

ALBERTA SECURITIES COMMISSION

APPROVAL ORDER

Citation: Re MFDA Investor Protection Corporation, 2015 ABASC 654 Date: 20150430

MFDA Investor Protection Corporation and Mutual Fund Dealers Association of Canada/ Association canadienne des courtiers de fonds mutuels

Background

1. Pursuant to section 6(2) of the *Alberta Securities Commission Rules (General)* (the **Rules**), every mutual fund dealer must participate in and contribute to a compensation fund or contingency trust fund approved by the Executive Director of the Alberta Securities Commission (the **Commission**) and established by, among others, a recognized self-regulatory organization (**SRO**).
2. The Executive Director issued an order dated 17 May 2005, as amended on 18 May 2006 (the **Previous Order**), approving the MFDA Investor Protection Corporation (**MFDA IPC**) as a compensation fund for customers of mutual fund dealers that are members of the Mutual Fund Dealers Association of Canada/ Association canadienne des courtiers de fonds mutuels (the **MFDA**) pursuant to section 6(1)(b)(i) of the Rules.
3. The MFDA IPC is established by the MFDA.
4. The MFDA is the subject of a 6 November 2014 order (the **MFDA Recognition**) of the Commission recognizing the MFDA as a SRO under section 64 of the *Securities Act* (Alberta) (the **Act**).
5. The terms and conditions of the MFDA Recognition refer to the MFDA IPC.
6. Members of the MFDA must contribute to the MFDA IPC by way of assessments pursuant to the MFDA requirements.
7. The MFDA IPC provides protection to eligible customers of the MFDA members on a discretionary basis to prescribed limits if securities, cash and other property held by any such member are unavailable as a result of the member's insolvency.
8. The MDFA IPC commenced coverage of customer accounts on 1 July 2005.
9. The MDFA IPC entered into an agreement with the MFDA pursuant to which the MFDA IPC will receive all information it deems necessary to ensure that the MFDA IPC can fulfil its mandate and manage risks to the public and MFDA IPC assets on a reasonable basis.

10. The MFDA IPC filed an application with the Executive Director requesting a variation to the Previous Order to move the definition of the term “Public Director” to the MFDA IPC By-law #1 and to make other housekeeping changes.
11. The Executive Director considers it appropriate to revise the terms and conditions of the approval of the MFDA IPC to delete the definition of “Public Director”, to update the requirements on MFDA IPC and to make other housekeeping changes.

Representations

12. The MFDA IPC and the MFDA have agreed to the terms and conditions set out in Schedule “A” (the **Revised Terms and Conditions**).
13. The Revised Terms and Conditions may be varied or waived by the Executive Director.
14. The MFDA and the MFDA IPC have made certain representations and undertakings to the Commission.

Order

15. The Executive Director, considering that it would not be prejudicial to the public interest, orders:
 - (a) the approval of the MFDA IPC as a compensation fund pursuant to section 6(1)(b)(i) of the Rules, subject to the Revised Terms and Conditions; and
 - (b) that the Previous Order is revoked pursuant to section 214(1.1) of the Act.

This order takes effect on 30 April 2015.

“original signed by”

David C. Linder, QC
Executive Director
Alberta Securities Commission

SCHEDULE A

Terms and Conditions

1. Authority and Purpose

The MFDA IPC has, and must continue to have, the appropriate legal authority to carry out its mandate (the **MFDA IPC Mandate**) of providing compensation for losses of property for which coverage from the MFDA IPC is available (**Property Covered**) to customers eligible for coverage from the MFDA IPC (**Eligible Customers**), in accordance with established by-laws, policies, or other similar instruments of the MFDA IPC (collectively, **Policies**).

2. Corporate Governance

- (a) The board of directors for the MFDA IPC (the **Board of Directors**) must be selected in a fair and reasonable manner, and the Board of Directors must fairly represent the size, diversity, nature and regional distribution of the businesses of MFDA members and the interests of Eligible Customers, in order to provide a proper balance between the differing interests among MFDA members and Eligible Customers.
- (b) The Board of Directors must be composed of an odd number of directors, the majority of which must be “Public Directors” as defined in the MFDA IPC’s By-law Number 1 (**Public Directors**).
- (c) The MFDA IPC's governance structure must provide for:
 - (i) fair and meaningful representation on the Board of Directors and any committees of the Board of Directors, having regard to the differing interests among MFDA members and Eligible Customers;
 - (ii) appropriate representation of persons independent of the MFDA or any of its members or of any affiliated or associated company of such member on MFDA IPC committees and on any executive committee or similar body;
 - (iii) appropriate qualification, remuneration, conflict of interest provisions and limitation of liability and indemnification protections for directors and officers and employees of the MFDA IPC generally; and
 - (iv) an audit committee, the majority of which will be made up of directors that are Public Directors.
- (d) The Board of Directors must ensure that a public accountant is appointed and conducts an audit engagement of the MFDA IPC’s annual financial statements in accordance with applicable legislation.

3. Funding and Maintenance of MFDA IPC

- (a) The MFDA IPC must have a fair, transparent and appropriate process for setting fees, levies and assessments (collectively **Assessments**) for each MFDA member's contribution. Assessments must:
 - (i) be allocated on an equitable basis among MFDA members and may be based on the amount of risk an MFDA member exposes the assets of the MFDA IPC to; and
 - (ii) balance the need for the MFDA IPC to have sufficient revenues to satisfy claims in the event of an insolvency of an MFDA member and to have sufficient financial resources to satisfy its operations costs against the goal that there be no unreasonable financial barriers to becoming a member of the MFDA.
- (b) The MFDA IPC must make all necessary arrangements for the notification to MFDA members of Assessments and the collection of Assessments, either directly from MFDA members or indirectly through the MFDA.
- (c) The Board of Directors must determine the adequate level of assets for the Fund. The Board of Directors must conduct an annual review, on a calendar year basis, of the adequacy of the level of assets, Assessment amounts and Assessment methodology and must ensure, in its opinion, that the level of assets for the Fund remains adequate to cover Eligible Customer coverage obligations under section 4.
- (d) Any increases in the Fund size or changes to Assessments or Assessment methodology must be determined by the Board of Directors after consultation with the MFDA. If the MFDA does not agree with the MFDA IPC's proposed changes, the MFDA IPC must immediately report such disagreement to the Commission. However, this will not prevent the MFDA IPC from imposing Assessments in order to permit the MFDA IPC to meet its obligations to its lenders or to satisfy claims incurred from Eligible Customers of MFDA members that exceed the assets available to the MFDA IPC.
- (e) Moneys in the Fund must be invested in accordance with investment policies approved by the Board of Directors (**Investment Policies**). The Board of Directors will be responsible for regular monitoring of the MFDA IPC's investments. The general parameters of the Investment Policies must include safety of principal and a reasonable income while at the same time ensuring that sufficient liquid funds are available at any time to pay potential claims from Eligible Customers. All moneys and securities must be held by an acceptable securities location as defined by the MFDA or IIROC.
- (f) The MFDA IPC must maintain an appropriate accounting system, including a system of internal controls, for maintaining MFDA IPC assets.

4. Customer Protection

- (a) The MFDA IPC must provide, on a discretionary basis, fair and adequate coverage for all Eligible Customers, for losses of Property Covered resulting from the insolvency of an MFDA member.
- (b) The MFDA IPC must maintain policies relating to customer coverage (**Coverage Policies**) including, but not limited to:
 - (i) a definition of eligible customer and ineligible customer;
 - (ii) types of property covered and amount of coverage per Eligible Customer account;
 - (iii) a process for the review of claims that will be based on fairness to Eligible Customers, expediency and cost efficiency and that will ensure that decisions by the MFDA IPC will be objective and consistent with prior decisions according to the Coverage Policies; and
 - (iv) a fair and reasonable internal appeals or review process whereby customer claims that are not accepted for payment by the initial reviewer(s) must be reconsidered by members of the Board of Directors, either individually or in a sub-committee, who were not involved in the initial decision under review.
- (c) The MFDA IPC must offer coverage in a jurisdiction only if the requirements for risk management, prudent business conduct and practices, and firm solvency that apply in that jurisdiction are not materially different from the requirements established by the MFDA IPC and/or the MFDA and the MFDA and the MFDA IPC are able to monitor and enforce their requirements in this regard.
- (d) The Coverage Policies must not prevent a customer from taking legal action against the MFDA IPC in a court of competent jurisdiction in Canada. The MFDA IPC must not contest the jurisdiction of such a court to consider a claim where the claimant has exhausted the MFDA IPC's internal appeals or review process.
- (e) The MFDA IPC must adequately inform customers of MFDA members, either directly or indirectly through the MFDA, of the principles and policies on the basis of which coverage will be available, including, but not limited to, the process for making a claim and the maximum coverage available per customer account.
- (f) In the event of an insolvency of an MFDA member, the MFDA IPC will respond quickly and decisively, in accordance with its Coverage Policies, in assessing and paying claims.

5. Financial and Operational Viability

The MFDA IPC must maintain adequate financial and operational resources, including adequate staff resources or external professional advisers, to permit the MFDA IPC to exercise its rights and perform its functions including, but not limited to,

- (i) assessing and managing risks to the public and to MFDA IPC assets;
- (ii) administering any insolvencies, including the processing of customer claims;
- (iii) setting and collecting Assessments, including conducting reviews of the Assessment methodology;
- (iv) maintaining an adequate Fund size, including assessing the Fund size on a regular basis; and
- (v) day-to-day administrative work, including required reporting to the Commission.

6. Risk Management

- (a) The MFDA IPC must have policies and procedures, including a process to identify and request all necessary information from the MFDA, in order for the MFDA IPC to:
 - (i) fulfill the MFDA IPC Mandate and manage risks to the public and to MFDA IPC assets;
 - (ii) assess whether the prudential standards and operations of the MFDA are appropriate for the coverage provided and the risks incurred by the MFDA IPC; and
 - (iii) identify and deal with MFDA members that may be in financial difficulty.
- (b) While the MFDA IPC may rely on the MFDA to conduct reviews of MFDA members for MFDA IPC purposes, the MFDA IPC must reserve the right to conduct reviews of MFDA members in particular situations where the MFDA IPC has concerns about the integrity of the Fund or possible claims.
- (c) The MFDA IPC must, at least annually, conduct a risk management review, which includes a review of how the MFDA IPC identified, evaluated and resolved risk management issues, including the different risks posed by different types of products. The review will also assess the appropriateness of offering coverage for all Property Covered and assess the need for additional risk management tools.

7. Reporting to the Commission

The MFDA IPC must comply with the reporting requirements set out in Appendix A, as amended from time to time by the Commission or its staff in writing. The MFDA IPC must also promptly provide the Commission with other reports, documents and information as the Commission or its staff may request.

8. Policies

- (a) The MFDA IPC must establish and maintain Policies that:
 - (i) are in the public interest; and
 - (ii) are necessary or appropriate to govern all aspects of its business and affairs.
- (b) More specifically, the Policies:
 - (i) will be designed to ensure:
 - (A) reasonable funding of the MFDA IPC through Assessments to MFDA members, without creating unreasonable barriers to the mutual fund industry and without compromising investor protection;
 - (B) the maintenance of a reasonable level of MFDA IPC assets to afford protection for Eligible Customers of MFDA members; and
 - (C) its business is conducted in an orderly manner so as to afford protection to Eligible Customers; and
 - (ii) will not:
 - (A) be contrary to securities legislation;
 - (B) permit unreasonable discrimination among customers of MFDA members and among MFDA members; or
 - (C) impose any burden on competition that is not necessary or appropriate in furtherance of securities legislation.

9. Agreement between the MFDA IPC and the MFDA

The MFDA IPC must maintain the services agreement signed by the MFDA and MFDA IPC, as the same may be amended or replaced from time to time (the **Services Agreement**), and pursuant to which the MFDA IPC will, among other things, receive all information it deems necessary to ensure that the MFDA IPC can fulfill its mandate and manage risks to the public and to the MFDA IPC assets on a reasonable basis. Any amendment to the Services Agreement must receive the prior approval of the Commission or the Executive Director, as applicable, prior to taking effect.

10. Co-Operation with the MFDA

The MFDA IPC and the MFDA will co-operate and provide reasonable assistance to each other when an MFDA member is in or is approaching financial difficulty, or when either the MFDA IPC or the MFDA is administering an insolvency.

11. Collection of Information

Subject to applicable law, the MFDA IPC must collect, use and disclose personal information only to the extent reasonably necessary to carry out the MFDA IPC mandate.

Appendix A

Reporting to the Commission

1. Prior Approvals

The MFDA IPC must file for prior approval with the Commission changes to any of the following:

- (a) By-laws;
- (b) Coverage Policies; and
- (c) Policies.

If required such changes will be published for a 30-day or other comment period.

2. Prior Notification

- (a) The MFDA IPC must provide to the Commission at least 60 days prior notice prior to:
 - (i) implementing any changes to its method of assessing MFDA members; or
 - (ii) implementing any changes to its Investment Policies.
- (b) In emergency situations where, in the opinion of the MFDA IPC, 60 days prior notice is considered unreasonable, the MFDA IPC will inform the Commission with as much advance notice as possible in the circumstances. Such notice will include an explanation of why the 60-day period is considered to be unreasonable.

3. Ad Hoc Reporting

- (a) The MFDA IPC must immediately notify the Commission upon becoming aware of:
 - (i) any conditions which in the opinion of the MFDA IPC could give rise to payments being made out of the MFDA IPC, including any conditions which have contributed substantially to or, if appropriate corrective action is not taken, could reasonably be expected to:
 - (A) inhibit an MFDA member from promptly completing securities transactions, promptly segregating customers' property as required or promptly discharging its responsibilities to customers, other MFDA members or other creditors,
 - (B) result in material financial loss,

- (C) result in material misstatements of an MFDA member's financial statements, or
 - (D) result in violations of the minimum record requirements of the MFDA to an extent that could reasonably be expected to result in the conditions described in paragraphs (A), (B) or (C) above;
 - (ii) misconduct or apparent misconduct by an MFDA member or its registered or approved employees and others where customers, creditors, MFDA members, or the MFDA IPC may reasonably be expected to suffer serious damage as a consequence thereof, including where the solvency of an MFDA member is at risk, fraud is alleged or there is a concern of deficiencies in supervision or internal controls; and
 - (iii) the withdrawal or expulsion of any MFDA member from the MFDA.
- (b) The MFDA IPC must immediately report to the Commission any actual or potential material adverse change in the level of the MFDA IPC's assets, together with the MFDA IPC's plan to deal with the situation.
- (c) The MFDA IPC must provide to the Commission a report detailing any action taken with respect to an MFDA member in relation to the member's insolvency. The report must describe the circumstances of the insolvency, including a summary of the actions taken by the MFDA member, the MFDA and the MFDA IPC and any committee or person acting on behalf of such parties.

4. Annual Reporting

- (a) The MFDA IPC must file with the Commission its annual audited financial statements prepared in accordance with Canadian accounting standards for not-for-profit organizations, together with the report of the public accountant, within 90 days after the end of each fiscal year. Prior to the filing, the MFDA IPC must notify the Commission immediately if the public accountant is of the view that a qualified or modified opinion should be issued on the annual audited financial statements.
- (b) The MFDA IPC must provide the following information to the Commission, within 90 days after the end of each fiscal year:
 - (i) description of any changes to the composition of the Board of Directors in the previous fiscal year, including the names and terms of any incoming directors, the names of any outgoing directors, and whether any incoming directors are Public Directors as defined in the MFDA IPC's By-law Number 1;
 - (ii) any suggestions that the MFDA IPC has made to the MFDA in the previous fiscal year regarding the MFDA making new rules or amending, revoking in whole or in part, or suspending existing rules of the MFDA, and the MFDA's response to those suggestions; and

- (iii) where the MFDA IPC has requested the MFDA to take certain actions about MFDA members that are in financial difficulty, details about the MFDA IPC's request and whether the MFDA IPC is satisfied with the MFDA's response.
- (c) The MFDA IPC must provide a written report to the Commission and meet with Commission staff at least once a year to report on the MFDA IPC's operations and activities, including but not limited to:
- (i) the Board of Director's annual review of the adequacy of the level of assets in the Fund, Assessment amounts, and Assessment methodology;
 - (ii) MFDA IPC resources, including whether the MFDA IPC is fully staffed;
 - (iii) MFDA member insolvencies and any resulting customer claims;
 - (iv) the risk management review conducted pursuant to section 6(c) of Schedule A of this Order; and
 - (v) the extent and results of any MFDA member reviews conducted by the MFDA IPC.