. As a result, Filer entered into a consumer proposal and agreed to pay a high six figure amount to the CRA over a defined five year payment schedule. After reviewing Filer's financial disclosure change submission under NI 33-109, Staff followed general practice and recommended that Filer's registration be subject to close supervision terms and conditions to mitigate against an identified solvency concern. During the OTBH, Filer submitted, among other things, that he had the financial means to meet the payment schedule, had never been the subject of a client complaint or criminal charge, and that colleagues provided necessary checks and balances with respect to his activities. Nonetheless, the Director found no reason to vary from the Commission's long standing practice of imposing close supervision terms and conditions in circumstances where Staff has solvency concerns with a registrant, finding the practice appropriate in the Filer's case and consistent with the Commission's investor protection mandate. The Director determined that the registration of the Filer should be subject to the close supervision terms and conditions until such time as his financial obligation under the consumer proposal to the CRA is satisfied.

vi) Misleading staff or sponsor firm

Registrant and date of Director's decision	Description
Sital Singh Dhillon July 31, 2017	Following an OTBH, the Director refused Sital Dhillon's application to reactivate his registration as a mutual fund dealing representative, finding that Dhillon did not meet the proficiency requirement because it had been almost 27 years since he passed the Canadian Investment Funds Course Exam, and none of the exemptions to the rule that an exam must have been completed within three years of the date of the application were applicable (see section 3.5 of NI 31-103). The Director also found that Dhillon lacked the integrity required for registration based on conduct issues that had occurred at two previous sponsor firms, his participation in the preparation of a false tax return for a client, and misrepresentations made to Staff during the application process. The Director found that Dhillon lacked any remorse for his conduct and refused to acknowledge any wrongdoing on his part. Dhillon's application for a hearing and review under section 8 of the Act by a panel of the Commission was heard on February 12, 2018, and dismissed with reasons on April 3, 2018. In the time between the Director's decision and the commencement of the hearing and review application, the firm that had been sponsoring Dhillon's application withdrew its support. The panel allowed the hearing and review to proceed on the basis that, notwithstanding the firm's withdrawal of its sponsorship, Dhillon was still directly affected by the Director's decision, and should be entitled to continue with his application. However, the panel dismissed the application for the same reasons as the Director concluding that Dhillon lacked integrity and was ungovernable.

vii) Outside business activity

Registrant and date of Director's decision	Description
Donald Mason November 30, 2017	Donald Mason, a registered mutual fund dealing representative, disclosed that he had begun an outside activity as a lay minister in a church, visiting people in need and assisting the congregation in prayer during religious services. Staff recommended "restricted client terms and conditions," by which Mason would be restricted from acting as a dealing representative with members of his church or their families, citing the potential for undue influence given his position of spiritual leadership and caregiving. Although Mason had not traded in securities with church members, he nevertheless exercised his OTBH right. Mason argued that his religious freedoms were compromised by these terms and conditions, and that he should not be required to confirm that his clients are not church members. However, the Director imposed the terms and conditions, citing the need to protect investors from potential undue influence. Mason has requested a hearing and review of the Director's decision under section 8 of the Act, which has been scheduled for late 2018.

viii) Trading or advising without appropriate registration

Registrant and date of Director's decision	Description
Kashmir Singh Marok July 4, 2017	Kashmir Marok was a registered mutual fund dealing representative. In March 2016, Marok initiated contact with a school board regarding a proposal by him to distribute securities marketing materials relating to registered disability savings programs to parents of children with special learning needs who might be eligible for such programs. In his communications with the board, Marok was informed of specific concerns that the board had about the proposal, was informed that consent was not being given for a board-wide distribution, and that if Marok wanted to seek approval from principals on a school-by-school basis, he could do so. Marok told the principal of the school where his wife was a teacher (and that was within the board) that he had the board's approval for his proposal, and the principal then authorized him to distribute his materials at the school. Marok assembled approximately 30 information packages and provided them to his wife, who in turn placed them in the mailboxes of teachers with special needs children in their class (which information she had obtained from the school's special education department) to be taken home by the children to give to their parents.

viii) Trading or advising without appropriate registration (cont'd)

	A number of parents who received the packages distributed by Marok were upset. Nobody who received a package ever became a client of Marok, and he claimed that he had honestly misunderstood the instructions given to him by the board, although he admitted that he failed to take reasonable care to ensure that he had the informed consent of the principal (and his own supervisor) before carrying out his plan. On July 5, 2017, the Director approved of a settlement agreement between Marok and Staff in which Marok agreed that: • his registration would be suspended for two months, • upon reregistration, his registration would be subject to supervisory terms and conditions for a period of not less than nine months, and • he would successfully complete the Conduct and Practices Handbook Course.

Part 5 ADDITIONAL RESOURCES

5.1 Registrant Advisory Committee

Established in January 2013, the Registrant Advisory Committee (**RAC**) is currently comprised of 10 external members. The RAC's objectives include:

- advising on issues and challenges faced by registrants in interpreting and complying with Ontario securities law (registration and compliance related matters), and
- providing feedback for the development and implementation of policy and rule making initiatives that promote investor protection and fair and efficient capital markets.

The RAC meets quarterly with members serving a minimum of 2 year terms. Topics of discussion over the past fiscal year included:

- proposed amendments to enhance the client-registrant relationship,
- referral arrangements,
- sales practices, incentives and compensation structures, and
- the OSC's whistleblower initiative.

5.2 Fintech Advisory Committee

We have a Fintech Advisory Committee (**FAC**) to advise OSC staff on developments in the fintech space as well as the unique challenges faced by fintech businesses in the securities industry. The current FAC includes key players from a broad spectrum of the fintech community, ranging from innovation hubs, to startups, to financial institutions. The committee plays a critical role in advising the OSC on meeting the novel demands of the rapidly growing fintech space.

The FAC meets quarterly, with members serving one-year terms. Topics of discussion over the past fiscal year included:

- blockchain technology,
- issues around cryptoasset offerings, including custody and auditing,
- artificial intelligence and machine learning,
- open data, and
- KYC onboarding processes.

5.3 CRR directory

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