Pearls of wisdom: Investment management regulatory trends and preparing for the new SRO

January 17, 2023

There were pearls, boas and other Harry Styles references aplenty at BLG's annual investment management seminar, as we welcomed guests back to "BLG's house" after two years of virtual gatherings. It's been a busy year for those staying on top of changes in the investment management space, and speakers were full of helpful tips on topics ranging from enforcement and fund management to ESG issues, conflicts of interest and tax challenges – plus information about the new self-regulatory organization (SRO) coming into effect in January 2023.

We've summarized some of the main points below. For all the details, watch the webinar recording or skim the full transcript*. Let's see how many Harry references you can get!

**Recording and transcript available in English only.*

What are the key enforcement trends from 2022?

Speaker: David Di Paolo
Find it in the recording: 00:04:03-00:17:32

The areas of emphasis for IIROC and the MFDA are:

Seniors. Once again, protecting seniors and vulnerable clients is a key priority.

Conflicts of interest . Client-focused reforms (CFRs) will be enforced. Expect audits that look for conflict of interest and documentation relating to how conflicts of interest are managed.

Know your product (KYP). Depending on the results of those audits, there will be more investigations. We're seeing more conflicts of interest in KYP investigations than in the last decade.

When it comes to SRO consolidation, not much is expected to change on the enforcement side in the short-term while the two organizations operate as silos. From

summer 2023 to early 2024, we expect more focus on compliance audits and enforcement, accompanied by bigger fines.

What we know (and don ’t know) about the new SRO

Speakers: Julie Mansi and Bill Donegan
Find it in the recording: 00:18:07-00:38:10

Heading into Jan. 1, 2023, we will have a new SRO and a new Canadian Investor Protection Fund. All current MFDA and IIROC members will automatically be members of the new SRO and investor protection fund.

What we know:

- New interim rules have been published.
- The compliance manual will need to be updated.
- Policies and procedures will have to be revised.
- This is an opportunity for organizations to rethink their distribution model, including consolidating their mutual fund dealers and investment dealers into a single platform.

What we don ’t know:

- The name of the SRO, which is important for those looking at creating a new dealer. You don’t want to create documentation, put a name on it and then have to redo it.
- Details of new fee models, which will significantly influence the business case you develop if you’re changing your business model.
- The content and timing of the combined rules, including whether changes will be significant.
- What will happen in Québec.

What’s new for investment funds?

Speakers: Lynn McGrade, Grace Pereira, Donna Spagnolo and John Stanley
Find it in the recording: 00:34:18-00:58:52

In terms of investment funds, this is a time of intense regulatory change and scrutiny, geopolitical risk and market uncertainty, and shifting investing patterns.

ESG disclosure management and marketing

The CSA published Staff Notice 81-334, which sets out the disclosure standards for funds that incorporate ESG criteria, especially in their investment objectives and strategies.

From a regulatory perspective, ESG disclosure isn’t going away, given the popularity of ESG products with investors and the regulators’ mandate to protect these investors. Regulators are looking at ESG-related disclosures in prospectuses as well as in

continuous disclosure documents. Regulators in other countries have taken different approaches to ESG integration funds and it remains to be seen whether Canadian regulators will follow their lead.

Conflicts of interest

Registrants have just finished a significant review of their conflicts of interest. This has helped them consider how they will avoid and resolve conflicts in the best interests of investors.

Tax compliance issues

The new FATCA/CRS changes impacting custodians, dealers, portfolio managers and funds are effective Jan. 1, 2023. The latest changes that impact client-name accounts also remove the ability for the parties in those relationships to rely on written agreements to insulate themselves from penalties where it is clear that one party is not fulfilling its FATCA/CRS responsibilities.

Tips to clear the regulatory haze

Speakers: Sarah Gardiner, Jason Streicher (BLG Beyond AUM Law), Michael Taylor, Matthew Williams
Find it in the recording: 00:59:27-1:18:15

In this time of great change, here are some tips to set yourself up for success.

- **Update and file your F4 amendments** for your current registrants and permitted individuals. You have until June 2023 to file your F4 updates, but this is accelerated if changes in your F4 trigger the requirement to update the form.
- **Develop an internal tracker for outside activities** so that the chief compliance officer who is approving an outside activity can see what was done, even if the activity is no longer reportable.
- **Refresh your compliance manual** . Confirm it's up to date, taking a broad perspective in your review.
- **Review the OSC 's latest annual summary report for dealers, advisors and investment fund managers** for good guidance on policies and procedures.
- **Have a remote working supervision policy in place** and make sure your reps are following it.
- **Update your account documentation for client-refocused reform.** To be ready for compliance audits**,** update your KYC forms, KYC update forms and investment management agreements.

In summary

With the new SRO having come into effect in January, we can expect ongoing changes. If you have any questions about the content from this seminar – or you just want to let us know how many Harry Styles references you counted – reach out to any of the key contacts listed below.

Read the full transcript here

Kathryn Fuller

Good afternoon everyone, and welcome back to BLG's house. It is so nice to be able to do these events again in person. But we're also very thankful for this new hybrid world that allows us – those of you who are not working in person – to be able to attend by webinar. For those of you who don't know me, my name is Kathryn Fuller. I'm a partner at BLG and the Toronto leader of our investment management group. And if you have not yet figured it out from our introductory music, or are wondering about my accessories for today, our theme for the event is Harry Styles. We have a poster you'll see and we've got the clouds for you. We've actually managed to get the weather to tie into our theme for those of you who are in person. But if you're not familiar with this music, then do what I did, you can ask your children. My 9 year old son thinks now that I might actually do something cool when I go to work. Please don't disabuse him of that. Although he did suggest that the World Cup might be a better theme for today's event. So thank you for choosing us and Harry over soccer this afternoon. 2022 has continued to be a whirlwind of change on many fronts. As Harry Styles said, things haven't been quite the same. There's a haze on the horizon. And by that, I'm sure Harry was talking about regulatory haze. But don't worry, BLG is here to take you through some late night talking about regulatory trends, with the goal of making you happier baby, by the end of our seminar. We've seen strong enforcement action from the regulators in the past year. Unlike Harry, who could never learn the sign of the times, I know that none of you will be crying and running from any regulatory bullets after my securities litigation partner takes us through what's been happening in the enforcement world. As well as what we can expect for the future, including the future under the new SRO.

And speaking of the new SRO, does anybody want to take bets on when we're going to get a proper name? Clearly, picking a name is not the priority at the moment, as the new organization is just getting ready to set up the basic infrastructure in place for January 1. We saw, today in fact, some announcements from the CSA that they recognize the new SRO and the new CIPF. So I know we're all looking forward to hearing from my BLG partner, Julie Mansi and my AUM law colleague, Bill Donegan, about the opportunities and challenges that arise from the new SRO. Will it taste like strawberries and be all watermelon sugar high? Or will dealer firms encounter head winds as they make strategic decisions about whether and how to change their business model. And for those fund managers who think they don't need to worry about the new SRO, I'll point out that it also brings change for them. For example, the new rules permit investment dealer to carry for a mutual fund dealer, which may allow MFDA firms more easily offer ETFs to the clients. And speaking of funds, the regulatory haze continues for them as well. We hear from our panel of fund experts about actions managers can take to address green washing risks, liquidity risks, conflicts of interest and tax challenges followed then by our rapid fire registrant regulation and compliance panel. They'll take us through the 12 tips you need to know to clear that regulatory haze.

Regardless of whether you are a fund manager, dealer, portfolio manager or service provider, it's clear that the regulatory environment for the investment management industry continues to evolve at a rapid pace. To put it into Harry's words, you know, it's

not the same as it was. So following on, from Harry's words of wisdom, I'd like to invite my disputes partner, Dave Di Paulo, to share his views on trends and enforcement from the securities regulators so he can help us all stay out of trouble.

Dave Di Paolo

Thank you very much Kathryn, and I'm very happy to be here. I recognize the irony of hosting an event in which we're welcoming you back to your house, and the first speaker is participating by video. Sadly, I'm fighting a terrible cold and I think you would all much prefer that I not be in the room with you. I am going to tackle this topic really through the lens of three things. I'm going to give you a sense of the enforcement trends for 2021/2022 which is the last year for which we have data. I'll talk to you a little bit about what I think the upcoming enforcement priorities will be, and then and try and tie all three of those things together as we move forward.

So, if we move to the 1st slide, I'll start with the MFDA and what we can draw out of the MFDA enforcement report. And I will say that I had a theory going into 2021 and 2022 after SRO consolidation was announced, and my theory was that both SROs would be tripping over themselves to be more aggressive on enforcement to position themselves better for the ultimate merger. As we go through the statistics you'll see I was right with one of them and very, very wrong with the other. So, let's start with the MFDA. With the MFDA, you can see they were incredibly active in 2021, in relation to their enforcement activity. Disciplinary proceedings, up significantly. Disciplinary hearings that were concluded, up significantly. And total fines that were levied in 2021, 4.3 Million dollars + 1 in 33,000 in costs. So that's a significant uptick in the overall fine amount and a significant uptick in the overall cost award, including the number of registrants who were subject to discipline. I'll talk a bit in a moment about why that is, but just to draw your attention to the fact this is a significant uptick.

On the next slide, I set out sort of what some of their enforcement priorities were in the previous year. And there were really four that you can derive to their most recent enforcement report. The first is they continue to bring cases in relation to supervision whether it's financial requirements, supervision of sales. They are always looking at supervision as an issue and they continued to do that in the last year for which there's data available. Similarly, they did prosecute and continue to look at issues involving sales incentives. So these are dealers who sell proprietary products and looking at the circumstances in which most dealers are incentivizing the sales of those products and whether they violate the applicable national instrument.

Two other reports with priorities that we have on the next slide are client complaints. This is a trend that's been going on frankly for a while. And what I'm referencing here is what I described as sort of the micro management by the MFDA, the complaint handling process. So, well they don't have jurisdiction to tell dealers how much they should be paying to settle client complaints. They look at it through the lens of the obligation to handle complaints fairly and in the last year for which data was available, they actually brought 7 cases against members in relation to deficiencies in their complaint handling. Namely you didn't pay enough to settle this particular complaint. And then lastly, continuing with trending, we've seen in the last couple of years, seniors and vulnerable persons. Any cases involving seniors and vulnerable persons were investigated and there are a number of prosecutions in relation to those issues.

So, then over to the IIROC story. Firstly, in relation to IIROC, a few highlights, that IIROC sort of alludes to in their enforcement report; one is the early resolution. So you'll all remember that with great fanfare IIROC published an early resolution guideline in the early part of 2021 which said that if you qualified, you get a 30% discount. Many were skeptical as to how that would play out in practice. How do you calculate the 30%? What's it off of? I shared that skepticism. I could tell you, I was involved in 3 of the 4 cases that got credit for early resolution. It's legitimate. We know she negotiated with settlement amounts based on precedent cases and the 30% was applied to that. So it does work. Secondly, IIROC now has the ability to enforce their fining powers, if it's a court order in every jurisdiction in the country, and they tout that as a big success. And lastly, they did go fully virtual as did the MFDA frankly. And it was a huge success. It's certainly a lot easier for registrants being investigated and interviewed can do that from the comfort of their own home or offices, as opposed to being forced to do it in the MFDA or IIROC hearing rooms, which are intimidating. In terms of the stats, and here, you'll see where I was dead wrong. IIROC stats, in terms of enforcement activity, went way, way down in their last fiscal year. You can see from a high of about 127 in 2019, and 113 in 2021 when everything was virtual, they went down to 76 investigations completed. That's a really, really dramatic drop. The other step that I found just astonishing is that they only levied fines of 4 million dollars. Now if you think about that and you compare it to the MFDA fines and you look at the different kind of scope in terms of size of the members on the IIROC platform versus the MFDA platform, etc., that's a really staggering number, That IIROC's fine total was less than the fine total for the MFDA.

On the next slide, this just sort of gives you a sense, and it is consistent with the MFDA story, of what is driving the investigations that IIROC is doing and not surprisingly, most of it is matters have been reported on concept and, and I think that's been true for a number of years and it really was true in the last couple of years. Followed, you know, quite far behind by complaints they received directly from the public. And so, IIROC, just like the MFDA, most of the things they investigate are things that are self reported by members over the course of the year.

Over the next slide, just to give you a sense of how often we're getting contested hearings, you can see that most of the IIROC proceedings are dealt with by way of settlement. Although we are starting to see, finally, a bit of an uptick in terms of the number of contested proceedings. Although I will say that the vast majority of contested proceedings continue to be contested proceedings by individual registrants and not by dealers. Dealers continue to be extremely reluctant to fight their regulator for all the obvious reasons. I'm not sure if that's going to change as the fine amounts go up. One of the things that both IIROC and the MFDA have indicated, and I think you can see it when we get into the consolidated SRO, is the fine amounts will start to not creep up but jump up and jump up dramatically. Query whether or not dealers will start to contest hearings where they might have a defence in circumstances where they previously would be prepared to settle those cases, if these fine amounts go up as predicted.

On the next slide, I just sort of summarize for all of you just the types of cases that come up most regularly at IIROC, relative to their proceedings and investigations and it's not totally dissimilar to the MFDA. A few things, suitability continue to investigate suitability cases, failure to cooperate, supervision, but also inappropriate personal financial dealings. We're gonna touch on that in a second because that obviously highlights the issue of conflicts of interest. And I think that's an important one. And then lastly, before

we look at trends for next year, just the concluded proceedings by respondent type on the next slide, again most of the cases are cases against individual registrants with a much smaller number of cases against the dealers themselves. So in terms of where we think this is going next year and what the regulators are saying, both in their published guidelines, but also anecdotally in the discussions I'm having with enforcement council and senior leadership at IIROC and the MFDA, there really are three things that will be areas of emphasis for IIROC and the MFDA for the balance of this year and the consolidative SRO next year. The first is seniors again. No surprise there. But the last two are interesting. So, it's conflicts of interest in KYP. I was speaking recently at a conference on a panel with Karen McGinnis and Andrew Kriegler, and both of them said quite clearly to the attendees at that conference that the CFRs are meaningful. That they didn't go through all the headache and aches and all the consultations in the publishing the CFRs, if they weren't going to have teeth. And the way in which you give regulatory change teeth, is unfortunately for all of you, through enforcement. So we're going to see more emphasis in the context of audits on conflict of interest, in the resolution of conflict of interest, and the documentation relative to how conflicts of interest were managed, and similarly with respect to KYP and depending on the results of those audits, there will be more investigations in relation to those issues. And I can tell you, I'm already seeing it. I'm seeing way more conflicts of interest in KYP investigations than I've seen in the preceding, call it 10 years, and so much more to come on that score.

That's all the lead in then to SRO consolidation. I am still curious, as is Kathryn, with what the new name is going to be for this regulator that Mr. Kriegler at the last at the conference I was at said, we will have to wait and see, that's not a priority but something will come. In the next couple of slides, I sort of set up with the short term expectations and then the kind of medium term expectations. Short term expectations in a nutshell are, not much is going to change. Effectively they are going to take these two silos and operate them as silos in the short term. All of the technical requirements in terms of the special resolutions have now been passed and effectively they're going through the corporate process of amalgamating these two organizations. As Andrew said at this conference, you know, this is - we are amalgamating two very very large businesses. And I think that that was sort of a sobering comment and explains why some of the things that we all may be interested in will take a little bit longer than we may have otherwise anticipated. On January the 1st not much is going to change. We will have two sets of rules, two sets of people frankly, those in the MFDA and IIROC operating effectively as silos over the beginning parts of next year as the new consolidated SRO tries to figure out - Where do we find those synergies that were promised? How do we create the consolidation that everyone is anticipating as we move forward?

On the next slide I've set out medium term expectations and so when I talk about medium term, I'm talking about into the summer of 2023, the end of 2023 and early into 2024. And I think the first thing that the consolidated SRO, the new SRO will turn its attention to is, what do the new rules look like? And, you know, in my view, IIROC's approach to the rules has been very much more principals based, and the MFDA has been very much more prescriptive and I'm not commenting on which is better and which isn't better. I think my guess is the given the relevant degree of control that IIROC is going to have in the new SRO, we're probably going to see much more principal based rules that are harmonized and frankly will be easier sort of easier to grapple with as move forward. We will see more focus compliance audits and enforcement and I do think an increase over sight by this new SRO with a higher sort of emphasis on bigger fines as we think about the enforcement side. So lastly, before I turn it over to Julie and

Bill just in terms of where I think new SRO will be in relation to enforcement priorities, I reckon the MFDA have taken a very different approach to enforcement priorities. The MFDA's approach to enforcement priorities have been very much of a strict liability approach, in other words there is no violation to small that we won't prosecute and that's why you see pre-signed blank forms cases driving up their fine numbers. If you have one pre-signed blank form you are going to get prosecuted just like if you had 15 with maybe a smaller fine amount. IIROC's approach to enforcement has been very much more materiality driven looking at whether or not the type of kicks under investigation warrants a public prosecution or can be dealt with in some other way, like a warning letter or a cautionary letter. My guess again, given my expectation that IIROC's will have much more control in its consolidated organization then the MFDA is that the new SRO will take much more of that materiality approach to which cases they take on and which cases they ultimately prosecute. So again, I'm sorry I couldn't be with you, I hope you have a wonderful evening this evening with my colleagues and I will turn it over to Bill and Julie.

Kathryn Fuller

Thanks Dave. I'm not sure the regulators have figured out how to treat the industry with kindness at least not when it comes to enforcement actions but perhaps there's hope for some positive changes coming from the new SRO. I would now like to invite my BLG Partner Julie Mansi and my AUM Law colleague Bill Donegan to share some thoughts and opportunities and challenges offered by new SRO. I'm sure they were frantically reading the materials that came out today from the MFDA and IIROC so please treat them with kindness and don't quiz them too hard. At least give them the 24 hours to finish reading before you ask your hard questions.

Bill Donegan

Thanks Kathryn and thanks Dave. Can we go to the next slide please? Ok, what I wanted to start was to talk about what we know and what we don't know about the new SRO and what we know is that heading into January 1, 2023 we will have a new SRO and a new Investor Protection Fund and all current MFDA and IIROC members will automatically be members of the new SRO. Initially as Dave said, nothing should really change for members. The other thing we know about the interim rules that were published. They were published in May and after public comment through the summer there are going to be some changes made and the final version will be released before the end of the year. The interim rules are in two separate volumes, one is what they call the investment dealer and partially consolidated rules and then there are the mutual fund dealer rules and at a very high level the investment dealer rules are the old IIROC rule book modified to handle dual registered entities. That would be an entity which has both the mutual fund registration and an investment dealer registration. The mutual fund dealer rules are basically the current MFDA rules. The other thing that we know and really this is the thing that, I think if we take something away from today it's this. This is an opportunity for organizations to rethink their distribution model. What we have is at the high level and Julie is going to talk about this. Organizations will have the opportunity to consolidate their mutual fund dealers and investment dealers into a single platform. Mutual fund dealers with have the opportunity to add an investment dealer to their platform and vice versa. Also, the opportunity to explore quite creatively introducing carrying arrangements is something that everyone should think about.

Now the unknowns are fairly significant. The first is the name and you know what's in a name. The name is pretty important for people that are looking at first of all creating a new dealer. You don't want to go through the whole process of creating all your documentation, putting a name on it and then having to change that name and redo your documentation subsequently. Also for dealers that are updating their documentation on a regular cycle, it's really important to be able to include that new name in it rather than have to do an extra update when the new name comes out and that goes for the membership disclosure policy which you know requires IIROC and MFDA membership to be displayed, and everywhere from websites to signage, etc. The sooner we get to the name I would suggest the better and the longer the implementation period organizations have to make all of those changes, the better so that organizations can fit it into their normal course updates. Fee models are going to change. We don't know what the fee models will be but obviously for anyone thinking about adding a new platform or going to a dual register platform, fee models are going to be significant in terms of the business case that you are trying to develop.

The combined rules. We have the two rule books going into January but there will be combined rules coming at some point. We're not sure when and what those rules will look if there will be any material changes will be significant. Québec is another question mark for mutual fund organizations that carry on business in Quebec. The Québec only mutual fund dealers will be part of the new SRO but basically any mutual fund business by national dealers or Québec only dealers will remain regulated by the AMF for an indefinite transition period and we don't know how long that transition period will be and it just briefly, you can see continuing education is going to be harmonized. How it's harmonized will be significant more for advisors and for administration within a dealer and hill creates quite a bit of stress within a dealer when we're getting near the end of a cycle when trying to get everything into IIROC. So that's basically what I think we know and don't know. Julie?

Julie Mansi

So I want to be the person in the room that gets compliance and legal voice in this process and I think the way to sell it to the executive is to truly talk about the opportunities that come with this new legislation and this new structure and again, it's not another new rule, it's not another line on the compliance matrix which I'm sure we all have and love and adore. I think that in order to really kind of put compliance and legal on the forefront in your organizations, this is the project because I think the question that comes about is this a transformation moment for the industry and I'm going to talk about a few points here that respectfully don't have much to do with legal but this is the type of topics and tasks we're being asked about. How we manage this, is there new insight that we should be aware of and a few of the topics are.

So number one we know there will be regulatory impact, we know there will be updates to the compliance manual, we know we'll have to revisit policies and procedures but what about other things. What about the first topic being does or could this enhance your client user experience rather than the regulation. Is not better to stand back right now and say "are we selling the products that people want, are we not offering the services that an evolving group of millennials need, is this not a time to consider much larger issues how you communicate with clients". This is going to get, again this is transformative across the industry and something like a client focus on this type of topic I think will actually buy you a lot of credit in the executive management team, like as to

you know here's an opportunity. So where's another opportunity, advisor retention, attracting them and then the inevitable succession plan. Is this a moment in time when we need to start thinking about advisor retirement, advisor turn over. There will be a reaction from a significant number of advisors that are like "and this is it, that was the signal that I needed to know that now I want to move on, I want to go do something else" and are we addressing that type of focus right. Because here now you have got advisors that may want the new product offering, they may be the ones that are going to be pushing the transformation, pushing the platform, they may want a new service, they may want a new robo advisor, they may want to manage accounts. So I think that's an important part of this conversation that is happening right now.

The other one is simply restructuring. So when we think about. Okay so the one thing that I always hear "what, is there tax losses, like can we capitalized on tax losses, can we restructure around tax losses"? So there's a lot of activity and focus on again, this being an opportunity at a point in time to assess whether this is the platform you want, is this a product you want, is this meeting your user experience that you want, is it what your advisors want. So again, I think I kind of want, I'm probably sounding like I'm lecturing here, but it takes compliance and legal into the business and I think that is a good transition and discussion to be having. As I said, this is, so when we talked about this, you know finding the right path, cost benefit analysis, synergy, functionality. Prema is not in here but she always makes fun of me because I always us the word functionality in pretty much any context but these are important issues now that I think need to be drawn to the business and I think compliance and legal will be the touch point for this. So I think we're going on to the two current structures obviously that are dumping off so one of course will be dual registration. So this is where you are now going to conduct mutual fund business with investment dealer business and again this is what is coming up in our conversations, because we live in a universe where our regulatory system was siloed into products which is not the way that clients look at it. Clients don't look at it as you are a mutual fund dealer, you are an equity dealer, they look at exposure, investment opportunities. So here I think we have an opportunity to provide those dual platforms with the flexibility to attract new clients so this is one of the options. It's a big one right because you would be taking to probably large enterprises and respectfully with different cultures possibly. Like corporate cultures, compliance cultures and trying to merge this into one. Now how is this going to be done? So first of all you have to actually present a plan to the new SRO. So before the application starts, you have to in writing comment on what the operational transformation is going to look like. The big question is going to be how are you going to continue to meet and meet your compliance obligations from the plan. Once they're comfortable with the plan then you get to file the application. So please note the plan is significant because the plan will dictate how those dominos fall going forward. So the plan should not be seen as step one, the plan is like phase 1 through 7. The application is actually just now getting that into writing and I will say the new SRO has promised, and I think we have heard him say a multiple of times about there, "there will be simplified application process". Of course there will be a simplified process. I think the intention is to get everyone where they want to be but obviously the operational aspects are going to be significant. So simplified, I will take that with a grain of salt. In terms of things you need to consider in this structure, will be like exemptions because now we are taking one universe and another universe and moving it into one. So we've got kind of repapering exemptions. Right now as Bill pointed out to me. You know, what the mutual fund dealers are struggling with is the account frequency because the mutual fund dealer rules don't neatly comply with the investment dealer rules. So it's just things that we have to be aware of. Directed commissions which I thought was going to be the thing that was

never going to allow this happen by the way. They're in place for dealing reps, mutual fund dealing reps. So again, advisor retention, attraction, that's going to be a piece of the pie. Again, I'm not trying to down play the rules, we have to be careful of the rules, we have to be careful how they work within your business model. As I said I think this would be, this is going to be the meatiest option but can come with the largest rewards, depending on obviously the space. How's that?

Bill Donegan

That was great. Thanks Julie.

Julie Mansi

You like that. Okay.

Bill Donegan

Now I can't believe I'm actually going to say this, but I'm going to say it anyway. This is a regulatory development which is really exciting and positive. *[Laughing in crowd]*. I don't think I've ever heard anyone say that before but the reason why I say that is because it really does provide dealers and organizations with a lot of flexibility to change and develop their business models and you know, Julie's talked about the dual reg model and also they're going to be allowing mutual fund dealers to introduce business through investment dealers. That's a new thing as well and it's very flexible in that mutual fund dealers can choose to introduce all their business through an investment dealer or part of it and it can be very product specific. So as Kathryn said in the opening, it will allow mutual fund dealers to distribute ETFs through an introducing relationship with an investment dealer as opposed to the cumbersome omnibus arrangement which is the only option now for a mutual fund dealer. Now if an organization which has both mutual fund platforms and investment fund platforms is thinking about the introducing arrangement and the investment fund dealer isn't already approved and introduced, they will have to go through a material change notice process with IIROC to gain that ability and the thing is that organizations with affiliated dealers you know just don't have to think about moving to an introducing arrangement while rethinking how they do business. It may end up they want to pursue back office consolidation. They may see opportunities to out source both outside their corporate organization or within their corporate organization. It's a real opportunity to think about governance, to think about bringing together perhaps your compliance teams on the mutual fund side and the investment side doing complaints in a consolidated way and also thinking about your, the way your product is managed, the way legal is structured and the way the executive team is structured to bring in more efficiencies and more improvements of services for both clients and advisors. So to carry on from what Julie was saying, it's not just an opportunity to look at ok we're going to go from one entity, or from two entities to one entity or we're going to add an investment dealer platform but while doing that, it's a real opportunity to rethink the whole business and to try to find efficiencies that you weren't able to utilize before.

Julie Mansi

Or didn't have the trigger before.

Bill Donegan

Yeah, yeah and that's basically what I had to say.

Julie Mansi

That's it.

Bill Donegan

That's it.

Julie

I think we're turning it back to Kathryn.

Bill Donegan

Kathryn.

Kathryn Fuller

Alright. Thank you Julie and Bill. *[Applause]* So next up is our fund panel. Moderated by Lynn McGrade, National Leader of our Investment Management Group. She'll be joined by my Securities and Insurance Partner, Donna Spagnolo and my Tax Partner, Grace Pereira and presenting for the first time at our IMG seminars our Associate John Stanley. They're going to help you put your house in order. And they're going to talk about ESG, trends and disclosure and tax issues impacting funds among other topics. Over to you.

Lynn McGrade

Thank you Kathryn. Well, it's so nice to be here and to see and welcome you all to our house in person and I also want to welcome those on the Webex, it's great that you are able to join as well. Well we are going to do our little bit to salute Harry Styles on our panel by making pearls the theme of our panel and a special shout out to John whose is really rocking the Harry Styles pearl model and you know some of you may know that Harry has a love of pearls and since the 2019 Met Gala, he has been regularly sporting pearls as a fashion accessory. Some have said that he loves to wear pearls because they symbolize wisdom and good luck and so with this panel we hope to impart our pearls of wisdom on what's new for investment funds and also provide some practical tips on what you should be thinking of for 2023 in order to enable good luck at your firms in the year to come. But before I turn it over to my panel, I thought I would take a moment as National Leader of the group just to share some high-level themes that I feel are setting the current stage in the investment fund industry and you know they really are driving and reflecting the work that we are doing at BLG and I think it's important to step back once in a while and think about these big themes because these themes really need to drive the agenda of the industry and the leaders in the industry at this time, you people.

You will see on the next slide some lyrics inspired by Harry Styles and again we felt this was appropriate especially where it say “you know it’s just not the same as it was” and I think that is a very good lead in to some of my themes. So here are my three themes, 1. It is a time of intense regulatory change and scrutiny. 2. It’s a time of geopolitical risk and market uncertainty and 3. It’s a time of shifting investing patterns and I think as we turn it over to the panel, they will be looking at some of these more, how these are driving more speciality issues but at a big level this is what’s driving everything that this panel is going to be talking about right now.

So if we start first on it’s a time of intense regulatory change and scrutiny there’s just a tsunami of regulation impacting the investment funds industry. We felt sorry for our client, how you keep up with the tsunami and we’ve had the new prospectus forms, we had the ESG notice in January, we’ve had new regulatory initiatives still to come for us in the priorities, we saw the total cost reporting for example of coming. We’ve seen OFC desk reviews and surveys in the areas of A-1107, ESG and principal distributors and then there’s all the other areas, like privacy, accessibility, sanctions, French language rules, seniors and of course tax changes. So it really is a tsunami of regulation and I feel it’s a time to try and find a new and efficient ways to keep up.

Secondly, I mentioned geopolitical risk and market uncertainty. So many factors are impacting the markets right now and impacting risk and risk management is becoming so key at IFMs and fund managers. We are seeing inflation, high interest rate, Russia, China, political turmoil, democracy, pandemic, it’s really quite an unprecedented time a time we haven’t really did see, we didn’t realize how lucky we were frankly for many, many, years. So firms need to assess and ensure that risk management is strong at this time. It also needs to make sure that risk management is multi-dimensional and not separated. All these risks have to talk to each other. Need to stress test liquidity, need to ensure disclosure of these risks is robust and last I feel it’s a time of shifting investing patterns. Unfortunately, the large “R” word redemptions is happening. We see a lot of new product development. Move to alternatives. We’ve been very busy both in the public and private area launching alternative products, real estate, infrastructure, private income, derivatives, market mutual strategies. Also the move to ESG, and responsible investing is real. I think we did a count, Kathryn can confirm, this was only half way through the year, we worked on 70 different ESG products and responsible investing products in terms of new launches this year. It’s a very active area as fund managers are trying to take advantage of this investor demand or request for ESG strategies and new fund structures. Like the interval funds and new asset classes that we’ve seen. For example, the carbon credit funds and crypto and with all of this change of course comes new risk. In the ESGA area an example would be greenwashing risk or in the recent Goldman Sach settlement with the SEC, not just the greenwashing as an issue but a failure to adequate ESG policies and adhere to the one it did have. So I think all of these new things bring a lot of work on the compliance and risk management side as well. So I’m really happy to talk about all of this and maybe the best place to talk about it all is over drinks but for now in the meantime I’m going to pass it over to Donna who’s going to lead off our panel discussion on the topic of liquidity risk management and T+1.

Donna Spagnolo

And I’m going to start by throwing out a challenge to the guests to see if you can count the number of Harry Styles songs, the song titles I’m able to put into the next few minutes. So in September of 2020, the CSA published guidance in the form of CSA Staff

Notice 81-333. This notice was about IFMs, developing and maintaining an effective liquidity risk management framework. If you remember, we were assured that this guidance was based on existing on 81-102 rules and didn't create or modify existing requirements. Arguable but not a topic for today, that is for late night talking. I bring it up because near the beginning of lockdown, some funds experienced significant redemptions. In July of 2020, the investment funds branch sent out a survey to find out how or if Covid was impacting fund companies. As part of that survey, they asked about and reviewed the liquidity risk management for those IFMs that had experienced significant redemptions in the first half of 2020. And then they followed up with some of those firms to see how they dealt with the redemptions. Did they need medicine? They did not. The OSC found that all of the IFMs were able to manage their fund's significant redemptions without breaching any of the borrowing restrictions in 81-102 or requiring relief from those rules. This news doesn't surprise me because we've been seeing IFMs manage redemptions during hard times for decades. They're golden. But that doesn't mean that liquidity management using current rules is easy for IFMs Particularly with the coming of T+1 which requires settlement within one day of the trade. Thinking about liquidity is a sign of the times. Canada's rules are different than rules seen elsewhere in the world and there are differing views on whether Canada's rules should be remaining different or whether changes should be made. But it's time to take a fresh look, perhaps do some daydreaming at how the liquidity rules impact our funds and whether changes or exemptions need to be considered. Is it time to ask the OSC to consider new sources of liquidity? So turn the lights up, take a look at your liquidity policies and look for areas of concern to your funds during times of stress since we've learned that liquidity concerns tend to come at us unexpectedly and that's not a good time to be dealing with liquidity problems. So how many did you get? There were 6.

Lynn McGrade

There's obviously some new songs that he should be developing. Somebody heard. 8. Thank you Donna. Now John I know you have a few pearls of wisdom to share on marketing and ESG, something that's pretty topical these days so over to you.

John Stanley

Of course. Thanks Lynn. So I'm going to be talking about ESG disclosure management and marketing so much like Harry Styles, I'm going to start off in one direction. And then do something completely different. So back in January, the CSA published Staff Notice 81-334 which set out the disclosure standards for funds that involve ESG especially in their investment objectives and strategies. And since that staff notice came out, we've been diligently tracking ESG disclosures in mutual funds in their prospectuses and have been working with clients to develop those disclosures and responses to comment letters from regulators. Now one thing that we've noticed is that the OSC has cast a pretty wide net (*shocker*!) when it comes to examining ESG disclosures and requiring clarification or additional disclosures to be added. And we see this particularly with funds that have an ESG integration strategy. In other words, funds that factor ESG into their investment approach along with many other inputs but ESG isn't a key feature. Now the OSC has treated this kind of fund in the same way as funds that do have ESG as a key feature of their investment approach. Like funds that completely screen out carbon-intensive industries. And the OSC, in a lot of cases, has asked for the same level of ESG specific disclosure from integration funds as these more ESG focused funds. We've tended to push back on this because including a high level of ESG disclosure

when it's only a small portion of the investment process could actually be misleading to investors and could be greenwashing. And now also over the last year, we've also seen a number of different reviews of continuous disclosure documents and sales communications by regulators and those have happened to 32 different ESG-related funds managed by 23 different IFMs. These have also been fairly wide-ranging seeking answers on topics like MRFP disclosure on portfolio composition, whether portfolio holdings are inconsistent with ESG values and how IFMs measure and monitor that ESG performance or outcomes of their funds. Now the OSC plans to publish a summary of their findings of these reviews along with any updates to the ESG guidelines by December 2023. So a couple key takeaways from the key regulators push on the ESG disclosure.

1. It's not going away any time soon. ESG products are very popular among investors and that popularity plus the regulators mandate for investor protection have them locked in on this.
2. Regulators are looking at ESG-related disclosure in prospectuses as well as in continuous disclosure documents. The OSC in their most recent annual report for investment fund and structure product issuers indicated that they're going to be particularly focused on the summary of results of operations disclosure and MRFPs for this next round of reviews.
3. Where we see the biggest disconnect between the regulators industry is with ESG integration funds. Regulators in other countries like the SEC have taken a different approaches with them and it remains to be seen whether Canadian regulators will change their tune.

All in all, there are a lot of different styles of ESG disclosure and if things get Harry, and the regulators get involved, we are just a phone call away. But to backtrack a bit, the ESG disclosure reviews that I was talking about earlier have also included requests for copies of social media communications and sales communications regarding ESG-related funds. Of course, this is a sensitive way to prevent greenwashing which in other words is where a fund's marketing says that it does all of these wonderful things and has all of these wonderful ESG principles but it's offering documents don't actually back that up.

Social media is particularly under the microscope and the OSC has received a number of complaints about the use of social media by IFMs and their employees, mostly about insufficient disclosure and exaggerated or misleading claims. And of course there's limitations to some forms of social media advertising. You can't, for instance, provide all of the required disclaimers for the use of performance date via Tiktok dance but if you can please email. Despite all that, social media communications are still subject to the same regulatory requirements that were drafted with print advertisements. This can lead to some novel interpretations of what a sales communication actually is. In some cases, a "like" on Twitter could be considered to be a sales communication. A few things to keep in mind: 1) And this is the big one – treat all communications with investors and the public as sales communications; 2) it shouldn't take more than one click to get from an ad to a webpage that has all of the required disclosure and warnings in an easy to read format; 3) the rules around sales communications apply to both firm and employee accounts, even employees personal social media accounts when they're being used to market specific funds or to tout their performance; and lastly, firms should have policies and procedures relating to the use and monitoring of social media and employees

should be trained on those policies and procedures. Well, I've already used both of my Harry Styles jokes so back to Lynn.

Lynn McGrade

Thanks John. They were great jokes.

John Stanley

Very validating. Thanks.

Lynn McGrade

I liked them. Good effort. Donna, conflicts, conflicts are always a topic of discussion in an area of key risk for firms. What is your pearls of wisdom on this topic?

Donna Spagnolo

Alright and this is everyone's second chance to challenge. So when the IRC was originally conceived, it was very deliberately restricted for the most part to the role of providing recommendations in connection with conflict of interest matters that were brought to the attention of the IRC by the manager. By going to the IRC, the IFMs were able to keep driving but at the same time, there was an independent body keeping an eye on what was happening. The regulators could have imposed a U.S.-style system where each fund has a board of directors but they didn't. It wasn't deemed to be necessary even back then. At the time, managers thought about the potential conflicts of interest that they dealt with and documented them. They worked on procedures that included going to the IRC. More recently, as part of regulatory burden reduction, certain common exemptive relief was codified and some of that exemptive relief moved approvals or reviews from the regulators to the IRC. The point was to streamline compliance without compromising investor protection. This had no impact on some IFMs and a moderate impact on other IFMs. It wasn't quite a case of "meet me in the hallway and we'll get it done" but it was efficient. Earlier this year, the OSC sent out a questionnaire about 81-107 and asked questions about the role of the IRC. The regulators seemed to be asking about whether the role of the IRC should be changing. The timing of these questions is odd. Registrants have just finished a significant review of their conflicts of interest and have thoroughly help considered how they will avoid conflicts and how they will resolve conflicts in the best interests of investors. Compliance processes have been confirmed. The systems are in place and while client-focused reforms, exempted IFMs with public funds, the fund industry did tend to consider their conflicts regime holistically. Expanding the role of the IRC, a body put in place to guard against conflicts of interest, seems like an interesting topic at this point or is it a fine line. I would guess that the question for the people in this room is if you were asked what you wanted, what you want the IRC to do or what you don't want the IRC to do, bring your ideas into the daylight and this is the time to think about it particularly in the context of what Dave said earlier today. And how many titles? 4 yes,

Lynn McGrade

Well done. Ok, and finally, of course, there's another area very thorny tax compliance issues that are sorry there are a number of thorny tax compliance issues that we're tracking and working on with the industry right now and we just wanted to have a few comments on those so over to you Grace.

Grace Pereira

Hi, I was trying to figure out how to fit in the Harry styles references. Oh I know, I was going to say I'm not as ambitious as my colleagues so I'm sticking purely to his IMDB list so not as ambitious as Dunkirk but hopefully you'll be able to spot the movie titles.

But today I want to remind everyone of some important fact of CRS guidelines changes that will be effective in January, as well as what we are hearing financial institutions will be expecting with the upcoming fury of audits in this area. The subject of my presentation is covered off in BLG bulletin so don't worry darling, there's no need to take notes.

Next slide. Thank you. So the fact that CRS changes that we wanted to highlight are those that are applicable to client name accounts where the CRA has traditionally permitted a sharing of responsibilities between different market participants. In a client-named account scenario, the fund manager was able to see the name of the ultimate beneficial owner in its books and records. On this slide, we've outlined the client-named account relief provided in the mutual fund context. You will note with client-name accounts there's often a bifurcation of responsibilities between who is responsible for collecting the information, the due diligence obligation, and who is responsible for filing the information return, the reporting obligation. This bifurcation of responsibility results in the dealer who has more proximate relationships to the client being responsible for the due diligence and the fund manager being responsible for the reporting. However, as the CRA constantly reminds the industry, in the absence of client-name relief, all parties are responsible for both due diligence and reporting.

Next slide. The latest guidelines outlines the client-name relief in this context is only available if certain conditions are met. Those are outlined in the slide. Of note is the newest requirement that dealers are not only obligated to pass along the status of the accounts that are reportable for fact of CRS purposes but the status of all accounts to the fund manager on behalf of the funds. This change needs to be operationalized by January 1st. In short, the CRA now expects fund managers to really be the policeman of the dealers. They can no longer rely simply on the fact that they have written agreements in place with the dealers to satisfy their responsibilities.

Next slide. This slide outlines change to the guidance that caught many of us by surprise that applies to separately managed accounts for institutional account holders. In the client-name account circumstance for separately managed institutional accounts, the CRA had previously permitted custodians to be responsible for both the due diligence and reporting obligations. This again highlighted that custodians often have a more proximate relationship with the client. Effective January 1st of 2023, the CRA now expects the typical bifurcation of responsibilities for client name accounts to apply such that the investment portfolio manager is now becoming responsible for due diligence obligations and the custodian is responsible for the reporting obligations. Consistent with the change to client name accounts in the fund setting, the CRA no longer wants any two parties that are both technically deemed to maintain the same financial account

to rely on any sort of written standing agreement or declaration. Instead, they have the obligation to share the status of every account and make sure the non-reporting party is doing their own due diligence.

Next slide. This brings us to the importance of updating CRA policies and procedures particularly given the fact that we expect onsite audits of FIs to begin shortly. Back in the spring, CRA confirmed for the industry that they were currently staffing and training a regional team in Toronto and expected audits to start in late 2022 or early 2023. While we have not heard of any onsite audits, we do know the fact the CRS department has been conducting desk reviews. The CRA advised us back in the spring that the fact that an FI is selected for audit doesn't necessarily equate to it being deficient just higher risk. In determining who is higher risk and who is the lucky winner of the golden ticket, the CRA has indicated that they are looking at the data quality in the actual filings themselves. For example, the CRA will consider the number of missing 10s, error notices from the IRS and what degree that they have been resolved, circumstances where the date of birth is missing or inaccurate, unexplained unusual changes when records are compared year over year and whether the volume of reportable accounts is appropriate for the size of the financial institution.

Next slide. As discussed in our recent bulletin, winter in fact CRS audits are coming, we recommend that FIs update their policies and procedures, particularly if they reside solely in the brain of their compliance personal and also considering conducting their own internal audit to address deficiencies. The communal penalties for fact this year FI compliance can be considerable and in the case of investment funds, are borne by the funds themselves.

Next slide. The last slide simply demonstrates that compliance in increased transparency continues to be the themes on the world's stage. Consistent with the OAC guidelines, new taxpayer information reporting regimes are coming for digital platform operators and transactions in crypto assets. We expect to be drafting bulletins on these initiatives in the coming weeks. Thank you.

Kathryn Fuller

Thank you Lynn, Grace, Donna and John. Well done all. Next up, last but not least, is our registrant regulation and compliance panel, comprised of my BLG partners, Sarah Gardiner, Matt Williams and Michael Taylor as well as our AUM law colleagues who need to walk faster because they are going to do rapid fire discussions about current issues affecting registrants including disclosing outside activities, the OSC's fee rule, compliance manual updates, account opening documentation, the new derivatives rule and conflicts of interest. I'm tired just saying all that and that means you guys all have a lot on your plate so I'll leave you with this goal for the panel. Maybe we can find a place to feel good and treat registrants with kindness and let them find a place to feel good.

Matt Williams

Thank you Kathryn. It's kind of nice to see everybody here. I apologize for those I've seen on video for the last 2 years, I don't have my filters on. So we want to sort of start quickly on outside activities because that seems to be a thing that we're facing a lot of issues with obviously the amendments to 33-109 came in in June requiring updates to a variety of things not the least of which is outside activities. My main part of it is just to

kind of remind people, Hey this has to be done. We're seeing a lot of people that haven't yet started doing updates to things that you now happened in June. It's coming quickly. You have a year but I really just want to remind people that it is here, it is something that needs to be done and I'll let sort of Sarah and Jason go into a little bit more detail on what the issues are that we're seeing.

Sarah Gardiner

Yeah, so just to add to Matt's comments, although you do have until next June to file your F4 updates, that can be accelerated if there's something that changes in your F4 that otherwise triggers the requirement to update the form so if somebody moves addresses, if they have a new outside activity that is required to be reported, that automatically triggers a requirement to update the whole form and while that's relatively simple for certain individuals when there really isn't much to update if they've been register relatively recently, you may have to update to add their title and their designations but for individuals who have an exhaustive list of outside activities, it can actually be quite time sensitive to go through all of those activates and determine which ones still need to be reported under the new reportable category regime and which ones can be end dated. And the CSA do expect firms to end date those outside activities that no longer require disclosure. And so for large firms I really do recommend that you do this in stages because it is a lot of work and start now. We're working with a lot of firms already to update their F4 disclosure and we have a great team of lawyers and clerks both at BLG and AUM Law that can help with the updates.

Jason Streicher

And then I would say the priority I think is as Sarah and Matthew spoke to is to update the existing F4s that you have for your current registrants and permitted individuals but then don't lose sight of the fact that it could be the case that you know most firms compliance manuals are also now a bit out of date because they'll speak to the old rules and the sections of the compliance manual that deal with the deadlines of reporting and what the analysis of the CCOM compliance team would be as they look to first consider whether they should be allowing the outside activity, the person to take on the outside activity where there creates a conflict, client confusion and then lastly whether it's reportable or not like there's the guidance in the manuals currently do not reflect the new rules so we will need to touch up your manuals and then I'd say the third thing that needs to be done is, going forward, like I've been doing this a long time and I can tell you for 15 years that every time someone hey we have an employee with a new OA, what, Jason like give us the disclosure and it's kind on, like there's just the back and forth of a few emails. The way the OSC works now, is everything has to be in books and records and audit records. Like, I think now especially because you're not going to be reporting everything to the OSC, they in the future will be asking you but we've seen what you reported. What are all the other outside activities like that you've approved but weren't reportable? How did you check those for conflicts? How did you make sure there was no client confusion? Show us all your books and records to show us you're doing this properly. Firms really, in my view, really need to develop some kind of tracker internally so that they almost have every time the CCO's approving outside activity, they can show the thought process. We looked at conflicts. This was our conclusions. If it's a material conflict, this is why it's managing the best interests of the clients. If there's client confusion here's our analysis. Was it reportable to the OSC or regulators of category 1 through 5, here's what we concluded, you know, stamp all in a binder, get audited here

you go. And it's all, you know, so that's the kind of deeper longer term thinking I think firms need to think about. Painful for everybody but we're here to help you get through that if you want to take us up.

Matt Williams

And the last thing I'll mention on outside activities, a lot of people have actually been really good about updating the questions that say there was no response, so the old disclosure. One of the issues with doing that and then saying oh I'll deal with the outside activities later is most of the commissions will basically say if you filed a set of updates and you haven't amended your outside activities, they will deem you to basically have reviewed them and determined that they're still reportable. And so if you then go and date it later you in theory are open to late fees because you left it on there so, what I would recommend and what sort of we're seeing from an ease perspective is sort of gathering all of the updates at once and sort of filing them all at once rather than piece meal so that we don't get into those interpretation issues. The next thing I just wanted to talk about moving away from outside activities are amendments to the fee rule in Ontario that many people probably didn't pay attention to that were actually proclaimed in force yesterday. So last June they brought in amendments to the fee rule which would sort of inadvertently affects a lot of registrants daily lives, not the least of which is you know late fees when your Ontario 13-502 participation fee forms are due September 1, etc. Two or three big changes I just wanted to note to people. That December 1, deadline next year becomes November 1. I don't think a lot of people recognize that that change was coming in there so participation fee forms are now due November 1 starting in 2023 instead of December 1. Participation fees themselves have gone down. Lots of fees basically have come down across the board somewhere between 5 and 15% for the most part, which is a good thing. The other thing they are doing for the participation fee is they're moving back. Most of you probably have calendar fiscals. You probably have struggled with this concept of trying to estimate revenues through to the end in year etcetera. What they've done is reverted back to basically using a previous financial year model. So you will use 2022 estimated this year, next year you will use actual 2022's and then the previous financial year going forward. It makes things a little bit easier.

The other thing that they have done there is remove late fees for most filings including outside activities and updates to, you know, your F6 via F5 and stuff which is good. Basically the only thing that would be subject to late fees now is late filings of audited financial participation fees forms and a couple of other things. But one thing they have done and this is where a lot of firms sort of try to do a little bit of arbitrage. They have a clause in there that says if you were so a lot of people were still waiting, were sort of waiting to update outside activities to wait until these wait fees when away, there is a transition clause that says "If you were subject to a late fee under the old rule, you're still subject to that late fee". Curious whether they'll actually enforce that or not but that's the way they do. So you may want to start looking at updating outside activities before if you are waiting to try and you know arbitrage the disappearance of the late fees.

The third thing we'll move on to is compliance manual updates kind of in general. And, you know, obviously in addition to what Jason said on outside activities, a lot of the compliance manuals we're seeing right now haven't been updated for client focus reforms. We've been doing, for example, summer – often times in the summer, early fall we do a lot of our annual AM, our 2 year AML reviews for clients and thing like that

where we look at compliance manuals and see – a could of things we're commonly seeing, the June 2021 amendments to AML often haven't been incorporated into your compliance manuals. In addition to that, a lot of people paid attention, I think, on the client focus forums to update their manuals for the conflict of interest rules that came in for last June. Most of the kind of everything else part of it that came in last December I think people got lazy on. So we're seeing a lot of compliance manuals that don't have those elements built in. Now is the time to do that. There's sort of a lot of things in the last year and a half that have come in between, you know, conflicts of the interest, AML changes, client focus reforms, changes to 33-109 reporting regimes, etcetera. Now is the time sort of January project to look at your compliance manual kind of broadly and make those changes.

Sarah Gardiner

Yeah and in addition to the things that Matt talked about for your policies and procedures, I would believe strongly urge you to review the OSC's latest annual summary report for dealer's, advisors and investment fund managers because that was the one that was released in October. There's actually a really, a lot of good guidance in there about policies and procedures. Pretty much with respect to every common deficiency that they set out. In that stuff notice they have accompanying bullet points on policies and procedures. So things like use of prospective exemptions. So if you're distributing securities under prospective exemptions, you really should have policies and procedures regarding documentation and collection of information to demonstrate how you're meeting the conditions of the exemption. There's a lot of good guidance in there also, specifically for EMD's. I mean Matt touched on KYP's, stability, all the things related to client focus reforms, specifically for exempt market dealers. It's important to think about having policies and procedures about internal concentration thresholds and also product due diligence having a robust policy regarding product review.

Jason Streicher

And if we're there, one of the other things that came out in that latest policy staff notice, and hopefully, Matt, if you were to speak, is the limitation of liability.

Matt Williams

I bury my head in the sand on that one.

Jason Streicher

Ah, which I know Matt is dealing with as well. And they said this before but now they were a bit more, you know, forceful about it saying that okay because, you know, registrants in most circumstances have a best interest duty towards their clients that if their, for example, investment management agreement has a clause in it that kind of tries to narrow the scope of what they'll be liable for. It doesn't say you can't do that in all circumstances. You have to very careful of the kind of limitation of liability for non-clients. The specific example they use was a clause that said, you know, we'll only be liable if the client can show that there has been a breach of securities laws. And the reasoning of OSC staff was that well you're putting the onus on a client to prove a very specific, you know, we'll only be liable for this, well the client has to then maybe go to

court and prove that and that may be the only thing you should be liable for. There might be other reasons why you might be liable to the client even if they don't prove a specific breach of securities laws and why in a contract should you put that, you know, try to say well that's all I'll be liable for and force them to really then, you know, have a court case against you. So it's clear that some types of limitation of liability clauses aren't acceptable but as I speak to our clients and I look at different, very different IMA's in certain cases, it's kind of, even for clients it's kind of tricky to maneuver which one, what, you know, what can be acceptable and what isn't. It's an open, like there's a bit of open debate about it right now but I think you should be looking at your, the point is look at your IMA's. If you do see some limitation of liability language in there maybe consider against the guidance what you think about it and speak to counsel if you might have to think about removing it. This is something for sure your next regulatory audit the regulators will look at and what they've said is also if you do need to remove the language, what they've suggested is you also need to tell your clients that you've removed, you've changed the language and that, you know, that you've given them the heads up. You wouldn't in the future action, you know, complaint that they might have with you to enforce that language. So the client is, that's the other things concerned to our clients is that oh I might make a change, I don't necessarily want to write a letter telling all my clients out of the blue I've, here's some amendments I've made to your contract because it might be a bit awkward to explain to clients why you're doing that, but we're helping clients navigate this issue so feel free to contact us about it.

Michael Taylor

I think everyone was wondering if I was going to say anything on it [*laughter*]. Don't worry, I'm a master at doing that. So just on in terms of refresh of your compliance manuals, cybersecurity, cybersecurity incident planning I think should be top of mind. Lynn said, you know, risks that people face in the industry I think that is a significant risk. It's also on the CSA'S radar so good time to use this as a refresh of that to make sure you have a plan and process in place. Related to that is remote working obviously now very much prominent. You want to have a remote working supervision policy in place. You don't have your reps, you know, going into Starbucks with their Cranberry Latte's case sitting there with client documents. You want to make sure that their following the rules that you've put in place. And then OSC also sent a blast out I think in September to CCOs and UDPs about new virtual location, business locations on NRD that you can open up.

Sarah Gardiner

Sorry [*laughing*] I was thinking about something else there. So just one of the most important things I think in terms of compliance shifts is to update your account documentation of client refocused reform. We know the CSA has done the conflicts of interest sweep. Hopefully those are done now and I think next on the radar will be more general client focus reform sweeps. So make sure you update you KYC forms, your KYC update forms and your IMAs. You know, make sure you've got trusted contact person information, everything you're already aware really just to client focus reforms and also look at your IMAs, again as Jason talked about the limitation of liability clauses, I think that's going to be a key focus of the regulators as well.

Michael Taylor

So just briefly on derivative roles, I think we've all been waiting for this for awhile now. I think we've talked about this maybe for the past 10 years at our seminars but the OTC business conduct rule is finally going to go into effect next year, Q1 or Q2 with a one year transition. So that should be on, you know, everyone's New Years resolution list to get ahead of that and put in place policies procedures documentations, any new registrations needed or, I guess not registrations, registration rule, we still don't know status yet so it's really the business conducts rule should be a focus. Trade reporting very dull but there is derivative trade reporting sort of harmonization going on internationally. CSA recently released some guidance. Their rule is going into effect, I think it's going to be next year. CFDCs putting their rules in place as of December. A bit of a mismatch so some of that recent guidance was focused on, you know, harmonization or attempting to ease some of the burden for firms.

So turning to our last topic here on conflicts of interest, everyone's favourite topic - is the bar open yet, no, [*laughter*] unfortunate. So I just wanted to highlight the couple, maybe head scratching deficiencies that we've seen from recent OSC compliance reviews. One on referral arrangements, I mean, always referral arrangements is a focus of these reviews. One that was interesting we've seen is a scenario where a registrant firm collects fees on behalf of the non-registered referring entity which provides services to the client. So administrative convenience once he has paid, registrant pays some of that for services provided by the non-registered firm, OSC has been questioning how does a registrant satisfy itself that the fees charged are reasonable and this isn't even for a party relationships and that this service is provided by that non-registrant or, you know, professional. So interesting comment there. Another one that is sort of along the lines of some of these things with the limitation of liability clause I would say, conflicts around standard fee schedules. So OSC's been pointing out that if a firm has a standard fee schedule but certain clients can negotiate that fee schedule and the fees, the CSA or OSC views that as a material conflict of interest which is to me I don't fully understand because that to me is a commercial business relationship in negotiation, but there you have it so I would, you know, strongly push back on that deficiency if you receive it.

Jason Streicher

Well that's some, yeah I mean some specific things I've seen too on the, you know, in being involved in the conflicts sweep. One I've seen recently is, and I think a lot of portfolio managers looking to the future are trying to broaden their service offering and sometimes with affiliated companies, you know, as a PMI, your discretion and portfolio manager, but I an affiliate that can provide you tax, accounting services, other services. I've seen, it was in Quebec, the AMF came back and said well if you're referring a client to one of your affiliates for tax or accounting work, how do you know that's in the best interest of your client and that your affiliate is providing them the professional services that maybe they should be going elsewhere. Why are they going to your affiliate for those services and are you viewing that as a conflict and if you're not, well you should and how are you managing the best interest of your client? I've seen that one which was a bit surprising. And also I recently, the conflict about, again, how you incent, how a firm's incentivising its members, its individual registrants if, you know, for example, you're paying the individual registrants for new business they bring into the firm which again shouldn't be. I think people know that's how the world works, people who bring in clients and make money tend to get paid more than people who don't but the OSC's given an indication that can be a material conflict of interest. Like clients should be aware that the individual their facing might be more highly remunerated because they

bring you in as business so, you know, it seems obvious but the OSC has taken issue with it if it's a formalized plan, incentive plan to individuals.

Kathryn Fuller

Any final comments I'll ask from the two of you?

Sarah Gardiner

I think we'll skip it, I think [*laughter*].

Kathryn Fuller

Alright. Well then thank you very much to Sarah, Matt, Jason and Michael [*clapping*]. I think they made a wise choice. Those pearls of wisdom right there to stop us now. We certainly had a lot of information today about enforcement in the USRO, fund issues and registrant challenges as well as all the issues we didn't talk about. I think Lynn mentioned some like French translation requirements, privacy law changes, sanctions, but also, you know, I didn't hear her talk about unclaimed property in New Brunswick. That's coming into effect if you don't think you have enough on your plates. And there are changes in Quebec on their guidance too. So thank you everyone for joining us this afternoon and for those of us who didn't write down all those pearls of wisdom we will be sending out an email with the slides and recordings so you can watch this over and over again if you'd like. So with that, come on BLG clients and friends we want to say goodnight to you so please stay for our reception and some late night talking. And for those of you who have other responsibilities, maybe we can make it just an early evening conversation. Thank you. [*clapping*]

By

David Di Paolo, Julie Mansi, Lynn McGrade, Grace Pereira, Donna Spagnolo, Sarah Gardiner, Michael Taylor, Matthew P. Williams

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