

Chapter 13

SRO Notices and Disciplinary Proceedings

13.1.1 Notice of Request for Comments – Amendments to IDA Regulation 200.1(H) regarding Confirmations for Externally Managed Account Transactions

INVESTMENT DEALERS ASSOCIATION OF CANADA

REGULATION 200.1(H) – CONFIRMATION FOR EXTERNALLY MANAGED ACCOUNT TRANSACTIONS

NOTICE OF REQUEST FOR COMMENTS

I OVERVIEW

A Current Rules

Regulation 200.1(h) requires that Members issue a confirmation of each trade in securities or commodity futures in a customer account. Regulation 200.1(h) also lists the information that must be included on the confirmation. The Regulation provides an exemption from doing so for accounts managed by external portfolio managers provided that the customer consents and a confirmation is sent to the external portfolio manager (sub-paragraph (iv)(a) of Regulation 200.1). An exemption is also provided for accounts managed by internal portfolio managers of the Member provided that the customer consents, the account is not charged a commission or fees based on the volume or value of transactions and the monthly statement contains certain information that would have been contained in a confirmation (sub-paragraph (iv)(b) of Regulation 200.1).

B The Issue

Many external portfolio managers do not wish to receive confirmations as currently required. Clients would have sufficient disclosure and adequate protection if clients are provided with enhanced monthly statements that include some of the information that would have been contained in a confirmation.

C Objective

The objective of the amendment is to relieve external portfolio managers from receiving unnecessary confirmations and providing Members with the option of instead providing clients with monthly statements enhanced to include all the items of trade information that normally appear on a confirmation but not on a monthly statement, although for some such items the member may simply disclose that the information is available on request.

D Effect of Proposed Rules

The proposed rule change will reduce the cost of administration of managed accounts by eliminating the cost of sending out confirmations to external portfolio managers. In addition, the proposal would result in treating portfolio managers carrying out the same function in the same manner regardless of whether they work for the Member firm or are sub-advisers.

II DETAILED ANALYSIS

A Present Rules, Relevant History and Proposed Regulation Amendment

The current provision regarding confirmations for managed accounts was passed by the Board of Directors in 2003 and implemented in 2004. It revised earlier amendments to the Regulation that were made in 1997. The 1997 amendments responded to complaints from managed account holders that, having signed the management of their portfolios over to others, they had no use for and did not want to receive a separate confirmation of each trade, and would be satisfied with monthly statements showing all transactions.

The 1997 provision, as originally passed by the Board of Directors, did not restrict the exemption to externally managed accounts. That restriction was included at the insistence of those Canadian Securities Administrators (CSA) whose approval of IDA By-laws and Regulations is required.

Members that offered managed accounts internally continued to report that some clients complained about receiving separate confirmations of every trade for their accounts.

In May 2003 all members of the CSA, except the Prince Edward Island Securities Office, to which application was not made, granted to an applicant Member an exemption from providing confirmations to managed account customers in an internally managed program, subject to certain conditions. The Member sought an exemption from Regulation 200.1(h) for the accounts in the program. Consequently, the 2003 amendment provided an exemption to Members offering internally managed accounts, subject to the conditions already included in the exemption for externally managed accounts. These conditions are:

1. That the client must consent to not receive confirmations and must be able to terminate that consent by notice in writing. The firm must resume sending confirmation on receipt of the notice for trades the following day.
2. The provision of a confirmation is not required under any applicable securities law, regulation or policy of the jurisdiction in which the client resides or the Member has obtained an exemption from any such law, regulation or policy by the responsible securities regulatory authority.
3. The Member sends a monthly statement to the client.

The fundamental difference in the conditions for internal versus external accounts is that where the Member manages the account, the monthly statements must contain all of the information required to be contained in a confirmation except:

1. The day and the stock exchange or commodity futures exchange upon which the trade took place;
2. The fee or other charge, if any, levied by a securities regulatory authority in connection with the trade;
3. The name of the salesman, if any, in the transaction;
4. The name of the dealer, if any, used by the Member as its agent to effect the trade; and,
5. If acting as agent in a trade upon a stock exchange, the name of the person or company from or to or through whom the security was bought or sold.

This condition was in lieu of the requirement for externally managed accounts that a trade confirmation be sent to the external manager of the account.

The IDA has recently become aware of securities commissions granting relief applications to Member firms from the securities legislation requirement to send confirmations. The firms received relief in reliance on sub-paragraph (iv)(b). Specifically, although the firm was offering externally managed accounts, rather than having to send confirmations to the external portfolio manager, the firm was permitted to send monthly statements which included information usually contained in a confirmation. Another Member, BMO Nesbitt Burns, has recently received relief from the securities commissions and is now requesting permission from the IDA to also rely on sub-paragraph (iv)(b) for externally managed accounts.

The Association is of the view that it is appropriate for clients to receive a monthly account statement that includes the information required by paragraph (iv)(b) rather than a trade confirmation for each individual trade or a trade confirmation being sent to a sub-adviser for each trade.

The amendment will provide an alternative for Members who offer externally managed accounts from the present requirement that a trade confirmation be sent to the manager of the account. Members can choose instead for these accounts to comply with the exemption currently available only for internally managed accounts.

An amendment has also been made to sub-paragraph (iv)(a)(A) simply to clarify the language and maintain consistency with the language throughout sub-paragraphs (iv)(a) and (b).

In conjunction with this submission to the Board for a rule amendment, in order to assist BMO Nesbitt Burns with its relief application, a draft Resolution of the Board of Directors is being submitted. This Resolution is pursuant to By-law 17.15 and is intended to grant an exemption from the trade confirmation requirements contained in Regulation 200.1(h); specifically the requirements in sub-paragraph (iv)(a).

B Issues and Alternatives Considered

No alternatives were considered.

C Comparison with Similar Provisions

Provincial securities legislation such as Section 36 of the *Securities Act (Ontario)*, Section 36 of the *Securities Rules (B.C.)*, Section 90(1) of the *Securities Act (Alberta)* and Section 162 of the *Securities Act (Quebec)* requires that registered dealers send a confirmation of each trade to the customer. No similar provision applies to registered portfolio managers, who also manage customer accounts. Under Section 123 of Ontario Regulation 1015, registered portfolio managers are required to send quarterly statements of the portfolio.

D Systems Impact of Rule

The rule will have systems implications for some Members in that it will require that additional disclosures or information be added to the monthly statements if the Member chooses to comply with the requirements currently in place for internally managed accounts. However, the option still remains to send trade confirmations to the manager if Members do not wish to make use of the proposed amendment.

E Best Interests of the Capital Markets

The Board has determined that the public interest rule is not detrimental to the best interests of the capital markets.

F Public Interest Objective

According to the IDA's Order of Recognition as a self-regulatory organization, the IDA shall, where requested, provide in respect of a proposed rule change "a concise statement of its nature, purposes and effects, including possible effects on market structure and competition". Statements have been made elsewhere as to the nature and effects of the proposals with respect to the proposed amendments.

The purpose of the proposal is to ensure that the governance and organization structure is of paramount importance as it provides the platform from which the Association delivers upon its dual mandate. As a national not-for-profit Self-Regulatory Organization, the aim of the IDA's corporate governance structure must be to satisfactorily address the inherent conflicts between the public, Members and management. As a result the related general purposes of the amendment are to "ensure compliance with Ontario securities laws", "facilitate fair and open competition in securities transactions generally" and "standardize industry practices where necessary or desirable for investor protection."

The proposal does not permit unfair discrimination among customers, issuers, brokers, dealers, Members or others. It does not impose any burden on competition that is not necessary or appropriate in furtherance of the above purposes.

III COMMENTARY

A Filing in Other Jurisdictions

These proposed amendments will be filed for approval in Alberta, British Columbia, Quebec and Ontario and will be filed for information in Manitoba, Nova Scotia and Saskatchewan.

B Effectiveness

The revision will eliminate the Association requirement with regard to confirmations for externally managed accounts but does not address similar requirements under provincial and territorial securities legislation. Members seeking to use the exemption under the revised rule will have to apply for exemptions under securities legislation to the provinces and territories in which they are registered.

C Process

The issue was raised as a result of some Members receiving relief from the securities commissions on one of the conditions that for accounts managed by external portfolio managers, the Member sends to clients a monthly statement that includes certain information from the trade confirmation. A submission was consequently made to the IDA by BMO Nesbitt Burns seeking the approval of the IDA for a similar arrangement. The proposed amendments were developed by senior management of the IDA and have been approved by the IDA Board of Directors.

IV SOURCES

References:

- Regulations 200.1(c) and 200.1(h)

V OSC REQUIREMENT TO PUBLISH FOR COMMENT

The IDA is required to publish for comment the accompanying amendments.

The Association has determined that the entry into force of the proposed amendments would be in the public interest. Comments are sought on the proposed amendments. Comments should be made in writing. One copy of each comment letter should be delivered within 30 days of the publication of this notice, addressed to the attention of Michelle Alexander, Senior Legal and Policy Counsel, Regulatory Policy, Investment Dealers Association of Canada, Suite 1600, 121 King Street West, Toronto, Ontario, M5H 3T9 and one copy addressed to the attention of the Manager of Market Regulation, Ontario Securities Commission, 20 Queen Street West, 19th Floor, Box 55, Toronto, Ontario, M5H 3S8.

Questions may be referred to:

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INVESTMENT DEALER ASSOCIATION OF CANADA
REGULATION 200.1(H)
CONFIRMATIONS FOR EXTERNALLY MANAGED ACCOUNT TRANSACTIONS

ATTACHMENT #1

The BOARD OF DIRECTORS of the Investment Dealers Association of Canada hereby makes the following amendments to the By-laws, Regulations, Forms and Policies of the Association:

1. Regulation 200.1(h) is amended as follows:

“Notwithstanding the provisions of this Regulation 200.1(h), a Member shall not be required to provide a confirmation to a client in respect of a trade in a managed account, provided that:

- (i) Prior to the trade, the client has consented in writing to waive the trade confirmation requirement;
- (ii) The client may terminate a waiver by notice in writing. The termination notice shall be effective upon receipt of the written notice by the Member, for trades following the date of receipt;
- (iii) The provision of a confirmation is not required under any applicable securities law, regulation or policy of the jurisdiction in which the client resides or the Member has obtained an exemption from any such law, regulation or policy by the responsible securities regulatory authority; and
- (iv) (a) where a person other than the Member manages the account
 - (A) the Member
 - (1) sends a trade confirmation ~~has been sent~~ to the manager of the account, and
 - (2) ~~(B) the Member~~ complies with the requirements of Regulation 200.1(c); or
 - (B) the Member complies with the requirements of paragraph (b) below.
- (b) where the Member manages the account:
 - (A) the account is not charged any commissions or fees based on the volume or value of transactions in the account;
 - (B) the Member sends to the client a monthly statement that is in compliance with Regulation 200.1(c) and contains all of the information required to be contained in a confirmation under this Regulation 200.1(h) except:
 - (1) the day and the stock exchange or commodity futures exchange upon which the trade took place;
 - (2) the fee or other charge, if any, levied by any securities regulatory authority in connection with the trade;
 - (3) the name of the salesman, if any, in the transaction;
 - (4) the name of the dealer, if any, used by the Member as its agent to effect the trade; and,
 - (5) if acting as agent in a trade upon a stock exchange the name of the person or company from or to or through whom the security was bought or sold,
 - (C) the Member maintains the information not required to be in the monthly statement pursuant to paragraph (B) and discloses to the client on the monthly statement that such information will be provided to the client on request.”

PASSED AND ENACTED BY THE Board of Directors this 26th day of October 2005, to be effective on a date to be determined by Association staff.