

13.1.5 MFDA – Summary of Public Comments and Responses Respecting Proposed Amendments to MFDA Recognition Order and MFDA By-law No. 1

MUTUAL FUND DEALERS ASSOCIATION OF CANADA

**Summary of Public Comments Respecting Proposed Amendments to
MFDA Recognition Order and MFDA by-law No.1
(Definition of “Public Director”)**

On May 23, 2008, the British Columbia Securities Commission published proposed amendments to the MFDA's Recognition Orders in British Columbia, Alberta, Saskatchewan, Manitoba, Ontario, New Brunswick and Nova Scotia and to the definition of "Public Director" in MFDA By-law No. 1. (the "**Proposed Amendments**") for a 30-day public comment period.

The public comment period expired on June 23, 2008.

Two submissions were received during the public comment period from:

1. Portfolio Strategies Corporation
2. Kenmar Associates

Copies of comment submissions may be viewed at the offices of the MFDA, 121 King Street West, Suite 1000, Toronto, Ontario by contacting Ken Woodard, Director, Communications and Membership Services Manager, (416) 943-4602.

The following is a summary of the comments received, together with the MFDA's responses.

Amendment of Recognition Orders

Kenmar noted that there was no benefit to investor protection in removing the definition of "Public Director" from the MFDA's Recognition Orders on the basis that it duplicates the MFDA's By-laws which can be changed without prior approval from securities commissions.

MFDA Response

The MFDA is not able to change its By-laws without the prior approval of the relevant members of the Canadian Securities Administrators.

Broadening Definition of "Public Director"

Kenmar questioned whether the amendments to the definition of Public Director designed to permit individuals currently ineligible to act as Public Directors to qualify would enhance investor protection or degrade it. It questioned whether as an example it would be wise to have a registered lobbyist or organization as a Public (or Industry) Director.

MFDA Response

The purpose of the proposed amendments to the definition of MFDA Public Director is, among other things, to permit a broader range of persons to be considered as Public Directors. This provides the MFDA governance process with a wider choice of potential candidates. At the same time, however, the MFDA governance and nominating procedures are robust and judgment can be brought to decisions on whether any particular individual is appropriate or not to serve as a Public Director. With respect to the particular example of a registered lobbyist qualifying as a Public Director, if the candidate lobbied on behalf of the mutual fund industry and derived a material part of his or her income from such activities, it is doubtful that the candidate would be appropriate as a Public Director. On the other hand, a person who was registered as a lobbyist in respect of an entirely unrelated industry may or may not be appropriate according to his or her circumstances.

Aggregate Term of Office Extended to Eight Years

Kenmar observed that Boards get stale and that six years is about the maximum period for a director as long as there is a plan for rotation.

MFDA Response

The MFDA believes that a maximum term of eight years for Industry and Public Directors is appropriate. In the case of Public Directors, in particular, eligible persons with appropriate experience are not always readily available and ensuring that they will be available to serve the industry for a period of eight years is not viewed as being unreasonable.

Experience in Selecting Directors

Kenmar notes that no rationale was provided for the experience of MFDA's Governance Committee being that the current definition of Public Director may be too rigid and inappropriate.

MFDA Response

It is not possible to discuss in a public forum particular candidates but, as an example, the MFDA has in the past identified potential candidates who were entirely appropriate and could act without any real or perceived conflict of interest but who were disqualified as a result of being technically a crown employee or having a remote family relationship with other ineligible persons.

Representative Public Directors

Kenmar observed that representative seniors groups, retired regulator commission personnel, retail investors and investor advocates ought to be considered for MFDA Public Directors.

MFDA Response

The MFDA believes that representatives of any such groups, as well as any other groups, ought to be eligible as Public Directors. In fact, such representatives are, unless otherwise disqualified, eligible and a number of former securities commissioners are MFDA Public Directors.

Chair of the Board to be a Public Director

Kenmar stated that it should be mandatory that the Chair of the MFDA Board be a Public Director.

MFDA Response

The MFDA is a self-regulatory organization which conducts its activities in the public interest. As a self-regulatory organization, members of the mutual fund dealer industry must be represented on the Board as well as Public Directors. In fact, to date the Chair of the MFDA Board has been a Public Director.

Definition of Public Director and Roles and Responsibilities

Kenmar indicates that the roles and responsibilities of Public Directors in the different committees and their composition should be clearly defined.

MFDA Response

The governance structure of the MFDA is reflected in its By-laws as well as the various committee mandates, procedures and directors' handbooks and manuals which together are a complete statement of Board member and committee roles and responsibilities as measured against comparable governance benchmarks. Such materials are under ongoing review by the appropriate committees to ensure they are current and responsive to the requirements of the MFDA, its Members and the public.

Nomination Versus Recommendation of Directors

Portfolio Strategies commented on the proposed amendment to the MFDA By-law to clarify that members have the opportunity to recommend rather than nominate individuals for election to the MFDA Board of Directors. In support of their position that the change is of concern to many members, Portfolio Strategies attached its paper previously circulated to the CSA relating to the MFDA Board selection process.

MFDA Response

The proposed change of wording in the MFDA By-law reflects the result of the debate previously engaged in by Portfolio Strategies, other Members, the MFDA and members of the CSA relating to the MFDA Board selection process and the issues raised in the position paper of Portfolio Strategies. At that time the procedures of the MFDA were confirmed and the result – for

the reasons summarized below - was that the MFDA nomination process, i.e. the act of putting a candidate before the annual meeting of Members for election as a director was confirmed. It was widely regarded (including support by Members in approving the By-laws and the lack of objection by all but a few Members in responding to a Members' survey) that this approach was the most reliable one for ensuring that a Board representative of the wide diversity of MFDA Members as well as the public would be elected. However, it is part of the process that Members should have the opportunity to recommend to the Governance Committee appropriate candidates although they would not be able to make nominations directly to the membership at the annual meetings. The latter approach, it was widely felt, would be simply unworkable in view of the many constituencies that should be represented and the size of the MFDA Board.

The basic governance structure for constituting the MFDA Board reflects the objectives and principles of the Corporate Governance Committee Report of February 2003. That Report was the result of the requirements of the Recognition Orders of various CSA members to the effect that MFDA's governance structure should properly and fairly represent the diversity of its Members. The Report was commented on by CSA staff and the MFDA By-laws implementing the principles of the Report were all approved by the MFDA Board, its Members, the CSA members and Industry Canada. Notwithstanding the foregoing and as indicated above, the basis on which the MFDA Board of Directors was to be constituted was the subject of considerable discussion and review following the Annual General Meeting of Members held in December 2003. In summary, at that time the MFDA took the following steps

- Review and Assessment – the process for constituting the MFDA Board was reviewed and assessed including a careful analysis of the criticisms and comments raised as well as the views expressed by staff of the CSA
- Alternatives – several possible alternatives and/or amended processes for the MFDA were identified and reviewed
- Legal Status – the legal status and compliance of the existing and proposed process as well as the By-laws of the MFDA were reviewed and confirmed
- Member Views – a detailed notice by the MFDA containing a survey was sent to all of its Members explaining the background of the issues under review and soliciting comments
- Responses to Survey – the response to the notice and survey referred to above was very limited and, apart from a few specific continuing criticisms of the process, MFDA Members did not express concern with respect to the adopted processes.

The conclusion of the foregoing review was that there was no reliable basis on which the diversity of MFDA Members could be fairly represented upon the MFDA Board without the nominating process of the kind provided for. A 13 person board is a relatively small group in which the diversity of members in terms of region, industry or public, small and independent, large institutional interests etc. can be represented. Although a nominating process was generally agreed to be necessary to effect the desired result, the process did not preclude wide solicitation of Members and interested parties for recommendations as to nominees and the MFDA has solicited Member participation in that regard. The MFDA has also recognized the importance of continuing and complete communication to its Members so that they have confidence in the Board of Directors that serves the MFDA and its Members.

Approved Amendments to MFDA By-law No. 1 – Definition of “Public Director”, blacklined to version published on May 23, 2008 at (2008) 31 OSCB 5348

MUTUAL FUND DEALERS ASSOCIATION OF CANADA

AMENDMENTS TO SECTION 1 (DEFINITIONS) AND SECTION 3 (DIRECTORS)

The Board of Directors of the Mutual Fund Dealers Association of Canada has made the following amendments:

By-law No. 1 of the Corporation is hereby amended as follows:

1. AMENDMENTS TO SECTION 1 OF MFDA BY-LAW NO. 1

1.1 Amend the definition of “associate” as follows (changes are marked):

1. DEFINITIONS

“~~a~~**Associate**”, where used to indicate a relationship with any person, means:

- (a) any corporation of which such person beneficially owns, directly or indirectly, voting securities carrying more than 10 per cent of the voting rights attached to all voting securities of the corporation for the time being outstanding;
- (b) a partner of that person ~~acting on behalf of the partnership of which they are partners;~~
- (c) any trust or estate in which such person has a substantial beneficial interest or as to which such person serves as trustee or in a similar capacity;
- (d) any relative of such person who resides in the same home as that person ~~including his/her spouse, or his/her spouse who has the same home as such person;~~
- (e) any person who resides in the same home as the person and to whom that person is married, or with whom that person is living in a conjugal relationship outside of marriage; or
- (f) any relative of a person mentioned in clause (e) above who has the same home as such person;

~~but where the Board of Directors orders that two persons shall, or shall not, be deemed to be associates, then such order shall be determinative of their relationships in the application of By laws, Rules and Forms, with respect to that Member;~~

1.2 Amend the definition of “Public Director” as follows (changes are marked):

“Public Director” means a ~~d~~**Director** who is not:

- (a) an officer (other than the Chair or a Vice-Chair) or an employee of the Corporation;
- (b) a current partner, director, officer, employee or person acting in a similar capacity of, or the holder of a Significant Interest in:
 - (i) a Member;
 - (ii) an Associate of a Member; or
 - (iii) an affiliate of a Member; or
- (c) an Associate of a partner, director, officer, employee or person acting in a similar capacity of, or the holder of a Significant Interest in, a Member.

For all purposes of this By-law, a Public Director as at the date this definition of Public Director became effective and who does not qualify as a Public Director under such definition shall be deemed to qualify as a Public Director and to continue so qualified as long as and until he or she ceases to be qualified as a Public Director according to the definition of that term in force immediately before the date this definition becomes effective.

"Significant Interest" means in respect of any person the holding, directly or indirectly, of the securities of such person carrying in aggregate 10% or more of the voting rights attached to all of the person's outstanding voting securities.

- ~~(a) — who is not a current director (other than a Public Director), officer or employee of, or of an associate or affiliate of:
 - ~~(i) — the MFDA;~~
 - ~~(ii) — any protection or contingency fund in which Members (at the time the director holds the relevant office) are required to participate; or~~
 - ~~(iii) — the Investment Funds Institute of Canada or the Investment Dealers Association of Canada;~~~~
- ~~(b) — who is not a current director, partner, significant shareholder, officer, employee or agent of a Member, or of an associate or affiliate of a Member, of:
 - ~~(i) — the MFDA;~~
 - ~~(ii) — any protection or contingency fund in which Members (at the time the director holds the relevant office) are required to participate; or~~
 - ~~(iii) — the Investment Funds Institute of Canada or the Investment Dealers Association of Canada;~~~~
- ~~(c) — who is not a current employee of a federal, provincial or territorial government or a current employee of an agency of the Crown in respect of such government;~~
- ~~(d) — who is not a current member of the federal House of Commons or member of a provincial or territorial legislative assembly;~~
- ~~(e) — who has not, in the two years prior to election as a Public Director, held a position described in (a)-(d) above;~~
- ~~(f) — who is not:
 - ~~(i) — an individual who provides goods or services to and receives direct significant compensation from, or~~
 - ~~(ii) — an individual who is a director, partner, significant shareholder, officer or employee of an entity that receives significant revenue from services the entity provides to, if such individual's compensation from that entity is significantly affected by the services such individual provides to,~~~~the MFDA or any protection or contingency fund in which Members are required to participate, or a Member of the MFDA; and~~~~
- ~~(g) — who is not a member of the immediate family of the persons listed in (a)-(f) above.~~

~~For the purposes of this definition:~~

- ~~(i) — "significant compensation" and "significant revenue" means compensation or revenue the loss of which would have, or appear to have, a material impact on the individual or entity;~~
- ~~(ii) — "significant shareholder" means an individual who has an ownership interest in the voting securities of an entity, or who is a director, partner, officer, employee or agent of an entity that has an ownership interest in the voting securities of another entity, which voting securities in either case carry more than 10% of the voting rights attached to all voting securities for the time being outstanding.~~

2. AMENDMENTS TO SECTION 3 OF MFDA BY-LAW NO. 1

2.1 Amend Section 3 of the By-law as follows (changes are marked):

3. DIRECTORS

3.1 Duties and Number

The affairs of the Corporation shall be managed by a Board of Directors. The number of persons comprising the Board of Directors shall be 13.

3.2 Composition of the Board of Directors

The Board of Directors shall be composed of 6 Public Directors, 6 Industry Directors and the President and Chief Executive Officer. The members of the Board of Directors (other than the President and Chief Executive Officer) shall collectively and over time be nominated and elected on the basis that there will be timely and appropriate regional representation on the Board of Directors of Members of the Corporation across Canada, provided that at any time (subject to the occurrence of vacancies) not less than 4 of the directors shall represent regions other than the Provinces of Ontario and Quebec. In addition, at any time (subject to the occurrence of vacancies) five of the Industry Directors shall be officers or employees of a Member of the Corporation or of an affiliate or associated corporation **which is an Associate** of a Member. No Member, affiliate or associated corporation **which is an Associate** of a Member shall have more than 1 director, officer, employee or other representative on the Board of Directors and, if such event should occur, the Board of Directors in its discretion may request the resignation of or remove as a director, any director or directors in order that the requirements of this section are satisfied. Each director shall be at least 18 years of age.

3.3 Election and Term

~~3.3.1~~ *Initial Election*

~~At the Annual Meeting of the Corporation when this Section 3 of By-law No. 1 is sanctioned and becomes effective, 12 directors shall be elected from persons nominated and recommended to the Board of Directors by an ad hoc nominating committee established by the Board of Directors according to the requirements of Section 3.6.1 as if that Section were in force and a Governance Committee had been established in accordance with its provisions. Of the 6 Public Directors to be so elected, the terms of 3 Public Directors to be designated by the Board of Directors shall each expire at the second and third successive Annual Meetings. Of the 6 Industry Directors to be so elected, the terms of 3 such Industry Directors to be designated by the Board of Directors shall each expire at the first and second successive Annual Meetings on the election of their successors.~~

3.3.21 *Public Directors*

At each Annual Meeting, commencing in the year 2005 3 Public Directors shall be elected to fill the vacancies created by the expiry of the terms of office of the 3 Public Directors whose terms have expired at such meeting. The term for each Public Director to be elected at an Annual Meeting shall expire at the ~~third~~ **second** Annual Meeting next following such election on the election of his or her successors, unless expired earlier in accordance with this By-law. The Board of Directors shall be authorized to fix the term of any Public Director to be elected for a period of less than ~~3~~ **2** years in order to maintain the intended staggered terms of all Public Directors, but no such term shall be shortened if the Public Director has commenced his or her term of office. A Public Director shall be eligible to serve for only ~~2~~ **4** successive terms of ~~3~~ **2** years which shall include any shorter term as may have been fixed by the Board of Directors in accordance with this By-law, but shall exclude any portion of a term of office in respect of a vacancy filled pursuant to Section 3.5. Each Public Director to be elected at an Annual Meeting shall have been recommended by the Governance Committee to the Board of Directors for nomination for election by the Members according to the requirements of the By-laws and the terms of reference of the Governance Committee adopted by the Board of Directors. Any Member shall be entitled to submit to the Governance Committee ~~nomination~~ **recommendations** for Public Directors provided that such ~~nomination~~ **recommendations** shall have been received by the Corporation not less than 60 days prior to the relevant Annual Meeting.

3.3.32 *Industry Directors*

At each Annual Meeting, commencing in the year 2004 3 Industry Directors shall be elected to fill the vacancies created by the expiry of the terms of office of the 3 Industry Directors whose terms have expired at such meeting. The term for each Industry Director to be elected at an Annual Meeting shall expire at the second Annual Meeting next following such election on the election of his or her successors, unless expired earlier in accordance with this By-law. The Board of Directors shall be authorized to fix the term of any Industry Director to be elected for a period of less than 2 years in order to maintain the intended staggered terms of all Industry Directors, but no such term shall be shortened if the Industry Director has commenced his or her term of office. An Industry Director shall be eligible to serve only ~~3~~ **4** successive terms of 2 years which shall include any shorter term as may have been fixed by the Board of Directors in accordance with this By-law, but shall exclude any portion of a term of office in respect of a vacancy filled pursuant to Section 3.5. Each Industry Director to be elected at an Annual Meeting shall have been recommended by the Governance Committee to the Board of Directors for nomination for election by the Members according to the requirements of the By-laws and the terms of reference of the Governance Committee adopted by the Board of

Directors. Any Member shall be entitled to submit to the Governance Committee ~~nominations~~ **recommendations** for Industry Directors provided that such ~~nominations~~ **recommendations** shall have been received by the Corporation not less than 60 days prior to the relevant Annual Meeting.

3.3.3 **Transition**

At the Annual Meeting in 2008 when this Section 3.3.3 is sanctioned and becomes effective,

- (i) Public Directors whose terms expire at such time (having then served 2 consecutive 2 or 3 year terms) shall be eligible to be nominated and elected for 1 further 2 year term;**
- (ii) Public Directors whose terms do not expire at such time (having served less than 2 consecutive 2 or 3 year terms) shall remain eligible to be nominated and elected as Public Directors at subsequent Annual Meetings for further consecutive 2 year terms provided that no such Public Director shall be eligible to serve in aggregate for more than 8 consecutive years as a Public Director;**
- (iii) Industry Directors whose terms expire at such time (having then served 3 consecutive 2 year terms) shall be eligible to be nominated and elected for 1 further 2 year term; and**
- (iv) Industry Directors whose terms do not expire at such time (having served less than 3 consecutive 2 year terms) shall remain eligible to be nominated and elected as Industry Directors at subsequent Annual Meetings for further consecutive 2 year terms provided that no such Industry Director shall be eligible to serve in aggregate for more than 8 consecutive years as an Industry Director.**

3.4 **Vacancies**

The office of a director shall be automatically vacated:

- 3.4.1 if the director by notice in writing to the Corporation resigns his or her office, which resignation shall be effective at the time it is received by the Secretary of the Corporation or at the time specified in the notice, whichever is later;
- 3.4.2 if the director is found to be a mentally incompetent person or becomes of unsound mind;
- 3.4.3 if the director dies;
- 3.4.4 if the director becomes bankrupt or suspends payment of debts generally or makes an arrangement with creditors or makes an assignment or is declared insolvent;
- 3.4.5 in the case of a Public Director, if the director ceases to be qualified as a Public Director;
- 3.4.6 if the director is requested to resign pursuant to Section 3.2 and does not do so in a reasonable time;
- 3.4.7 if the Public or Industry Director is removed by a resolution passed by either three-quarters of the votes cast at a meeting of the Board of Directors or two-thirds of the votes cast at a meeting of Members;
- 3.4.8 in the case of the President and Chief Executive Officer, the director ceases to hold such office.

3.5 **Filling Vacancies**

If a vacancy in the Board of Directors shall occur for any reason, the vacancy shall be filled by a resolution electing or appointing a director passed by either a majority of the votes cast at a meeting of the Members or the Board of Directors, provided that in either case the director has been identified and recommended by the Governance Committee to the Board of Directors for nomination for election and the nominee is otherwise qualified as a director. In recommending any such nominee as a director, the Governance Committee shall ensure the requirements for the composition of the Board of Directors set out in Section 3.3.2 are satisfied and that the nomination process followed by the Governance Committee shall be in accordance with the requirements for nominees to be recommended to the Board of Directors for the election of directors at Annual Meetings except that no notice of the vacancy or request for nominations need be given to Members.

3.6 Committees

3.6.1 Governance Committee

The Board of Directors shall establish a Governance Committee composed of 2 Public Directors and 2 Industry Directors. The 2 Industry Director members of the Governance Committee shall be officers or employees of a Member of the Corporation or of an affiliate or ~~associated~~ corporation **which is an Associate** of a Member. The Chair of the Governance Committee shall be 1 of the 2 Public Directors as selected by the Board of Directors. The Governance Committee shall be responsible for identifying and recommending to the Board of Directors Public and Industry Directors for election to the Board of Directors in accordance with the By-laws and the terms of reference adopted for the Governance Committee by the Board of Directors. In addition, the Governance Committee shall perform such other duties as the Board of Directors may delegate or direct from time to time. 1 Public Director and 1 Industry Director shall constitute a quorum of the Governance Committee.

3.6.2 Audit Committee

The Board of Directors shall establish an Audit Committee composed of 2 Public Directors and 1 Industry Director. The Chair of the Audit Committee shall be 1 of the 2 Public Directors as selected by the Board of Directors. The Audit Committee shall review and report to the Board of Directors on the annual financial statements of the Corporation and shall perform such other duties as the Board of Directors may delegate or direct from time to time. 1 Public Director and 1 Industry Director shall constitute a quorum of the Audit Committee.

3.6.3 Executive Committee

The Board of Directors may in its discretion establish an executive committee (which may be otherwise named) composed of an equal number of Public Directors and Industry Directors. The Chair of the Executive Committee, if any, may be either a Public Director or Industry Director and shall be selected by the Board of Directors. The Executive Committee shall exercise such powers and such duties as are delegated or directed by the Board of Directors including, without limitation, the authority to exercise any of the powers of the Board of Directors. 1 Public Director and 1 Industry Director shall constitute a quorum of the Executive Committee.

3.6.4 Other Board Committees

The Board of Directors may from time to time in its discretion appoint any other committee or committees as it considers necessary or appropriate for such purposes and with such powers as the Board of Directors may determine including, without limitation, the authority to exercise any of the powers of the Board of Directors and to act in all matters for and in the name of the Board of Directors under the By-laws. Subject to any provisions of the By-laws otherwise, any such committee may be composed of Public Directors or Industry Directors, or both. A majority of the members of a committee established under this Section 3.6.4 shall constitute a quorum, provided that if the committee is composed of 1 or more Public Directors, a quorum shall include 1 Public Director.

3.6.5 Committee Membership and Procedures

Members of any committee of the Board of Directors including, without limitation, the Governance Committee, Audit Committee, Executive Committee (if any) or any other committee established pursuant to Section 3.6.4 and shall be appointed and subject to removal by the Board. The Board of Directors may prescribe rules and procedures not inconsistent with the Act and the By-laws relating to the calling of meetings of, and conduct of business by, committees of the Board. Subject to the By-laws and any resolution of the Board of Directors, meetings of any such committee shall be held at any time and place to be determined by the Chair of the committee or its members provided that 48 hours' prior written notice of such meetings shall be given, other than by mail, to each member of the committee. Notice by mail shall be sent at least 14 days prior to the meeting. No error or accidental omission in giving notice of any meeting of a committee shall invalidate such meeting or make void any proceedings taken at such meeting.

3.7 Remuneration of Directors

The Board of Directors may determine from time to time such reasonable remuneration, if any, to be paid to the directors of the Corporation for serving as such and the Board may determine that such remuneration need not be the same for all directors including, without limitation, as between Public and Industry Directors. Public and Industry Directors may be reimbursed for reasonable expenses incurred by the director in the performance of the director's duties. Subject to Sections 6 and 7.1, nothing herein contained shall be construed to preclude any director from serving the Corporation as an officer or in any other capacity and receiving compensation therefor.