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MFDA Bulletin

Membership Information

For Distribution to Relevant Parties within your Firm

2018 Compliance and Member Education Priorities

1. COMPLIANCE

This section of the Bulletin highlights MFDA compliance issues and priorities that Members should be aware of in focusing their supervisory activities. The examination process for 2018 has not substantially changed. However, Members are reminded that MFDA examiners require access to Member books and records to complete an examination. This includes access to the Member's electronic records in the firm's back-office system and may also include access to electronic communications between Approved Persons and clients, including e-mails.

1.1. Conflicts of Interest

On December 15, 2016, the MFDA issued [a report](#) summarizing the results of its review of all Member compensation and incentive programs. The objectives of the MFDA review were to gain a more detailed understanding of Member compensation and incentive programs, assess compliance with certain sections of National Instrument 81-105 (Mutual Fund Sales Practices) and identify any compensation or incentive practices that might lead to mis-selling or unsuitable advice. MFDA will continue to review Member compensation and incentive practices, including practices that may originate from sales locations or affiliated/related organizations. Further, we expect Members to have policies and procedures and to maintain records relating to Approved Persons' receipt of promotional items from mutual fund companies or participation in promotional activities that are funded by mutual fund companies.

1.2. Approved Person Targeted Review

The [Client Research Report](#) issued on May 23, 2017 provided the MFDA with detailed client information relating to Approved Persons' books of business. MFDA data, including data obtained from the Client Research Report, will be used to review a sample of Approved Persons for issues such as concentration in high risk investments and suitability for senior investors. The

Approved Person Targeted Review will be conducted separately from the normal course examination process.

1.3. Lower Management Expense Ratio (“MER”) Series Funds

There have been several settlement agreements between provincial securities regulators and registrants relating to firms not having sufficient controls to advise clients when they become eligible for a lower MER series of the same mutual fund. We expect Members and Approved Persons to understand the products they recommend, including understanding circumstances where clients may be eligible for a lower MER series of the same fund. This expectation applies to both proprietary and third-party funds. Members should have policies to:

- require Approved Persons to advise their clients and make appropriate recommendations when their clients become eligible for a lower MER series of the same fund; and
- supervise trading and client accounts to identify instances where clients are eligible for a lower MER series and determine if clients have received appropriate recommendations.

Several mutual fund companies have implemented programs to automatically provide investors with a lower MER upon eligibility. However, not all mutual funds have implemented an automatic feature. Therefore, where there is no automatic feature, Members are expected to implement reasonable supervisory procedures to determine if clients meet the lower MER eligibility criteria. Supervisory procedures could include a review of trades over a certain amount or a regular review of accounts with a certain amount invested with the same fund company. In determining the trade and account supervisory thresholds, Members need to consider the eligibility criteria for the particular funds they offer. In some instances, the eligibility criteria are based on combining accounts within the same family or household. Accordingly, Member procedures should address the need for Approved Persons to properly link accounts in these circumstances.

In our examinations, we will be assessing whether Members have implemented appropriate policies and controls in respect of lower MER series funds.

1.4. Cybersecurity

In 2017, MFDA retained a consultant and issued a questionnaire to all Members to understand their cybersecurity practices. Each Member subsequently received an individual consultant’s report that identified areas for improvement and provided recommendations where applicable. In 2018, MFDA will focus efforts on Members who may require further guidance and assistance (including smaller Members with limited resources) to strengthen their cybersecurity practices.

1.5. Client Relationship Model Phase 2 (“CRM2”)

In 2017 MFDA began reviewing Member compliance with CRM2 requirements and performed a sweep of integrated Member Charges and Compensation Reports. MFDA will continue its examination of Member compliance with CRM2 requirements and will work with other regulators and stakeholders to further the discussion on expanding cost reporting.

1.6. Use of New Technology

Increasingly Members have been implementing new technology to offer new products (e.g. exchange traded funds) and services (e.g. electronic reporting, signatures, onboarding, advisory services, etc.) to clients. Members routinely meet with Compliance staff to keep us apprised of the proposed operational changes and obtain feedback relating to potential regulatory concerns. We support Members in their goals of achieving increased efficiencies and expanding investor choice while, at the same time, meeting regulatory requirements. Accordingly, we encourage Members to speak with us before implementing new technology that may have a significant impact on their operations or services offered to clients.

2. MEMBER EDUCATION

The Member Education Department will continue to provide education and training assistance to Members by participating in Member and industry events. In addition to assisting with MFDA educational initiatives, the Member Education Department will be involved in the research project outlined below.

2.1. Client Research Project Update

The MFDA gathers information regarding its Members' business and activities on an ongoing basis in order to effectively achieve its regulatory mandate of protecting investors. The data obtained from the first Client Research Project conducted by the MFDA provided us with valuable information and insight into Members' business, their Approved Persons and their clients. In 2018, to gain additional insight and to support our ongoing compliance efforts, we will be exploring whether to issue another data request to update the information received in 2016 and to obtain additional data derived from the new performance and charges and compensation reports.