

## THE MUTUAL FUND DEALERS ASSOCIATION OF CANADA

### HOUSEKEEPING AMENDMENTS TO MFDA RULE 5.3 (CLIENT REPORTING) AND MFDA POLICY NO. 7 (PERFORMANCE REPORTING)

#### Background

On July 27, 2017, the CSA published, in final form, certain amendments to National Instrument 31-103 – *Registration Requirements, Exemptions and Ongoing Registrant Obligations* (“NI 31-103”), and related Instruments. Among other things, the NI 31-103 amendments make permanent certain relief set out under CSA Staff Notice 31-341 – Omnibus/Blanket Orders Exempting Registrants from Certain CRM2 Provisions of National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations*, clarify existing requirements under the Instrument, and deal with other housekeeping matters. Conforming changes are necessary to MFDA Rule 5.3 and MFDA Policy No. 7 to ensure that requirements under MFDA regulatory instruments remain consistent with those under securities legislation.

#### Classification of the Amendments

The proposed amendments to Rule 5.3 and Policy No.7, as summarized below, are classified as housekeeping. In adopting this classification, the MFDA has relied upon section 3(b)(vi) of the Joint Rule Review Protocol for the MFDA, which provides, in relevant part, that housekeeping Rule changes include those that are reasonably necessary to conform MFDA Rules to applicable securities legislation, statutory or legal requirements.

Attached as Schedule “A” to this Notice are the proposed amendments to MFDA Rule 5.3 and Policy No. 7. The current versions of the Rule and Policy have been blacklined to show changes introduced by the proposed amendments.

#### Nature of the Amendments

*Client Reporting – Definitions (Rule 5.3(1)(j) / Rule 5.3(1)(c)(i)):*

The definition of “similar clients”, which was adopted into MFDA Rules on a transitional basis, has been deleted. Corresponding revisions have been made to Rule 5.3(1)(c)(i) to replace the reference to “similar clients” with revised wording adopted under Policy No. 7;

*Content of Account Statement – Market Value and Cost Reporting, Cost of Each Investment Position (Rule 5.3.2(c)(ii)(C)):*

When market value is being used to determine the cost of an investment position, the Rule now requires disclosure of that fact in the account statement. These changes are based on similar revisions made under NI 31-103, **section 14.14.2(2.1)**, regarding account statement disclosure of the cost of security positions, and also formalize guidance previously provided under the MFDA’s CRM2 Implementation

Guide and Tips, respecting account statement disclosure that may be used when market value is used to calculate position cost information (see Bulletin #0657-C, published on September 14, 2015);

*Content of Account Statement – Market Value and Cost Reporting, How Investments are Held (Rule 5.3.2(c)(ii)(H)):*

The Rule has been amended to permit more general disclosure in respect of the party that holds or controls each investment. This change has been adopted directly from NI 31-103, **section 14.14.1(2)(f)** and is consistent with guidance previously provided to Members, respecting the permissibility of more general disclosure (see Bulletin #0689-P, published on May 13, 2016);

*Performance Reporting (Policy No. 7):*

Requirements under NI 31-103, **section 14.19** have been reordered. Appropriate amendments have been made to Policy No. 7 to reflect such changes.

### **Process**

The MFDA followed its established internal governance practices in approving the proposed amendments and considered the need for consequential amendments. The proposed amendments were reviewed by the Regulatory Issues Committee of the MFDA Board of Directors on November 15, 2017, and approved by the full MFDA Board on November 29, 2017. The Board has determined that the proposed amendments are in the public interest.

### **Conflict with Applicable Laws or Terms and Conditions of Recognition Order**

The proposed amendments do not conflict with applicable laws or the Terms and Conditions of a Recognizing Regulator's Recognition Order.

### **Exemption from Requirements Under Securities Legislation**

The proposed amendments involve requirements with which MFDA Members and Approved Persons must comply in order to be exempted from requirements under securities legislation.

### **Effective Date**

The proposed amendments to Rule 5.3 and Policy No. 7 will become effective on a date to be subsequently determined by the MFDA.

**DM 585959v3**

## SCHEDULE "A"

### 5.3 CLIENT REPORTING

#### (1) Definitions

For the purpose of client reporting requirements under Rule 5.3:

- (a) “book cost” means the total amount paid to purchase an investment, including any transaction charges related to the purchase, adjusted for reinvested distributions, returns of capital and corporate reorganizations;
- (b) “connected issuer” has the same meaning as in section 1.1 of National Instrument 33-105 *Underwriting Conflicts*;
- (c) “cost” for each investment position in the account means, subject to paragraphs (i), (ii) and (iii), either “book cost” or “original cost”, provided that only one cost calculation methodology, either “book cost” or “original cost,” is used for all positions;
  - (i) **Investment Positions Opened before December 31, 2015.** For investment positions opened before December 31, 2015, means cost, as determined in accordance with subsection 5.3(1)(c), above; or the market value of the investment position as at December 31, 2015 or an earlier date, if the Member reasonably believes accurate, recorded historical market value information is available for the client’s account and it would not be misleading to the client to provide that information as at the earlier dates~~same date and value are used for all similar clients of the Member and it is also disclosed in the account statement that it is the market value as of that date, not the cost of the investment position, that is being disclosed;~~
  - (ii) **Investment Positions Transferred In.** For investment positions transferred into an account at the Member, means cost as determined in accordance with subsection 5.3(1)(c), above; or the market value of the investment position as at the date of the position’s transfer if it is also disclosed in the account statement that it is the market value, not the cost of the investment position, that is being disclosed; and
  - (iii) **Where Cost Not Determinable.** Where a Member reasonably believes that it cannot determine cost in respect of an investment position, the Member must provide disclosure of that fact in the statement.
- (d) “investment” means any asset, excluding cash, held or transacted in an account of the Member;
- (e) “marketplace” has the same meaning as in section 1.1 of National Instrument 21-101 *Marketplace Operation*;
- (f) “market value” of a security has the meaning given to it under MFDA Form 1 *Financial Questionnaire and Report*;
- (g) “operating charge” means any amount charged to a client by a Member in respect of the operation, transfer or termination of a client’s account and includes any federal, provincial or territorial sales taxes paid on that amount;

- (h) “original cost” means the total amount paid to purchase an investment, including any transaction charges related to the purchase;
- (i) “related issuer” has the same meaning as in section 1.1 of National Instrument 33-105 *Underwriting Conflicts*;
- (j) ~~“similar clients” means any of the following: (i) clients whose accounts or investment positions were transferred together to a Member; (ii) clients whose accounts or investment positions are on the same reporting system, if a Member has more than one reporting system; or (iii) other clients whose accounts or investment positions would appear to a reasonable person to be similar in a way that relates to the recording or calculation of market value or position cost;~~
- (k) “total percentage return” means the cumulative realized and unrealized capital gains and losses of an investment, plus income from the investment, over a specified period of time, expressed as a percentage;
- (l) “trailing commission” means any payment related to a client’s ownership of a security that is part of a continuing series of payments to a Member or Approved Person by any party;
- (m) “transaction charge” means any amount charged to a client by a Member and includes any federal, provincial or territorial sales taxes paid on that amount.

### **5.3.2 Content of Account Statement.**

Each account statement must contain the following information:

#### **(c) Market Value and Cost Reporting.**

for all investments in an account at the Member:

(ii) as at the end of the period for which the statement is made:

(C) the cost of each investment position presented on an average cost per unit or share basis or on an aggregate basis, and determined as at the end of the applicable period. Where market value is used to determine the cost of an investment position, disclosure of that fact must be provided in the account statement.;

**DM 568042**

### **5.3.2 Content of Account Statement.**

Each account statement must contain the following information:

#### **(c) Market Value and Cost Reporting.**

for all investments in an account at the Member:

(ii) as at the end of the period for which the statement is made:

- | (H) disclosure in respect of the name of the party that holds or controls each investment and a description of the way it is held.

**DM 567157**



## **MFDA POLICY NO. 7**

### **PERFORMANCE REPORTING**

#### **Purpose**

Under Rule 5.3.4 (Performance Report), Members are required to deliver a performance report to a client. The purpose of this Policy is to set out additional requirements that Members must comply with when meeting requirements under MFDA Rules respecting the performance report.

#### **General Requirements**

- (1) The performance report required under Rule 5.3.4 must be delivered in a separate report for each account of the client;
- (2) Notwithstanding subsection (1), a Member may provide a performance report that consolidates, into a single report, the required information for more than one of a client's accounts if:
  - (a) the client has consented in writing; and
  - (b) the consolidated report specifies which accounts it consolidates.
- (3) Where a consolidated performance report is sent to a client, pursuant to subsection (2), above and a consolidated report on charges and other compensation is sent to the client pursuant to Rule 5.3.3(3), both consolidated reports must consolidate information for the same accounts.
- (4) The requirement to provide a performance report, as prescribed under Rule 5.3.4, does not apply to a client account that has existed for less than a 12-month period.
- (5) ~~If a Member is not required to provide a performance report to a client for a 12-month period referred to in Rule 5.3.4 if the Member reasonably believes no market value can be determined for any there are no investments of at the client, for which a market value can be determined, the Member is not required to deliver a report to the client for the period.~~

## Content of Performance Report

- (1) A performance report required to be delivered under Rule 5.3.4 must include all of the following in respect of investments reported on the account statement required to be delivered under Rule 5.3.1:
- (a) the market value of all cash and investments in the client's account as at the beginning of the 12-month period covered by the report;
  - (b) the market value of all cash and investments in the client's account as at the end of the 12-month period covered by the report;
  - (c) the market value of all deposits and transfers of cash and investments into the client's account, and the market value of all withdrawals and transfers of cash and investments out of the account, in the 12-month period covered by the report;
  - (d) ~~subject to paragraph 1(e), the market value of all deposits and transfers of cash and investments into the client's account, and the market value of all withdrawals and transfers of cash and investments out of the account, since opening the account;~~ the market values determined under subsection (1.1);
  - (e) ~~if the client's account was opened before July 15, 2015 the following:~~
    - (i) ~~the market value of all cash and investments in the client's account as at July 15, 2015;~~
    - (ii) ~~the market value of all deposits and transfers of cash and investments into the account and the market value of all withdrawals and transfers of cash and investments out of the account, since July 15, 2015;~~
    - (iii) ~~notwithstanding the provisions of (1)(e)(i) and (ii) above, an earlier date may be used to comply with requirements under (1)(e), if the same date and value are used for all similar clients of the Member.~~

### *Annual Change in Market Value*

- ~~(f)~~(e) the annual change in the market value of the client's account for the 12-month period covered by the performance report, determined using the following formula:

$$A - B - C + D$$

where

- A** = the market value of all cash and investments in the account as at the end of the 12-month period covered by the performance report;
- B** = the market value of all cash and investments in the account at the beginning of that 12-month period;
- C** = the market value of all deposits and transfers of cash and investments into the account in that 12-month period; and
- D** = the market value of all withdrawals and transfers of cash and investments out of the account in that 12-month period.



### ***Cumulative Change in Market Value***

~~(g)(f)~~ subject to ~~paragraph subsection (h1.2)~~, the cumulative change in the market value of the account since the account was opened, determined using the following formula:

$$A - E + F$$

where

**A** = the market value of all cash and investments in the account as at the end of the 12-month period covered by the performance report;

**E** = the market value of all deposits and transfers of cash and investments into the account since account opening; and

**F** = the market value of all withdrawals and transfers of cash and investments out of the account since account opening.

~~(h)~~ if the market value of all deposits and transfers of cash and investments into the account since the account was opened or the market value of all withdrawals and transfers of cash and investments out of the account since the account was opened, as required in paragraph (g), is not available to the Member, the cumulative change in the market value of the account determined using the following formula:

$$A - G - H + I$$

where

~~A~~ = the market value of all cash and investments in the account as at the end of the 12-month period covered by the performance report;

~~G~~ = the market value of all cash and investments in the account as at July 15, 2015 or an earlier date used for all similar clients;

~~H~~ = the market value of all deposits and transfers of cash and investments into the account since the date used for G; and

~~I~~ = the market value of all withdrawals and transfers of cash and investments out of the account since the date used for G.

### **Annualized Total Percentage Return**

~~(i)(g)~~ the amount of the annualized total percentage return for the client's account calculated net of charges, using a money-weighted rate of return calculation method generally accepted in the securities industry;

~~(j)~~(h) the definition of “total percentage return” set out under Rule 5.3(1) and a notification indicating the following:

- (i) that the total percentage return in the performance report was calculated net of charges;
- (ii) the calculation method used; and
- (iii) a general explanation in plain language of what the calculation method takes into account.

(1.1) For the purpose of paragraph 1(d), include the following, as applicable:

- (a) if the client’s account was opened on or after July 15, 2015, the market value of all deposits and transfers of cash and investments into the client’s account, and the market value of all withdrawals and transfers of cash and investments out of the client’s account, since opening the account;
- (b) if the client’s account was opened before July 15, 2015, and the Member has not delivered a performance report for the 12-month period ending December 31, 2016:
  - (i) the market value of all cash and investments in the client’s account as at
    - (A) July 15, 2015; or
    - (B) a date that is earlier than July 15, 2015, if the Member reasonably believes accurate, recorded historical market value information is available for the client’s account and it would not be misleading to the client to provide that information as at the earlier date, and
  - (ii) the market value of all deposits and transfers of cash and investments into the account and the market value of all withdrawals and transfers of cash and investments out of the account, since the date referred to in clause (i)(A) or (B), as applicable;
- (c) if the client’s account was opened before July 15, 2015, and the Member has delivered a performance report for the 12-month period ending December 31, 2016:
  - (iii) the market value of all cash and investments in the client’s account as at
    - (A) January 1, 2016; or
    - (B) a date that is earlier than January 1, 2016, if the Member reasonably believes accurate, recorded historical market value information is available for the client’s account and it would not be misleading to the client to provide that information as at the earlier date, and

(iv) the market value of all deposits and transfers of cash and investments into the account and the market value of all withdrawals and transfers of cash and investments out of the account, since the date referred to in clause (i)(A) or (B), as applicable;

(1.2) Paragraph 1(f) does not apply if the client's account was opened before July 15, 2015 and the Member includes in the performance report the cumulative change in the market value of the account determined using the following formula, instead of the formula in paragraph 1(f):

$$\underline{\mathbf{A - G - H + I}}$$

where

A = the market value of all cash and investments in the account as at the end of the 12-month period covered by the performance report;

G = the market value of all cash and investments in the account determined as follows:

(a) if the client's account was opened before July 15, 2015, and the Member has not delivered a performance report for the 12-month period ending December 31, 2016, the market value of all cash and investments in the client's account as at:

(i) July 15, 2015, or

(ii) a date that is earlier than July 15, 2015, if the Member reasonably believes accurate, recorded historical market value information is available for the client's account and it would not be misleading to the client to provide that information as at the earlier date, or

(b) if the client's account was opened before July 15, 2015, and the Member delivered a performance report for the 12-month period ending December 31, 2016, the market value of all cash and investments in the client's account as at:

(i) January 1, 2016, or

(ii) a date that is earlier than January 1, 2016, if the Member reasonably believes accurate, recorded historical market value information is available for the client's account and it would not be misleading to the client to provide that information as at the earlier date;

H = the market value of all deposits and transfers of cash and investments into the account since the date used for G; and

I = the market value of all withdrawals and transfers of cash and investments out of the account since the date used for G.

## Annualized Total Percentage Return – Reporting Periods

(2) The information delivered for the purposes of paragraph (1)(g) must be provided for each of the following periods:

- (a) the 12-month period covered by the performance report;
- (b) the 3-year period preceding the end of the 12-month period covered by the report;
- (c) the 5-year period preceding the end of the 12-month period covered by the report;
- (d) the 10-year period preceding the end of the 12-month period covered by the report;
- (e) subject to subsection (3.1), the period since the client's account was opened if the account has been open for more than one year before the date of the report or, if the account was opened before July 15, 2015, the period since

(i) -July 15, 2015, or

(ii) -~~an~~ a date that is earlier than July 15, 2015~~date~~— if the Member reasonably believes accurate, recorded annualized total percentage return information is available for the client's account and it would not be misleading to the client to provide that information as at the earlier date.

~~(e) —used for all similar clients.~~

(3) Despite subsection (2), if any portion of a period referred to in paragraphs (2)(b), (c) or (d) was before July 15, 2015, the Member is not required to report the annualized total percentage return for that period.

(3.1) Paragraph (2)(e) does not apply to a Member that delivered a performance report for the 12-month period ending December 31, 2016 if the Member provides, in the report, the annualized total percentage return information referred to in paragraph (2)(e) for the period since

(a) January 1, 2016, or

(b) a date that is earlier than January 1, 2016 if the Member reasonably believes accurate, recorded annualized total percentage return information is available for the client's account and it would not be misleading to the client to provide that information as at the earlier date.

## Presentation

- (4) The information required to be delivered under Rule 5.3.4 must be presented using text, tables and charts and must be accompanied by notes in the performance report explaining:
  - (a) the content of the report and how a client can use the information to assess the performance of the client's investments; and
  - (b) the changing value of the client's investments as reflected in the information in the report.
- (5) If a Member delivers information required under Rule 5.3.4 in a report to a client for a period of less than one year, the Member must not calculate the disclosed information on an annualized basis.
- (6) If a Member reasonably believes the market value cannot be determined for an investment position, the market value must be assigned a value of zero in the calculation of the information required to be delivered under Rule 5.3.4 and the fact that its market value could not be determined must be disclosed to the client.

## ~~Exemptions Respecting First Performance Report~~

~~Notwithstanding the requirements noted above, the following exemptions apply in respect of the first performance report sent by Members to their clients:~~

### ~~Content of Performance Report~~

- ~~(1) A Member is exempt from the requirements under paragraphs 1(e) and (h), respecting the provision of market value information as at and since July 15, 2015 if instead a performance report is delivered that provides the information for the 12 month period ending December 31, 2016 and the included market value information is as at and since:
  - ~~(a) January 1, 2016; or~~
  - ~~(b) a date earlier than January 1, 2016, if the same date is used for all similar clients.~~~~

### ~~Annualized Total Percentage Return Reporting Periods~~

- ~~(2) A Member is exempt from the requirement under paragraph 2(e), respecting the provision of annualized total percentage return information, if, instead, an investment performance report is delivered that provides the information for the 12 month period ending December 31, 2016.~~