ONTARIO SECURITIES COMMISSION

OSC Staff Notice 33-754

Compliance and Registrant Regulation Branch

Summary Report for Dealers, Advisers and Investment Fund Managers

October 14, 2022

Ontario

Table of Contents

Director's Message

We are pleased to share this year's Summary Report for Dealers, Advisers and Investment Fund Managers, which provides an overview of our work during the 2021-2022 fiscal year.

As we return to the office in a hybrid model, staff of the Compliance and Registrant Regulation Branch and from across the Ontario Securities Commission are adjusting work practices to support effective and efficient oversight, guidance, and outreach. We continue to carry out compliance, financial disclosure and conduct reviews through a combination of electronic means. However, we are discussing how to reincorporate in-person meetings with registrants into our hybrid compliance review process and registrant conduct activities. We will keep registrants updated as to when in-person activity will resume.

Highlights from the past year include a compliance sweep of online adviser firms and reviews of firms with limited compliance staffing as compared to their assets under management. We also worked with industry stakeholders on the Client Focused Reforms Implementation Committee to publish comprehensive FAQs to assist the financial industry with operationalizing these important reforms.

Together with the Canadian Securities Administrators, the OSC continues to develop the regulatory framework for the rapidly evolving crypto asset trading industry. Current registrants considering the use of crypto assets are reminded to inform the regulator of this change to their business model. We intend to apply a consistent approach for both new registrants engaged in crypto-related securities activity and existing registrants that are modifying their business models to include crypto assets for the first time.

Looking ahead, our compliance review activity for 2022-2023 will prioritize:

- Assessing the effectiveness of the implementation of the Client Focused Reforms. This multi-year priority will start with a review of conflicts of interest and later transition to a review of KYC, KYP and suitability.
- Compliance reviews of high-risk firms, following the analysis of the data collected in response to the 2022 Risk Assessment Questionnaire.
- Compliance reviews of crypto asset trading platforms.

Our Registrant Outreach program remains a priority, and we continue to provide tools and programs to help registrants with their compliance obligations. Visit the Registrant Outreach webpage to access the Topical Guide for Registrants, Director's decisions, and calendar of events for past and upcoming educational webinars.

If you have a question, comment, or would like to discuss regulatory matters, please feel free to reach out to us. As always, we look forward to engaging with you.

Debra Foubert
Director, Compliance and Registrant Regulation

Glossary of legislative references

Act: *Securities Act*, RSO 1990, c. S. 5

Form 13-502F4: Form 13-502F4 *Capital Markets Participation Fee Calculation*

Form 13-502F5: Form 13-502F5 *Adjustment of Fee for Registrant Firms and Unregistered Capital Markets Participants*

Form 31-103F1: Form 31-103F1 *Calculation of Excess Working Capital*

Form 33-109F4: Form 33-109F4 *Registration of Individuals and Review of Permitted Individuals*

Form 33-109F5: Form 33-109F5 *Change of Registration Information*

Form 33-109F6: Form 33-109F6 *Firm Registration*

NI 21-101: National Instrument 21-101 *Marketplace Operation*

NI 23-101: National Instrument 23-101 *Trading Rules*

NI 23-102: National Instrument 23-102 *Use of Client Brokerage Commissions*

NI 23-103: National Instrument 23-103 *Electronic Trading and Direct Electronic Access to Marketplaces*

NI 24-101: National Instrument 24-101 *Institutional Trade Matching and Settlement*

NI 31-103: National Instrument 31-103 Registration Requirements, Exemptions and Ongoing Registrant Obligations

NI 31-103CP: Companion Policy to NI 31-103

NI 33-105: National Instrument 33-105 Underwriting Conflicts

NI 33-109: National Instrument 33-109 Registration Information

NI 45-106: National Instrument 45-106 Prospectus Exemptions

NI 45-106CP: Companion Policy to NI 45-106

NI 81-102: National Instrument 81-102 Investment Funds

NI 81-105: National Instrument 81-105 *Mutual Fund Sales Practices*

NI 81-107: National Instrument 81-107 Independent Review Committee for Investment Funds

OSC Rule 13-502: OSC Rule 13-502 *Fees*

OSC Rule 31-505: OSC Rule 31-505 Conditions of Registration

OSC Rule 91-507: OSC Rule 91-507 Trade Repositories and Derivatives Data Reporting

Introduction

Who we are

The Compliance and Registrant Regulation (**CRR**) Branch of the Ontario Securities Commission (**OSC**, **Commission**) is responsible for the registration and ongoing regulation of firms and individuals who are in the business of trading in, or advising on, securities or commodity futures and firms that manage investment funds in Ontario. The OSC's mandate is to:

- provide protection to investors from unfair, improper or fraudulent practices,
- foster fair, efficient and competitive capital markets and confidence in capital markets,
- foster capital formation, and
- contribute to the stability of the financial system and the reduction of systemic risk.

CRR's activities are integral to the OSC's vision of being an effective and responsive securities regulator, fostering a culture of integrity and compliance and instilling investor confidence in the capital markets.

The purpose of this report

This Summary Report for Dealers, Advisers and Investment Fund Managers (**Summary Report**) prepared by staff of the CRR Branch is designed to assist registrants with information on the following:

Education and outreach

Part 1 of this report provides links and information to the registration and ongoing educational resources and outreach opportunities available to current and prospective registrants.

Regulatory oversight activities and guidance

Part 2 of this report can be used by registrants as a self-assessment tool to strengthen compliance with Ontario securities law and, as appropriate, to make changes to enhance their systems of compliance, internal controls and supervision.

Impact of upcoming initiatives

Part 3 of this report provides insights into some of the new and proposed rules and other regulatory initiatives that may impact a registrant's operations.

Registrant conduct activities

Part 4 of this report is intended to enhance a registrant's understanding of our expectations for conduct of registrants and applicants for registration. This section also provides insight into the types of regulatory actions the CRR Branch may take to address non-compliance.

Who this report is relevant to

This Summary Report provides information for registrants that are directly regulated by the OSC. These registrants primarily include investment fund managers (**IFMs**), portfolio managers (**PMs**), exempt market dealers (**EMDs**) and scholarship plan dealers (**SPDs**). At present, registrants overseen by the OSC include:

Firms	Individuals
1,142[1]	68,626

IFMs	PMs	EMDs	SPDs
563[2]	313[3]	262[4]	4[5]

In general, firms must register with the OSC if they conduct any of these activities in Ontario:

- are in the business of trading in, or advising on, securities (this is referred to as the "business trigger" for registration)
- direct the business, operations or affairs of an investment fund
- act as an underwriter
- conduct trading or advising activities involving commodity futures contracts or commodity futures options

Individuals must register if they trade, advise or underwrite on behalf of a registered dealer or adviser, or act as the Ultimate Designated Person (**UDP**) or Chief Compliance Officer (**CCO**) of a registered firm.

---

1 Excludes firms registered solely in the category of MFD, ID, commodity trading adviser, commodity trading counsel, commodity trading manager and futures commission merchant.

2 Includes firms registered only as IFMs and IFMs also registered in other registration categories (with the exception of SPD).

3 Includes firms registered only as PMs, RPMs, and PMs/RPMs also registered in other registration categories (with the exception of IFM).

4 Includes firms registered only as EMDs, RDs, and EMDs/RDs also registered in other registration categories (with the exception of IFM or PM).

5 Includes firms registered only as SPDs and SPDs also registered in other registration categories.

There are seven dealer and adviser categories for firms trading in or advising on securities, or acting as an underwriter, as applicable:

- EMD
- SPD
- restricted dealer (**RD**)
- PM
- restricted portfolio manager (**RPM**)
- investment dealer (**ID**), who must be a member of the Investment Industry Regulatory Organization of Canada (**IIROC**)
- mutual fund dealer (**MFD**), who must, except in Quebec, be a member of the Mutual Fund Dealers Association of Canada (**MFDA**)

There are four dealer and adviser categories for firms trading in or advising on commodity futures:

- commodity trading adviser
- commodity trading counsel
- commodity trading manager
- futures commission merchant

IFM is a separate category for firms that direct the business, operations or affairs of investment funds.

Although firms registered in the category of MFD, ID or futures commission merchant, and their registered individuals, are directly overseen by the self-regulatory organizations (**SROs**) (the MFDA and IIROC), the OSC approves the registration of firms in these categories and approves the registration of individuals sponsored by a MFD. Applications for firm registration are reviewed by CRR staff, but we remind firms seeking registration in the category of MFD, ID or futures commission merchant to also apply separately for membership with the relevant SRO.

While this report focuses primarily on registered firms and individuals directly overseen by the OSC, firms directly overseen by the SROs are encouraged to review the Summary Report as certain information is applicable to them as well.

Service standards

The CRR Branch is committed to accountability and transparency, and to ensuring services are delivered in the most efficient and effective ways possible. All CRR service standards and timelines are incorporated into the OSC Service Commitment. Information about CRR-specific service standards and timelines can also be accessed at:

- Exemption Application
- Registration Materials
- Notices of Termination
- Compliance Reviews: Registrants

Organizational structure

The CRR Branch is led by the Director, Debra Foubert. The Director is supported by:

- Elizabeth King, Deputy Director, Registrant Conduct
- Felicia Tedesco, Deputy Director, Operations

The CRR Branch consists of six teams:

- Operations, which comprises three compliance teams
- Registrant Conduct Team
- Data Strategy and Risk Team
- Registration Team

Contact information for directors, managers and staff within the branch can be found in the staff contact information table below.

Operations

Operations is comprised of three teams of lawyers and accountants and is responsible for conducting compliance field reviews, reviewing applications for exemptive relief and working on policy initiatives. The three teams are:

- Investment Fund Manager Team
- Portfolio Manager Team
- Dealer Team

Operations staff also act as subject matter experts in support of registration files.

Registrant Conduct Team

The Registrant Conduct Team handles files referred from other CRR teams and other OSC branches for matters that require further regulatory action to remediate registrant misconduct or to review higher-risk registration applications.

Registrant misconduct may be addressed by applying terms and conditions to registration, suspension of registration or being referred to the Enforcement Branch. This team is also responsible for working on policy initiatives.

Data Strategy and Risk Team

The Data Strategy and Risk Team performs financial analysis of registrants' interim and annual financial statements and capital calculations, leads the Capital Markets Participation Fee process and oversees all fee matters. This team also supports CRR's data requirements and conducts data analytics.

Registration Team

The Registration Team focuses on the initial registration of firms and individuals, subsequent changes to registration, including the surrender of registration, and ongoing maintenance of registration information.

This team is also responsible for processing registration-related applications for exemptive relief and working on registration-related policy initiatives.

Staff contact information

Name	Title	Phone
Debra Foubert	Director	416-593-8101
Elizabeth King	Deputy Director, Registrant Conduct	416-204-8951
Felicia Tedesco	Deputy Director, Operations	416-593-8273
Louise Brinkmann	Manager, Data Strategy and Risk	416-596-4263
Michael Denyszyn	Manager, Registrant Conduct	416-595-8775
Vera Nunes	Manager, Investment Fund Manager Team	416-593-2311
Dena Staikos	Manager, Dealer Team	416-593-8058
Elizabeth Topp	Manager, Portfolio Manager Team	416-593-2377
Kamaria Hoo	Registration Supervisor, Registration Team	416-593-8214
Feryal Khorasanee	Registration Supervisor, Registration Team	416-595-8781
Jenny Tse Lin Tsang (jtselintsang)	Registration Supervisor, Registration Team	416-593-8224

The format for our e-mail addresses is first initial and last name(s): First Last, flast@osc.gov.on.ca.

For registration or fee inquires, please use the following contact information:

- Registration inquiries: registrations@osc.gov.on.ca
- Fees inquires: annualfees@osc.gov.on.ca

Part 1: Outreach

1.1 Outreach program and resources

We interact with our stakeholders through our Registrant Outreach program. The objectives of our Registrant Outreach program are to strengthen communication with Ontario registrants that we directly regulate and with other industry participants (such as lawyers and compliance consultants), to promote strong compliance practices and to enhance investor protection.

Registrant Outreach statistics since inception

Sessions (in-person and webinars)	Replays viewed	Individual attendance	Topical Guide for Registrants – annual page views
72	7,480	15,278	>10,800

Interested in attending an upcoming Registrant Outreach seminar?

Click here for our calendar of upcoming events.

Looking for information about regulation matters?

Take a look at our Registrant Outreach program webpage or our Topical Guide for Registrants for help with key compliance issues and policy initiatives.

Want to be informed about newly released guidance?

Register to receive our e-mail alerts here.

Looking for a listing of recent e-mail alerts and links to each?

Refer to the Compliance-related reports, staff notices and email notifications webpage.

Interested in reading previously published Director's decisions?

Refer to the Opportunity to be heard and Director's decisions webpage.

If you have questions related to the Registrant Outreach program or have suggestions for seminar topics, please send an e-mail to RegistrantOutreach@osc.gov.on.ca.

1.2 Registration

a) Registration Outreach Roadshow

The Registration Team completed another successful Registration Outreach Roadshow (the **Roadshow)** in early 2022. Once again, we hosted virtual sessions. This expanded reach allowed CRR to continue to build working relationships with the registration teams of the firms we have the most interaction with, as well as disseminate information to smaller firms that we do not interact with as often.

The registered firms and group of law firms that we met with were positive about the experience and appreciated the opportunity to have informal sessions with us to better understand our expectations, discuss registration best practices and discuss how to better integrate the registration process with their business needs.

Reviewing Form 33-109F4 during these sessions, with a focus on common deficiencies and deficiencies that impede the review process, continued to be a welcomed addition to the agenda. We see significant value in these Roadshows and gained useful feedback from our post-meeting survey to the participants, which will be taken into consideration for future Roadshows.

b) Common National Registration Database (**NRD**) Issues and Tips

On January 25, 2022, the OSC conducted a seminar that provided a general overview of the NRD online system. This included a presentation on how to navigate the system and an introduction to:

- the most common types of submissions which are filed on the system for the regulators' review
- the most common types of reports which can be generated
- how fees are submitted

This seminar identified common NRD issues encountered as well as provided general tips on completing and filing NRD submissions. To review this webinar, please refer to the National Registration Database 101 webpage on the OSC website.

1.3 Registrant Advisory Committee

Established in January 2013, the Registrant Advisory Committee (**RAC**) is in its fifth term. It is comprised of nine external members and is chaired by the Director of CRR, Debra Foubert. The RAC meets quarterly, with members serving a minimum two-year term.

The RAC's objectives are to:

- advise on issues and challenges faced by registrants in interpreting and complying with Ontario securities law, including matters related to registration and compliance
- provide feedback on the development and implementation of policy and rule-making initiatives that promote investor protection, fair and efficient capital markets, and contribute to the stability of the financial system

Discussion topics over the past year included:

- Amendments to NI 33-109
- the OSC's inclusion and diversity initiative
- CSA Position Paper 25-404 - *New Self-Regulatory Organization Framework*
- Client Focused Reforms (**CFRs**)
- Capital Markets Act consultation draft

Part 2: Information for dealers, advisers and investment fund managers

How to navigate Part 2 of the Summary Report

Part 2 of the Summary Report provides an overview of the key findings and outcomes from compliance reviews conducted during the 2021-2022 fiscal year.

Section 2.1 discusses the annual highlights of the work completed by CRR during the 2021 – 2022 fiscal year. Section 2.2 discusses key or novel issues, suggests best practices, and specifies applicable legislation and relevant guidance to assist firms in addressing each of the topic areas. For ease of reference, registration categories are listed beside each deficiency heading to indicate that the information is relevant to firms registered in those categories.

We encourage registrants to review all the information set out in Part 2 of this report as the guidance presented may be helpful to registration categories other than those listed.

2.1 Annual highlights

2.1.1 High risk firms

2.1.2 High impact firms

2.1.3 Online adviser sweep

2.1.4 Firms with limited compliance staff sweep

2.1.5 Registration of Crypto Asset Trading Platforms (CTPs)

2.1.6 FX conversion services dealer review

2.1.1 High risk firms (All)

In 2021, we commenced compliance reviews of firms that were risk-ranked as 'high' based on information collected from the 2020 risk assessment questionnaire (the **RAQ**). A firm may be risk-ranked as high based on a variety of factors, including: the broad nature of the firm's business activities, a large amount of client assets under management (**AUM**), the size of the firm, the number of clients and/or the type of clients serviced by the firm.

We reviewed registrants that were identified as high-risk and, where appropriate, issued warning letters and took further regulatory action to remediate identified deficiencies.

2.1.2 High impact firms (IFM / PM)

As part of our risk-based approach to selecting firms for review, we select firms that, given the size of their AUM, could have a significant impact on the capital markets if there was a breakdown in their compliance structure or key operations (**high impact firms**).

In 2021, we commenced compliance reviews of six high impact firms with a combined AUM of approximately $900 billion as of December 31, 2020. We apply a modified approach to reviewing high impact firms as part of our continued efforts to assess the most effective way to oversee our registrant population. Specifically, the reviews for high impact firms focus on assessing each firm's ability to identify and effectively manage its regulatory and compliance risks by reviewing each firm's:

- governance structure
- risk framework, including the risk identification and risk management process
- identified compliance issues during the review period, including how any non-compliance was remediated and what steps were put in place to prevent reoccurrence

2.1.3 Online adviser sweep (PM)

In 2021, we began a compliance sweep of PMs that provide discretionary investment management services to retail investors through an interactive website (**online adviser sweep**). Our sample consists of PMs for which the OSC is the principal regulator.

The purpose of the online adviser sweep is to assess the processes used by PMs who provide advice using an online platform. Staff are focused on certain processes which include know-your-client (**KYC**) and suitability, marketing, and the composition of investor profiles and model portfolios offered to investors.

We continue to execute these reviews and following the conclusion of the sweep, consideration will be given to publishing our findings and observations.

Registrants are reminded that the OSC must be notified when there is a material change to the firm's business model. This would include adopting an online advice platform or making a significant change in the way an existing online advice platform operates. As noted in CSA Staff Notice 31-342 *Guidance for Portfolio Managers Regarding Online Advice*, a registrant is required to submit a Form 33-109F5 if it changes its primary business activities, target market, or the products and services it provides to clients to something different than what is described in the firm's current Form 33-109F6 filing.

2.1.4 Firms with limited compliance staff sweep (All)

In late 2021, we began a sweep of firms that have AUM of at least $25 million and a small number of compliance staff (less than or equal to one full-time employee). Firms registered as either IFM, PM, EMD or a combination of these registration categories are included in this sweep.

The purpose of this sweep is to determine whether:

- firms with limited compliance staff have adequate resources and an effective compliance system to provide reasonable assurance that the firm and each individual acting on the firm's behalf complies with securities law
- these firms pose a higher risk of non-compliance with securities law
- there are trends in the type of deficiencies arising from this business model

To date, some of the common deficiencies identified from this sweep include:

- inadequate written policies and procedures
- inadequate cyber security internal controls
- incorrect calculation of the firm's excess working capital
- trade confirmations missing required information
- investment performance report missing required information
- various statements delivered to clients (i.e. trade confirmation, account statements, investment performance reports) which did not include the firm's letterhead or legal name

As this compliance sweep is in progress, additional findings may be communicated in next year's Summary Report.

2.1.5 Registration of Crypto Asset Trading Platforms (CTPs)

In 2021, the Canadian Securities Administrators (**CSA**) and IIROC issued Joint CSA/IIROC Staff Notice 21-329 *Guidance for Crypto-Asset Trading Platforms: Compliance with Regulatory Requirements*, which sets out how securities legislation applies to CTPs that facilitate the trading of security tokens (crypto assets that are securities) or of crypto contracts (instruments or contracts involving crypto assets). This notice stated that CTPs may seek time-limited registration as a restricted

dealer as an interim step to seeking registration as an ID and obtaining membership with IIROC.

The OSC also issued a press release in 2021 notifying CTPs that currently offer trading in derivatives or securities to persons or companies located in Ontario, that they must bring their operations into compliance with Ontario securities law or face potential regulatory action.

This is a multi-branch initiative involving teams from various branches within the OSC that are reviewing and granting exemptive relief where appropriate, including from:

- the suitability determination requirements in NI 31-103
- the prospectus requirements in respect of CTPs entering into crypto contracts with clients to purchase, hold and sell crypto assets that are not themselves securities or derivatives
- certain reporting requirements in Part 3 of OSC Rule 91-507
- requirements in NI 21-101, NI 23-101 and NI 23-103

As part of the exemptive relief decisions for registered CTPs, the following, among other requirements, are to address investor protection concerns:

- disclosure requirements
- the CTP must assess whether it is appropriate for an account to be opened for a client
- the establishment of loss limits for each client
- the imposition of investment limits
- the use of third-party custodians
- regular reporting to the Principal Regulator

As of March 31, 2022, the OSC was in the process of prioritizing the review of 20 applications received for dealer registration and relief. During the past fiscal year, four CTPs were registered and received exemptive relief to offer crypto products to investors in Ontario, bringing the total number of registered CTPs to eight as of June 30, 2022. We continue to assess the appropriate path to registration in Ontario for CTPs that have initiated discussions with staff.

For a listing of registered CTPs and the associated exemptive relief decisions, please refer to the Registered crypto asset trading platforms webpage on the OSC website.

2.1.6 FX conversion services dealer review

During the 2021/2022 fiscal year, a joint team from the OSC's Derivatives and CRR Branches conducted a review of certain market participants who offer foreign exchange (**FX**) conversion services tied to securities transactions. The market participants included were bank and non-bank owned dealers, contracts for difference providers and money service businesses.

The purpose of this review was to determine:

- if the FX rate/spread charged to retail clients was disclosed
- whether the FX rate/spread charged to retail clients was fair and consistent with the disclosure provided to clients

Staff collected information related to the procedures, disclosure and execution of FX rates/spreads associated with securities transactions. The information collected was used to understand the process to determine the FX rate/spread charged to clients, and how it was disclosed and applied to securities transactions.

CRR staff will continue to collaborate with the Derivatives Branch to communicate any findings to firms that were reviewed.

2.2 Registration and compliance deficiencies

2.2.1 Restriction on self-custody (IFM)

The custody provisions in NI 31-103 prohibit self-custody by registered firms except for certain limited exceptions. During our reviews, we noted instances where an IFM chose to self-custody certain portfolio securities of their prospectus-exempt investment funds, but it was unclear how the IFM qualified for an exemption from the restriction on self-custody. If a "qualified custodian" (as defined in NI 31-103) is not used to custody a fund's assets, then the IFM must be able to rely on an available exemption in subsection 14.5.2(7) of NI 31-103. If an IFM is relying on an exemption to engage in self-custody, the firm should assess the risks, comply with the requirements of section 14.6 of NI 31-103, and have policies and procedures that illustrate how the portfolio securities qualify for self-custody.

We continue to note instances where an IFM does not have a written custodial agreement in respect of the prospectus-exempt funds managed by the IFM. Written custodial agreements should cover the location of portfolio assets, any appointment of a sub-custodian, the method for holding client assets, the standard of care of the custodian and the responsibility of loss.

IFMs should:

- ✓ if considering self-custody, consult with legal counsel about whether they qualify for an exemption in subsection 14.5.2(7) of NI 31-103
- ✓ review and, if required, update existing custodial agreements to include all relevant and material requirements of the custody arrangement

Legislative references and guidance

- The Act, s. 19(1) *Record keeping*
- NI 31-103 and related NI 31-103CP, s. 11.5 *General requirements for records*
- NI 31-103 and related NI 31-103CP, s. 14.5.2 *Restriction on self-custody and qualified custodian requirement*
- NI 31-103 and related NI 31-103CP, s. 14.6 *Client and investment fund assets held by a registered firm in trust*
- OSC Staff Notice 33-749 *2018 Annual Summary Report for Dealers, Advisers and Investment Fund Managers*, page 72

2.2.2 Related party receivables in excess working capital calculations (All)

As part of our normal course compliance review process, we review the excess working capital calculations of registrants. Current assets that are included in Line 1 of Form 31-103F1 but are not readily convertible into cash should be deducted on Line 2 of Form 31-103F1.

Related party receivables, like shareholder loans, are considered higher risk when included in regulatory capital calculations as firms may loan funds to related parties

with solvency issues. During the year, we noted instances where firms were unable to provide support for related party receivables included in the current assets figure in Line 1 of Form 31-103F1. These firms did not maintain adequate evidence to support that shareholder loans were readily convertible into cash and therefore appropriately classified as a current asset in the firm's calculation of excess working capital.

We also identified frequently recurring transactions, whereby a shareholder loan was repaid to the firm, but the shareholder subsequently borrowed a similar loan amount shortly thereafter. In staff's view, the economic substance of these transactions was that the loan obligation to the firm was not settled, and the receivable balance remained uncollected. Frequently recurring transactions of this nature suggests that it is not appropriate to exclude the related party receivable balance as a deduction on line 2 of Form 31-103F1.

Registered firms should:

- ✓ maintain a record of all related party loans included in excess working capital calculations and their duration (the date the loan was made and the date it was repaid)
- ✓ document the terms of each related party loan, including the parties involved, the purpose of the loan, dollar amount, interest rate, and repayment terms and timeline
- ✓ retain documentation to support that the related party receivable can be readily convertible into cash (e.g. evidence that the loan is payable on demand)

Legislative references and guidance

- NI 31-103 and related NI 31-103CP, s. 12.1 *Capital requirements*
- Form 31-103F1
- OSC Staff Notice 33-742 *2013 OSC Annual Summary Report for Dealers, Advisers and Investment Fund Managers*, pages 33-35

2.2.3 Prohibited investments (IFM / PM)

We noted instances where PMs acting for investment funds knowingly directed a trade in portfolio securities to another investment fund for which the PM also acts as an adviser. These trades were conducted without a valid exemption.

In one instance, a PM, who was appointed as a sub-adviser to an investment fund that was winding down, purchased certain private securities from the fund's portfolio for the portfolio of another investment fund for which it acted as PM. Although the PM obtained consent from the directors of the terminating fund, this transaction was still not permitted under paragraph 13.5(2)(b) of NI 31-103.

In another example, a PM caused an investment fund it advised to enter into trades with another investment fund it advised. The IFM of both investment funds is affiliated with the PM and the firms operate closely. The trades conducted by the PM was prohibited as the PM acts as adviser for both funds. The IFM also did not identify the trades as being prohibited and relied solely on the PM's policies and procedures with respect to the inter-fund trade prohibition.

Paragraph 13.5(2)(b) of NI 31-103 prohibits inter-fund trading between two investment funds that have the same adviser. An inter-fund trade occurs when an adviser for an investment fund knowingly directs a trade in portfolio securities to another investment fund that it acts for or instructs the dealer to execute the trade with the other investment fund. An exemption from this prohibition may be available in section 6.1 of NI 81-107, but only if certain conditions are met.

PMs should:

- ✓ have policies and procedures in place to comply with the requirements of paragraph 13.5(2)(b) of NI 31-103
- ✓ for an inter-fund trade, consider whether the firm can rely on the exemption in NI 81-107 or exemptive relief from paragraph 13.5(2)(b) of NI 31-103 is required

IFMs should:

- ✓ as part of their oversight, verify that the adviser of the funds has appropriate inter-fund trading policies and procedures

Legislative reference and guidance

- NI 31-103 and related NI 31-103CP, s. 13.5(2)(b) *Restrictions on certain managed account transactions*
- NI 81-107, s. 6.1 *Inter-fund trades*
- OSC Staff Notice 33-746 *2015 Annual Summary Report for Dealers, Advisers and Investment Fund Managers*, pages 73-74

2.2.4 Suitability and client instructions (PM / EMD)

PMs and EMDs may receive instructions from clients to buy, sell, or hold a specific security. These requests are sometimes referred to as client directed trades or unsolicited orders (**client instructions**).

If a registrant receives client instructions, they must make a suitability determination by taking into consideration the impact of the action on the client's account, the impact of potential and actual costs on the return on investment and compare this information to reasonable alternative actions available when making the determination. If a registrant intends to take an action based on client instructions that would not be suitable for the client, they must take the measures set out in subsection 13.3(2.1) of NI 31-103.

a) Delegation of PM obligations when receiving client instructions (PM)

In some cases, we observed PMs communicating to clients that trades in response to a client instruction fall outside the client's normal relationship with the firm. In one case, a firm stated in its investment management agreement (**IMA**) that it does not have a fiduciary relationship with the client in respect of these trades.

We remind PMs that a registered firm has a duty to treat its clients fairly, honestly and in good faith. This duty applies to both advice given within a managed account and advice given in response to client instructions. It is not appropriate for PMs to suggest that trades made in response to client instructions, which do not follow subsection 13.3(2.1) of NI 31-103, fall outside the normal PM-client relationship or the duties owed by the PM to the client are any less with respect to these trades.

b) Inadequate measures when receiving client directed trades (EMD)

We identified instances where EMDs took inadequate measures when client directed trades were received. In certain cases, the EMD received and carried out client instructions, but the client was not clearly informed that the action was not suitable. In other cases, the client was not adequately informed of the basis for the EMD's suitability determination, and instead the client received an acknowledgement form to complete that included boilerplate language as to why the action may be unsuitable. We also noted that some EMDs who carried out client directed trades did not retain evidence of the client's instructions.

PMs and EMDs should:

- ✓ develop policies and procedures consistent with subsection 13.3(2.1) of NI 31-103 to be followed when client instructions are received
- ✓ refrain from contracting-out of their obligations to clients
- ✓ use clear and tailored language when informing the client of its suitability assessment
- ✓ maintain records to demonstrate compliance with its suitability obligations
- ✓ adhere to the duty to deal fairly, honestly and in good faith with clients

Legislative reference and guidance

- OSC Rule 31-505, s. 2.1(1) *General duties*
- NI 31-103, s. 11.5(1)(a) *General requirement for records*
- NI 31-103 and related NI 31-103CP, s. 13.2 *Know your client*
- NI 31-103CP, s. 13.2.1 *Transfers in and client directed trades*
- NI 31-103 and related NI 31-103CP, s.13.3 *Suitability determination*
- CSA Staff Notice 31-336 *Guidance for Portfolio Managers, Exempt Market Dealers and Other Registrants on the Know-Your-Client, Know-Your-Product and Suitability Obligations*, pages 15-17
- OSC Staff Notice 33-751 *2020 Summary Report for Dealers, Advisers and Investment Fund Managers*, page 35

2.2.5 Prospectus exemptions misuse (EMD)

Offering memorandum exemption (OM exemption)

During compliance reviews, we identified instances of EMDs not complying with the prescribed $30,000 investment limit for eligible investors when relying on the OM exemption. In some cases, EMDs assessed their clients' trades as unsuitable but proceeded with the trades, which exceeded the $30,000 investment limit, after obtaining a client directed trade form. To exceed the $30,000 investment limit, eligible investors must receive advice that their investment is suitable.

Some EMDs informed staff that, after a client directed trade form was received, the EMD subsequently determined that the client's investment was suitable. In these instances, there was no evidence of the EMD's suitability assessments. Firms are reminded to retain documentation to evidence that it complied with its obligations, including suitability.

We also remind EMDs that completion of a risk acknowledgement form alone is not adequate documentation to evidence that the firm met its obligations to assess suitability and provide eligible investors with advice that their investment is suitable.

Family, friends and business associates exemption

We found instances where EMDs relied on the family, friends and business associates (**FFBA**) exemption to distribute securities to clients who did not meet the relationship criteria required by the exemption. For an EMD to rely on the FFBA exemption, the client must have a relationship specified in subsection 2.5(1) of NI 45-106.

We also found that some EMDs did not collect and document adequate information about their clients and their relationships with the issuer and/or its principals. For example, some registrants relied solely on representations made by the purchaser verbally or in the risk acknowledgement form and did not ask questions or document the responses to the questions to confirm the nature and length of the relationship. EMDs should obtain information to confirm the purchaser meets the conditions of the exemption and keep documentation of the steps taken to establish the purchaser met the conditions of the exemption.

Asset acquisition exemption

Staff identified instances where an EMD relied on the asset acquisition exemption without ensuring that the conditions of the exemption were met. In these cases, investors exchanged securities they owned that were valued at less than $150,000 in return for securities of an issuer. A condition of the exemption is that the assets transferred by the investor, as consideration for the securities, must have a fair value of at least $150,000.

Staff also observed that, when the value of the securities transferred by an investor was less than $150,000, the client's investment was combined with other purchases of the issuer, either by the same investor, a related family member or a related corporate entity. These other investments, made on different dates, were combined by the EMD to reach a value greater than $150,000. This "layering" of investments is not permitted under the asset acquisition exemption. The exemption requires that assets transferred have a fair value of at least $150,000 at the time of distribution; it is not permissible to layer investments occurring on different dates to meet the $150,000 minimum required value.

EMDs should:

- ✓ take reasonable steps to confirm and document that the conditions of prospectus exemptions relied on are met
- ✓ when relying on the OM exemption for an eligible investor investing greater than the $30,000 investment limit, conduct a suitability analysis and maintain documentation to evidence why the trade was suitable
- ✓ when relying on the FFBA exemption, collect and document information about the individuals, including the nature of the relationship, the frequency of contact, and the level of trust and reliance between the individuals
- ✓ establish clear policies and procedures for all of the above

Legislative reference and guidance

- NI 45-106, s. 2.5(1) *Family, friends and business associates*
- NI 45-106, s. 2.9(2.1) *Offering memorandum*
- NI 45-106CP, s. 1.9 *Responsibility for compliance and verifying purchaser status*
- NI 45-106CP, s. 2.7 *Close personal friend*
- NI 45-106CP, s. 2.8 *Close business associate*
- NI 45-106CP, s. 3.8(1.1) *Eligibility criteria and investment limits*
- OSC Staff Notice 33-748 *2017 Annual Summary Report for Dealers, Advisers and Investment Fund Managers*, pages 50-55
- OSC Staff Notice 33-751 *2020 Summary Report for Dealers, Advisers and Investment Fund Managers*, page 36

2.2.6 Common issues identified in pre-registration reviews of CTPs

The "Registration as the First Compliance Review", also referred to as the pre-registration review, involves gathering information through written inquiries, requests for documentation and/or interviews of a firm's key representatives. The purpose of the pre-registration review is to assess compliance with Ontario securities law at the time of registration. The following sections highlight common areas where we have identified issues and includes guidance for CTPs applying for registration in a dealer category.

a) Insurance

During the pre-registration reviews of CTPs, we identified CTP firms whose insurance bonding policies were not compliant with the prescribed insurance requirements. For example:

- Insurance bonding policies did not include all bonding and insurance clauses as specified in Appendix A to NI 31-103.
- The CTP held or had access to crypto assets, but the insurance bonding policy only provided coverage for certain assets (e.g. cash and securities) and crypto assets were not covered by the insurance bonding policy.
- The insurance bonding policy only provided insurance coverage for crypto assets held in a specific type of wallet. The CTP had access to crypto assets maintained in hot wallets, but the insurance bonding policy only provided coverage for crypto assets held by the CTP in cold wallets.
- In determining total client assets held to which the CTP had access, the CTP only considered crypto assets held in certain wallets and, as a result, the coverage amounts provided by the insurance bonding policy did not meet the prescribed insurance requirements.

CTP dealer applicants should:

- ✓ verify that the insurance bonding policy includes coverage for all the required clauses specified in Appendix A to NI 31-103
- ✓ review the insurance bonding policy for coverage exclusions and limitations, especially where the insurance bonding policy specifically excludes coverage for certain types of client assets or includes limitations whereby insurance coverage is only available for crypto assets which are held in a specific manner
- ✓ assess the adequacy of coverage limits at the time of policy issuance, and have policies and procedures to review coverage limits regularly and at the time of renewal

Legislative reference and guidance

- NI 31-103, s. 12.3 *Insurance – dealer*
- NI 31-103, *Appendix A – Bonding and Insurance Clauses*

b) Custody

While the requirement to use a qualified custodian does not apply to firms holding crypto assets that are not themselves securities, section 14.6 of NI 31-103 requires firms to hold assets with an appropriate custodian, separate and apart from its own property and in trust for its clients.

As with custodians for other commodities (e.g. bullion), certain specialized custodians possess unique technical knowledge, skills and expertise in holding

crypto assets that a traditional custody institution may not have. Safeguarding crypto assets may require the use of specialized technology solutions to effectively address custodial risks. For example, a custodian specializing in holding crypto assets may use encryption techniques, cold storage and proprietary hardware devices to maintain the safekeeping of the crypto assets. Accordingly, there may be custodians that do not meet the definition of a "qualified custodian" (as defined in section 1.1. of NI 31-103) but have proficiency and experience in holding crypto assets.

During our pre-registration reviews of CTPs, we noted instances where CTP firms did not:

- hold client assets separate and apart from their own property and in trust for their clients
- have policies and procedures related to custodial arrangements and how the CTP will oversee outsourced functions such as custody
- maintain an effective system of controls and supervision to address custodial risks and safeguard crypto assets held in its custody

CTP dealer applicants should:

- ✓ when maintaining custody of client crypto assets,
  - maintain policies and procedures on how crypto assets will be safeguarded and monitored, including:
    - what approvals are required when crypto assets are transferred internally between the CTP's wallets or to client wallets
    - how the CTP will verify that its internal ledger reconciles to the amount of crypto assets held
    - what due diligence will be performed prior to using a third-party wallet service provider
  - establish safeguards to address cyber security, privacy and business interruptions
- ✓ have policies and procedures to address custodial arrangements, which include:
  - ensuring the written custodial agreement clearly sets out the roles and responsibilities of each party to the arrangement
  - conducting initial and ongoing assessments of the custodian including its expertise in holding crypto assets, financial condition and internal controls to safeguard crypto assets
  - if the CTP has terms and conditions on the amount of crypto assets to be held with a qualified custodian, how the CTP will monitor and verify that the amount of crypto assets held with a qualified custodian(s) is not less than what is specified by the terms and conditions on its registration

Legislative reference and guidance

- NI 31-103 and related NI 31-103CP, s. 14.6 *Client and investment fund assets held by a registered firm in trust*
- NI 31-103 and related NI 31-103CP, Part 11, *Division 1 – Compliance*

c) Marketing

In September 2021, CSA and IIROC staff released CSA/IIROC SN 21-330*,* which provided guidance for CTPs relating to advertising and marketing.

During pre-registration reviews of CTPs, we identified the following concerns in the advertising, marketing and social media for CTPs:

Exaggerated and unsubstantiated claims

Some CTPs made exaggerated and unsubstantiated claims related to the performance of crypto assets. For example, in certain advertisements and social media posts, we identified claims from CTPs which suggest that crypto asset returns were greater than returns in public markets, or that the returns for a crypto asset were "going to the moon" (implying extremely high returns). In these instances, the claims were exaggerated and there was no evidence to substantiate the claims made.

Misleading, incorrect, or false statements

We identified statements in advertisements and marketing materials for some CTPs that could be considered false or misleading. For example, we often saw that on websites, and in other advertisements, CTPs promoted commission-free trades. This could be false or misleading to investors because, in these instances, the CTPs would instead charge a markup on the price it is able to obtain or take a spread on trades where it acts as market maker (e.g. when selling crypto assets to a client).

Improper claims related to registration or compliance with securities laws

We noted instances where CTPs included improper claims related to their registration status or compliance with securities laws. On the websites for some CTPs, we identified the following claims: "compliant"; "approved by the OSC"; "platform is approved"; and "we meet all regulatory requirements". In these instances, the CTPs were not registered with any securities regulator in Canada. These claims may be false or misleading to investors as it could suggest that the CTP is registered with a securities regulator and in compliance with securities legislation.

Use of another CTP's name in advertisements

We observed CTPs directly referencing other CTPs by name in advertisements such as in social media posts. For instance, a CTP used its social media account to create a post which included the name of another CTP. The CTP did not obtain

authorization from the other CTP to do so. Unless a CTP can comply with section 43 of the Act, a CTP shall not use the name of another CTP in its advertisements.

CTP dealer applicants should:

- ✓ check that statements made in advertisements are accurate and can be substantiated
- ✓ provide adequate context and references to the information supporting claims, including third-party sources
- ✓ if using the name of another CTP, confirm that the requirements of section 43 of the Act are met
- ✓ have policies and procedures in place to review and approve advertising and marketing materials for compliance with securities law

Legislative reference and guidance

- The Act, s. 43 *Use of name of another registrant*
- OSC Rule 31-505, s. 2.1(1) *General Duties*
- *CSA-IIROC Staff Notice 21-330 Guidance for Crypto-Trading Platforms - Requirements relating to Advertising, Marketing and Social Media Use*
- OSC Staff Notice 33-752 *2021 Summary Report for Dealers, Advisers and Investment Fund Managers*, pages 23-25

2.2.7 Conflicts of interest (All)

The CFR amendments related to conflicts of interest came into force on June 30, 2021. As part of our normal course compliance reviews, staff have started to review registrants' implementation of the new requirements, and we have noted instances where firms:

- did not identify existing material conflicts of interest, or material conflicts of interest that are reasonably foreseeable
- did not address material conflicts of interest in the best interest of the client
- did not provide clients with the required disclosure of material conflicts of interest
- did not adequately update their policies and procedures to implement the CFR amendments to the conflicts of interest requirements

Firms were required to review their policies, procedures and controls and implement any changes necessary to reflect the new conflicts of interest CFR requirements by June 30, 2021. Firms were also required to update any training programs provided to their staff.

Additionally, the CSA and the SROs are currently conducting a targeted sweep of registered firms' compliance with the conflicts of interest amendments.

Registered firms should:

- ✓ implement adequate processes to identify existing and reasonably foreseeable material conflicts of interest between the firm and the client, and between each individual acting on the firm's behalf and the client
- ✓ avoid material conflicts of interest or use controls to mitigate those conflicts sufficiently so that the conflict is addressed in the client's best interest
- ✓ provide training to their staff on the conflicts of interest amendments
- ✓ maintain records to demonstrate compliance with the conflicts of interest requirements (e.g. maintain an inventory of all conflicts identified and the assessment that the controls in place are sufficient to address material conflicts in the best interest of clients)
- ✓ provide prominent and specific disclosure to clients regarding material conflicts of interest at a time and manner that will be meaningful to the client

Legislative references and guidance

- NI 31-103 and related NI 31-103CP, s. 11.5 *General requirements for records*
- NI 31-103 and related NI 31-103CP, s. 13.4 *Identifying, addressing and disclosing material conflicts of interest – registered firm*
- NI 31-103, s. 13.4.1 *Identifying, reporting and addressing material conflicts of interest – registered individual*
- NI 31-103, s. 13.4.2 *Investment fund managers*
- CSA website with Client Focused Reforms Frequently Asked Questions

2.2.8 Marketing review (IFM / PM / EMD)

In 2020, we conducted a desk review of the marketing practices of IFMs, PMs and EMDs (the **marketing review**). At the conclusion of the marketing review, we identified deficiencies which had been previously discussed in past guidance and deficiencies which related to novel areas.

a) Use of hypothetical illustrations (PM)

We noted instances where PMs used illustrations incorporating hypothetical information which were presented to retail investors for informational or educational purposes. For example, PMs posted illustrative graphs on their websites explaining the benefits of compounding or the impact of lower fees on portfolio returns over a period of time. These examples were accessible to all investors including retail investors. The performance inputs used in these illustrations were hypothetical as they did not reflect performance data from actual client portfolios.

In certain cases, we had concerns that the illustration's educational purpose or objective was unclear and that an investor could misinterpret an illustration as presenting potential performance returns available to clients.

As highlighted in CSA Staff Notice 31-325, we have concerns with the presentation of hypothetical performance data to clients lacking sophisticated investment knowledge (i.e. when the information is widely disseminated on a website or advertisement). However, we acknowledge that providing educational illustrations or tools that explain key investing concepts, such as compounding or the impact fees have on investment returns, can be beneficial, especially to investors that may not be sophisticated. As such, it may be appropriate to use hypothetical illustrations for general informational and educational purposes. Hypothetical illustrations used to educate investors should be accompanied by adequate explanations and disclosure that clearly describe the illustration to prevent misleading investors and reduce the potential for client confusion.

PMs should:

- ✓ label the illustrations as "hypothetical" in a clear and prominent manner
- ✓ provide clear and meaningful disclosure which explains the educational purpose or objective of providing the illustration to investors
- ✓ disclose the underlying assumptions used, the calculation methodology and any other relevant factors
- ✓ include a description of the inherent risks and limitations of the data

Legislative reference and guidance

- The Act, s. 44(2) *Representation prohibited*
- OSC Rule 31-505, s. 2.1(1) *General Duties*
- CSA Staff Notice 31-325 - *Marketing Practices of Portfolio Managers*

b) Use of Exchange Traded Funds (ETFs) as benchmarks (PM)

We noted instances where PMs used ETFs as benchmarks to compare to the PM's investment strategy or performance. We did not identify concerns with the use of ETFs as benchmarks provided that the ETFs used were comparable to the PM's investment strategy and were accompanied by sufficient disclosure to allow investors or clients to draw correct conclusions from the comparison. PMs must comply with their obligation to deal fairly, honestly and in good faith with their clients when presenting benchmarks, including ETFs as benchmarks, in their marketing materials.

PMs should:

- ✓ use ETFs that provide a meaningful and relevant comparison to their investment strategy
- ✓ provide sufficient disclosure to accompany the presentation of the ETFs as benchmarks, including:
    - the full name of the ETF, and if using a blended benchmark, the specific weighting of each component ETF within the blended benchmark

- an explanation of the material differences between the ETF as a benchmark and the investment strategy
- the reason ETFs are used rather than the underlying indices tracked by the ETFs, and disclosure that ETF tracking errors may result in a difference between the benchmark returns and the returns of the underlying indices
- whether the ETF returns used are gross or net of fees and other costs, and, if net of fees, the ETFs' expense ratios
- if ETF returns are based on market prices or net asset values
- any other information necessary to make the comparison fair and meaningful

Legislative reference and guidance

- The Act, s. 44(2) *Representation prohibited*
- OSC Rule 31-505, s 2.1(1) *General Duties*
- CSA Staff Notice 31-325 - *Marketing Practices of Portfolio Managers*

c) Inadequate policies and procedures on the review and approval of marketing materials (All)

We continue to identify firms with inadequate policies and procedures governing:

- the preparation, use and approval of marketing activities
- the independent review and approval of marketing materials

We also noted that some firms did not adhere to their own policies and procedures on marketing practices.

Registrants must establish, maintain and apply policies and procedures to establish an effective system of controls and supervision to ensure compliance with securities legislation and manage risks associated with their business in accordance with prudent business practices.

Registered firms should:

- ✓ establish, maintain and apply clear policies and procedures that are tailored to their marketing activities
- ✓ prior to dissemination of the marketing materials, establish controls to ensure that marketing materials are adequately reviewed and approved by an independent individual other than the preparer
- ✓ have processes in place to verify that policies and procedures related to marketing practices are adhered to

Legislative reference and guidance

- NI 31-103 and related NI 31-103CP, s. 11.1 *Compliance system and training*
- CSA Staff Notice 31-325 - *Marketing Practices of Portfolio Managers*

d) Unsubstantiated claims in marketing materials (All)

We identified instances where registered firms included claims or statements in their marketing materials that were unsubstantiated. A marketing claim or statement is considered unsubstantiated if there is inadequate evidence to verify the claim.

Registered firms must ensure that all claims or statements included in their marketing materials are supported by facts to substantiate or validate each statement made.

Registered firms should:

- ✓ maintain adequate support to substantiate claims or statements made in their marketing materials
- ✓ provide adequate references to the information supporting the claims or statements to allow investors to assess the merits of each claim
- ✓ ensure the claims are reviewed and approved by an individual independent of the preparer prior to their use in marketing materials
- ✓ have written policies and procedures to address all the above

Legislative reference and guidance

- The Act, s. 44(2) *Representation prohibited*
- OSC Rule 31-505, s. 2.1(1) *General Duties*
- NI 31-103 and related NI 31-103CP, s. 11.1 *Compliance system and training*
- CSA Staff Notice 31-325 - *Marketing Practices of Portfolio Managers*

2.2.9 Limitation of liability clauses (PM)

We noted registrants are including language in IMAs and other disclosure documents that attempts to limit the liability of the registrant or its representatives in its dealings with clients.

In some cases, registrants attempted to limit their liabilities to losses caused by breaches of securities laws. A provision of this kind could be interpreted as placing the onus on the client to prove a breach of securities law before a registrant can be found liable, which may require a finding by a regulatory tribunal, and implies that the registrant is not liable for negligence, willful misconduct, or bad faith conduct. In addition to securities laws, there may also be other regulatory or statutory requirements that apply to a registrant's business.

In other cases, registrants attempted to expressly exclude liabilities due to losses caused by their negligence or other material failures that are within their control.

These kinds of liability clauses are not consistent with normal expectations that a client would have with respect to a managed account relationship, and they are contrary to the standard of care under Ontario securities law, which is for registrants to deal fairly, honestly and in good faith with their clients.

PMs should:

- ✓ implement policies and procedures for the drafting, review and approval of disclaimers or other limiting clauses prior to their use, to ensure that they do not inappropriately purport to limit liability for losses, including losses resulting from negligence, willful misconduct or bad faith conduct
- ✓ remove inappropriate disclaimer language from the IMA and/or other disclosure documentation
- ✓ where previously disclosed disclaimer language has been removed, send a letter to all existing clients who had previously received the language to advise them that the language has been removed and that the registrant would not seek to rely on any inappropriate limitation of liability

Legislative reference and guidance

- OSC Rule 31-505, s. 2.1 *General Duties*
- OSC Staff Notice 33-740 *Report on the Results of the 2012 Targeted Review of Portfolio Managers and Exempt Market Dealers to Assess Compliance with the Know-Your-Client, Know-Your-Product and Suitability Obligations*, page 4
- OSC Staff Notice 33-747 *2016 Annual Summary Report for Dealers, Advisers and Investment Fund Managers*, page 39

2.2.10 Inadequate policies and procedures (All)

During our reviews, we often noted instances where firms did not have a written policies and procedures manual that was appropriately tailored to their operations and adequately covered the processes and procedures that the firm should have in place to establish an adequate compliance system. The written manual also did not reflect the changes to the firm's policies and procedures as a result of changes in securities law (e.g. changes as a result of the CFR amendments).

Generally, we found written policies and procedures to be lacking in the areas of:

- marketing, particularly the review and approval process for marketing material, use of benchmarks, presentation of hypothetical information and use of social media
- conflicts of interests including the process to identify material conflicts, implement controls to address the material conflict in the best interest of clients and disclose the material conflicts as required
- risk management including cyber security and business continuity plans

Other common areas where firms' written policies and procedures did not contain sufficient details included:

IFM activities

- fund accounting including detailed valuation policies, NAV error treatment, expense policies and oversight of service providers
- transfer agency including reconciliation of units outstanding and oversight of service providers
- trust accounting and oversight of service providers
- detailed policies on the firm's process to comply with NI 81-102 and NI 81-105 where applicable

PM activities

- KYC and suitability including timely updating of KYC information, documentation to support suitability of trades and communicating with vulnerable investors
- portfolio management including supervision of registered representatives and oversight of portfolios
- client reporting including account statements, additional statements, report on charges and other compensation, and investment performance reports
- trading and brokerage including selection of brokers, trade error policy and best execution

EMD activities

- KYC and suitability including when KYC information is to be updated and communicating with vulnerable investors
- how the firm uses different prospectus exemptions
- suitability including the use of internal concentration thresholds
- Know-your-product (**KYP**) including product review and due diligence process

Registered firms should:

- ✓ establish, maintain and apply policies and procedures that are tailored to their respective business operations to establish a system of controls and supervision
- ✓ have a process in place to ensure that written policies and procedures are regularly updated for changes in the firm's business operations, industry practice and securities law

Legislative references and guidance

- NI 31-103 and related NI 31-103CP, s. 11.1 *Compliance system and training*
- OSC Staff Notice 33-745 *2014 Annual Summary Report for Dealers, Advisers and Investment Fund Managers*, pages 43-44
- OSC Staff Notice 33-749 *2018 Annual Summary Report for Dealers, Advisers and Investment Fund Managers*, pages 36-40
- OSC Staff Notice 33-752 *2021 Summary Report for Dealers, Advisers and Investment Fund Managers*, page 21

2.2.11 Cyber security risks (All)

Cyber security risks to registered firms continue to be a concern. Staff are aware of instances where a scammer designed and posted marketing material on the internet, which was intended to fool investors and clients into visiting a malicious website, that looked similar to a registered firm's website.

Staff found many firms to be deficient in preparing for the risk of cyber attacks and cyber incidents.

Specifically, staff found that firms did not have or had inadequate:

- written policies and procedures for protecting the firm's electronic devices and networks
- assessment of the data and systems the firm needed to protect and the controls in place to protect these areas
- documented incident response plan to address cyber security incidents

Registered firms should:

- ✓ document policies and procedures to address:
  - use of electronic communications (e.g. types of information that may be collected or sent through email)
  - use of firm-issued electronic devices
  - loss or disposal of an electronic device
  - use of public electronic devices or public internet connections to remotely access the firm's network and data
  - detection of unauthorized internal or external activity on the firm's network or electronic devices (e.g. hacking attempts)
  - updating software, including anti-virus programs, in a timely manner
- ✓ regularly conduct a risk assessment and inventory of information and systems that require protection and outline the controls to protect these areas
- ✓ adequately train staff, as they are the first line of defense against an attack
- ✓ document an incident response plan to prepare for a cyber security attack or incident

Legislative reference and guidance

- NI 31-103 and related NI 31-103CP, s. 11.1 *Compliance system and training*
- CSA Staff Notice 33-321 *Cyber Security and Social Media*
- CSA Investor Alert: *Investment scams imitating well-known financial brands*

2.2.12 Registration and Commission filings

a) Changes in business activities or organizational structure – impact and obligations (All)

Changes to a firm's business activities or organizational structure are required to be reported using Form 33-109F5 to update previously reported information.

For example, changes to a firm's business, a revised description of the business activities, target market, or products and services may need to be provided to update information previously provided in item 3.1 of Form 33-109F6. In some cases, staff may ask for a revised business plan to better understand the change to the business.

While NI 33-109 requires that this information be provided within a set time frame after the change, certain changes may impact the firm's overall suitability for registration, such as changes in ownership or business activities. In some cases, additional filings are required from the firm, and these filings are required in advance of the change (e.g. a change in ownership resulting in a new major shareholder may require a filing under section 11.9 or section 11.10 of NI 31-103).

We encourage firms to contact staff in advance of a change to assist staff in understanding the change, and if additional steps are necessary, to verify the firm remains suitable for registration after the change has occurred. Staff may ask for additional information or documents to assess the firm's ongoing suitability for registration.

Registered firms that plan to establish, manage, advise and/or trade in securities of investment funds with portfolios of crypto assets and/or to facilitate transactions relating to crypto assets may need to report changes in their business activities by filing a Form 33-109F5 and updating information previously reported in item 3.1 of Form 33-109F6 to include a description of the crypto asset products and/or services. Staff will review the information provided and analyze the proposed product(s) or services. In some cases, we may impose terms and conditions on the firm's registration to ensure adequate investor protection.

With respect to new firm registration applications, significant changes to a firm's business activities, organizational structure or key personnel during the application process may contribute to delays in the review process. Depending on the extent of the changes, these applications may be considered non-routine applications. During the application review process, any significant changes which have been made to the original application (i.e. Form 33-109F6 and/or Form 33-109F4) should be communicated to staff on a timely basis and before registration is granted.

b) Time-limited relief granted to foreign broker-dealer to provide outsourced trading service to Canadian asset managers (EMD)

In April 2022, CRR staff, in consultation with staff from the Market Regulation Branch and staff from IIROC, finalized an application for time-limited dealer registration relief by a United States (**U.S.**) registered broker dealer (the **Filer**) that sought to provide an "outsourced trading service" (the **trading service**) to asset managers in Canada to assist the asset managers in achieving best execution.

The trading service involves the communication of trade orders relating to Canadian securities received from asset managers to their executing broker-dealers for execution, clearance and settlement but does not include the execution of trades in securities. Execution of trades in securities of Canadian issuers are made by executing brokers that have an existing relationship with the asset managers.

Prior to the granting of the relief, the Filer was able to provide its trading service to asset managers in Canada in relation to transactions involving foreign securities and certain debt securities of Canadian issuers but not Canadian equity securities in reliance on the international dealer exemption in section 8.18 of NI 31-103. The Filer sought exemptive relief by analogy to the "prime services" line of decisions to be able to provide its trading service for all types of securities to Canadian asset managers.

The relief was granted based on the regulatory framework established in the U.S. for this type of service and on the basis of the additional terms and conditions set out in the relief. Asset managers that use this type of service are reminded they must be able to reasonably conclude that the use of this type of service is consistent with the firm's best execution and conflicts of interest obligations and must comply with all disclosure requirements applicable to these types of services, including Part 4 of NI 23-102. A three-year sunset clause was included to allow OSC staff, in consultation with IIROC and CSA staff, to review our experience with filers offering this type of service. OSC staff continue to view this type of business model as novel and filers seeking to provide outsourced trading services in relation to securities and/or exchange-traded derivatives (commodity futures contracts and commodity futures options) and over-the-counter (OTC) derivatives are encouraged to make a pre-file with staff.

For more information, see Re Meraki Global Advisors LLC dated April 11, 2022.

Legislative reference and guidance

- NI 31-103 and related NI 31-103CP, s. 8.18 *International dealer*
- NI 23-101, s. 4.2 *Best execution*
- NI 23-102, Part 3 *Commissions on Brokerage Transactions* and Part 4 *Disclosure Obligations*

c) Unregistered individuals conducting registerable activities at investment consulting firms (PM / EMD)

Staff conducted reviews of registered firms operating with an investment consulting services business model. These firms typically advise institutional clients (e.g. pensions, foundations, etc.) on asset allocation strategy and portfolio manager selection, and perform oversight of portfolio managers.

During our reviews, we noted some consultants were conducting activities similar to advising representatives (**ARs**) at the firm, but they were not appropriately registered. These activities included:

- dealing directly with clients
- responding to and presenting requests for proposals
- providing investment advice and/or investment options to clients
- assisting clients in the development of investment policy statements

We raised concerns that these firms were not adequately supervising their unregistered consultants. A firm should apply consistent criteria when assessing whether AR or associate advising representative (**AAR**) registration is required for its consultants, and not allow unregistered consultants to conduct registerable activities. Once the firm is registered, it must have adequate procedures and controls in place to ensure that all individuals are appropriately registered.

In last year's summary report, we provided information on how individuals acting solely as client relationship managers (**CRMs**) can choose to register as an AR specializing in CRM activity.

PMs and EMDs should:

- ✓ take adequate steps to understand and comply with the registration requirements in Ontario by consulting compliance and/or legal advisors before commencing registerable activities in Ontario
- ✓ have adequate internal controls in place to ensure that only registered individuals are performing duties related to the firm's obligations as a registrant
- ✓ provide adequate training to employees on the registration requirements in Ontario

Legislative reference and guidance

- The Act, s. 25 *Registration*
- NI 31-103 and related NI 31-103CP, s. 11.1 *Compliance system and training*
- NI 31-103CP, s. 1.3 *Fundamental concepts*
- *Client Relationship Management specialists*, webpage on osc.ca
- CSA Staff Notice 31-332 *Relevant Investment Management Experience for Advising Representatives and Associate Advising Representatives of Portfolio Managers*

- OSC Staff Notice 33-750 *2019 Summary Report for Dealers, Advisers and Investment Fund Managers*, pages 27-28
- OSC Staff Notice 33-752 *2021 Summary Report for Dealers, Advisers and Investment Fund Managers*, pages 12-13

d) Inadequate supervision of ARs and/or AARs (PM)

We noted a number of cases where a PM firm did not adequately supervise its ARs and/or AARs.

In one case, a PM's sole AR failed to supervise the activities of the firm's only AAR. For example, the firm did not:

- establish adequate policies and procedures to supervise the firm's AAR
- maintain evidence that the AR pre-approved investment decisions that the AAR had made for clients' managed accounts
- perform due diligence to fully understand the structure, features and risks of each trade suggested by the AAR
- establish personal trading policies and procedures requiring the AAR to obtain pre-clearance for personal trades and submit brokerage statements for review
- provide training to the AAR so they understood the limitations of their role

Without adequate supervision, the AAR was able to provide investment advice to clients through verbal and electronic communications without first obtaining pre-approval of the investment decisions.

PMs are required to maintain a control and supervisory system sufficient to ensure compliance with securities law and to manage business risks. A PM's system of control and supervision should apply to all firm individuals acting on its behalf (i.e. ARs, AARs, unregistered individuals) and ensure individuals do not act independently of the firm's system of controls and supervision.

PMs should:

- ✓ establish controls to monitor the activities of the firm's ARs and AARs which include:
  - client onboarding and servicing
  - KYC and KYP
  - outside business activities reporting
  - social media use
  - personal trading
- ✓ develop procedures that outline how ARs responsible for supervising the advice of AARs will document their pre-approval of the AAR's advice
- ✓ train registered staff on the activities they are permitted to perform (and restrictions, if applicable) under their category of registration

Legislative reference and guidance

- The Act, s. 25(3) *Registration, advisers*
- The Act, s. 32(2) *Duty to establish controls, etc.*
- NI 31-103 and related NI 31-103CP, s. 4.2 *Associate advising representatives – pre-approval of advice*
- NI 31-103 and related NI 31-103CP, s. 11.1 *Compliance system and training*
- OSC Staff Notice 33-742 *2013 OSC Annual Summary Report for Dealers, Advisers and Investment Fund Managers*, pages 49-51

e) Common mistakes when filing Form 13-502F4 (All)

As required by Part 3 of OSC Rule 13-502, a registrant firm or an unregistered capital markets participant must, by December 1 in each year, file a completed Form 13-502F4 showing the information required to determine the participation fee.

A desk review of a sample of Form 13-502F4 conducted each year revealed some common mistakes made by firms.

Firms based their calculation on the wrong financial year

"Previous financial year" means the financial year ending in the current calendar year. For example, if the Form 13-502F4 is due December 1, 2022, firms should be using their financial year ending in 2022. If a firm's annual financial statements for a previous financial year are not completed by December 1, then a good faith estimate is used to complete Form 13-502F4. If a registrant firm's or an unregistered capital markets participant's participation fee, determined within 90 days after the end of its previous financial year, is less than the amount paid on December 31 then the firm or participant is entitled to a refund from the Commission of the excess fee paid. The request for a refund must be made within 90 days after the end of its previous financial year.

Form was not completed in thousands (000's) or in Canadian dollars

Dollar amounts should be entered in thousands and foreign currency balances should be translated to Canadian dollars using the Bank of Canada's exchange rate at the date of the filing or December 31st (whichever is later).

Incorrect application of the Ontario percentage definition

The definition of "Ontario percentage" is set out in section 1.1 of OSC Rule 13-502 and specifies that for firms with:

- a permanent establishment in Ontario and no permanent establishment elsewhere - must use 100%
- a permanent establishment in Ontario and elsewhere - the Ontario percentage is calculated based on taxable income earned in the year in Ontario (utilizing Schedule 5 of the firm's corporate income tax return)

- no permanent establishment in Ontario - the Ontario percentage is based on total revenues attributable to capital market activities in Ontario

Deductions were incorrectly made for non-Ontario revenues

Deductions were incorrectly made for non-Ontario revenues and instead a net revenue was reported on line 1 of Form 13-502F4, then an Ontario percentage less than 100% was applied, over-diluting the Ontario revenue. We remind firms that:

- Gross revenues must be reported under line 1 of Form 13-502F4 and align to the firm's gross revenues as shown in their financial statements or earned from all the firm's activities. For unregistered capital markets participants, line 1 of Form 13-502F4 is typically the firm's global revenues.
- The Ontario specific percentage must be calculated in accordance with the definition set out in section 1.1 of the OSC Rule 13-502 (see above).

Some firms also made inappropriate deductions under line 4, line 5 and/or line 6 of Form 13-502F4. These deductions are to prevent double counting of revenues for the purposes of calculating capital markets participation fees and are only allowed as a deduction when the firm pays these to another registrant firm or unregistered exempt international firm that include these fees as revenues in their Form 13-502F4.

We highlight the importance of accurate and timely fee calculations as there are deadlines which impact the firm, including:

- Registrant firms and unregistered capital market participants must, by December 31 of each year, pay the calculated fee.
- If an estimate was made for the Ontario specific revenues, firms must file a completed Form 13-502F4 and Form 13-502F5 and pay any amounts owing or request a refund for any overpayment no later than 90 days after the end of the previous financial year.
- Late filing of the Form 13-502F4 and late payment will subject the firm to late fees calculated in accordance with OSC Rule 13-502. The Commission and the Director will, in appropriate circumstances, consider tardiness in the payment of fees on whether the firm is suitable for registration.

Legislative reference and guidance

- OSC Rule 13-502
- Form 13-502F4
- Form 13-502F5

f) Tips for using the 11.9 and 11.10 standard form (All)

In February 2021, CRR staff published a template form that can be used for notices of acquisition that are required to be filed pursuant to sections 11.9 or 11.10 of NI 31-103. The purpose of the template notice was to make it easier for firms to prepare and submit the notice, and to provide direction on the type of information staff typically require when reviewing transactions. Several template notices were

filed this fiscal year, and in general, the form has worked well to provide the information necessary to complete a review. However, we identified instances where filers did not provide sufficient information in the template form to enable staff to complete a review. While the template is drafted to focus on key information, some filers did not provide sufficient detail in response to the standard form questions, which then required staff to contact filers with follow up questions.

If firms intend to use the template form, they must ensure that all sections are completed and that all parties to the transaction are referenced in the appropriate sections of the form, with all requested information provided. In addition, where there is space for additional text, firms should provide sufficient detail to describe the requested information. One word or overly abbreviated answers may not be clear enough for staff to understand the response and could result in follow up questions and delay our review.

The template form can be accessed from the Registration forms and documents webpage (refer to "Exemptions and applications for exemptive relief") on the OSC website.

Part 3: Initiatives impacting registrants

3.1 Client Focused Reforms

The CFRs introduced significant enhancements to the registrant conduct obligations which came into force in two stages in 2021. The CFR conflicts of interest requirements came into force on June 30, 2021. The remainder of the CFR requirements (i.e. KYC, KYP, suitability and relationship disclosure information reforms) came into force on December 31, 2021. These amendments to NI 31-103 are relevant to all categories of registered dealer and registered adviser, with some application to IFMs. The CFRs have also been incorporated into SRO member rules and guidance. All registrants should have reviewed their operating practices and implemented changes necessary to bring themselves into alignment with the CFRs.

The CFRs demonstrate a shared commitment by the CSA and the SROs to changes that require registrants to promote the best interests of clients and put clients' interests first. The CFRs are based on the fundamental concept that, in the relationship between registrants and their clients, clients' interests must come first.

Registrants are now required to have a process in place for identifying material conflicts of interest that arise at both firm and individual registrant levels, including those resulting from compensation arrangements and incentive practices, and ensuring that those material conflicts of interest are addressed in the best interests of their clients. They are also required to have implemented the KYC, KYP, suitability and relationship disclosure information reforms. Among other things, this includes having a framework to put clients' interests first when making suitability determinations. Firms are required to operationalize changes in the areas of KYC and KYP to support the enhanced suitability determination requirements, collect sufficient information about a client, and ensure that products and services made available to clients are assessed, approved and monitored for significant changes.

The CFRs Implementation Committee and your questions

The CFRs Implementation Committee, composed of staff from the CSA and the SROs, has published guidance on the CFRs FAQs webpage on operational issues and questions shared by industry stakeholders.

Implementation, compliance and enforcement

As outlined in our latest OSC Statement of Priorities, one of our priorities is ongoing compliance and oversight related to the implementation of the CFRs. The CSA and SROs are conducting reviews to test for compliance with all CFR requirements, including a targeted sweep of registered firms' compliance with the conflicts of interest amendments and identifying where processes need improvement. As with all registrant conduct requirements, the compliance review process is supported by the appropriate regulatory actions along the compliance-enforcement continuum.

3.2 2022 Risk Assessment Questionnaire

In May 2022, firms registered with the OSC in the categories of IFM, PM, RPM, EMD and RD were asked to complete the 2022 RAQ, which consisted of questions covering various business operations related to the different registration categories. The RAQ is a fundamental component of the risk-based approach used to select firms for compliance or targeted reviews.

Each response in the RAQ is assigned a risk score which is aggregated up to the firm level. This is done to identify firms whose business activities we perceive to be of higher risk. This aggregate risk score is an input in determining whether a firm will be recommended for a compliance review. In addition, responses to the RAQ are aggregated based on areas of interest and firms are selected for review based on their responses to questions in these areas of interest.

We continue to modify the RAQ process based on feedback we receive from firms; this includes continuing to pre-populate certain non-financial information in the RAQ, based on a firm's previous responses, and enhancing security by requiring both the firm's CCO and UDP to each create their own unique account in our system to access the 2022 RAQ.

3.3 CSA amendments to enhance protection of older and vulnerable clients

Amendments to NI 31-103 came into force on December 31, 2021. These amendments are intended to enhance the protection of older and vulnerable clients by providing registrants with tools and guidance to address situations involving financial exploitation or diminished mental capacity of their clients.

Registrants can be in a unique position to notice signs of financial exploitation, vulnerability or diminished mental capacity because of the interactions they have with their clients and the knowledge they acquire through the client relationship. The CSA acknowledges that, in order to protect older and vulnerable clients, it is important to provide registrants with tools and guidance they can use or rely on to take action against financial exploitation and to address issues arising from a client's diminished mental capacity, while being mindful of the importance of upholding client autonomy. It is also important to provide clients with avenues and the autonomy to protect themselves in vulnerable situations.

The amendments strengthen protection of older and vulnerable clients through two main components:

Trusted Contact Person (TCP)

Registrants will be required to take reasonable steps to obtain the name and contact information of a TCP from individual clients, and written consent for the TCP to be contacted in specified circumstances (e.g. if the registrant has concerns about possible financial exploitation of a client who is vulnerable or about the client's

mental capacity to make decisions involving financial matters). A TCP does not have authority to make transactions on the account but is intended to be a resource to assist registrants in protecting a client's financial interests or assets in these circumstances. While clients are not required to identify a TCP in order to open an account, registrants will be required to take reasonable steps to obtain and update TCP information as part of the KYC process.

Temporary holds

The amendments create a regulatory framework for registrants who place a temporary hold on trades, withdrawals or transfers in circumstances where the registrant has a reasonable belief that there is financial exploitation of a vulnerable client or where there are concerns about a client's mental capacity to make decisions involving financial matters.

Legislation, guidance and resources

We encourage registrants to refer to sections 13.2.01 and 13.19 of NI 31-103 and the related NI 31-103CP for more information on these requirements.

On October 5, 2021, the OSC presented a webinar relating to the amendments entitled Regulatory Framework and Resources to Enhance Protection of Older and Vulnerable Clients. To review this webinar, please refer to the Regulatory Framework and Resources to Enhance Protection of Older and Vulnerable Clients webpage on the OSC website.

In addition, the OSC has developed resources to assist registered firms and representatives with addressing the needs of older and vulnerable investors. These white label materials, developed by the Investor Office at the OSC, are intended to be resources that firms may refer to or choose to adapt, brand and deploy, at their discretion, to support their interactions with older and vulnerable clients, which may mitigate the burden of developing materials entirely independently. The white label materials also include a form intended for registrants to adapt and provide to their clients, which may then be completed and shared by a client with their trusted contact person. The form lets the TCP know that they have been named as the client's TCP and provides the TCP with an overview of what this means, in addition to providing them with the registered firm and representative's contact information.

Please refer to the Working with older and vulnerable clients webpage on the OSC website to access these resources.

3.4 NI 33-109 amendments

Amendments to NI 33-109 came into force on June 6, 2022. The amendments establish a more efficient registration and oversight process for firms, individuals and regulators by simplifying and streamlining certain regulatory requirements. The changes also provide firms and individuals with greater clarity on the information

required as part of the registration process, while improving the quality of information received by regulators.

With NI 33-109 amendments coming into force, registrants must now update their information on NRD.

Some highlights from the amendments include:

- establishing a new framework for reporting outside activities to regulators
- codifying existing requirements regarding outside activities that are positions of influence
- extending some deadlines to report changes in registration information
- implementing a new rule to reduce multiple filings of the same information
- amending certain registration requirements to reduce common errors
- clarifying the language on certain forms
- updating and improving the privacy notice to provide greater clarity on how personal information is collected and used by the CSA and SROs
- implementing a new requirement to report the business titles and professional designations used by registered firms and individuals

The amendments are not intended to change the nature of the registration process, the requirement to register or the assessment of suitability for registration.

For additional information, please refer to:

- Implementation Guide to Amendments to National Instrument 33-109: *Modernizing Registration Information Requirements, Clarifying Outside Activity Reporting and Updating Filing Deadlines*
- FAQs (Annex C) included in the publication of the final amendments
- the Registrant Outreach webinar relating to the amendments entitled Amendments Modernizing Registration Information Requirements, Clarifying Outside Activity Reporting & Updating Filing Deadlines

3.5 Institutional Trade Matching and Settlement

As part of the OSC's efforts to reduce regulatory burden, amendments to NI 24-101 came into force July 1, 2020, and provide a three-year moratorium on the applicability of section 4.1. Specifically, the reporting requirements under section 4.1 of NI 24-101 do not apply to a registered firm beginning on July 1, 2020 and ending on July 1, 2023.

Notwithstanding the moratorium, registered firms must still comply with all other requirements in NI 24-101 including establishing, maintaining and enforcing policies and procedures to achieve the matching threshold for institutional trades.

NI 24-101 provides a framework for efficient and timely settlement processing of institutional trades by registered firms. The institutional trade matching

requirements apply to a PM that places a DAP/RAP trade[6] in an equity or debt security with a dealer for one or more of its clients with DAP/RAP trading privileges. Clients having DAP/RAP trading privileges typically include institutional clients such as investment funds and pension plans but may also include clients that are individuals.

For further information, please refer to the notice.

3.6 Virtual business locations on NRD

On September 7, 2022, we issued an e-mail blast to UDPs, CCOs and persons on the Registrant Outreach subscriber list that introduced flexibility for firms to create virtual business locations on NRD.

Virtual business locations will allow firms, under certain circumstances, to open a branch location in a province or territory (or region of a province or territory) on NRD. Registered and permitted individuals of a firm who are not otherwise assigned to a business location in the province or territory of their residence and are working from home can select as their location of employment the virtual business location using Item 9 *Location of employment* of Form 33-109F4.

For further information, please refer to the procedural guidance included in the email blast.

3.7 Exemption from underwriting conflicts disclosure requirements

On March 1, 2022, the OSC made as a rule under the Act OSC Rule 33-508 *Extension to Ontario Instrument 33-507 Exemption from Underwriting Conflict Disclosure Requirements* (the **Rule**).

The Rule extends the blanket relief issued on February 18, 2021 by Ontario Instrument 33-507 *Exemption from Underwriting Conflicts Disclosure Requirements (Interim Class Order)* (the **OSC Blanket Order**) by 18 months. The OSC Blanket Order ceased to be effective after August 17, 2022.

The OSC Blanket Order eliminates the underwriting conflicts disclosure requirements that would otherwise apply under Ontario securities law in circumstances where foreign securities are offered to institutional investors in Ontario as part of a global offering and thereby facilitates participation by institutional investors in Ontario in such global offerings. Specifically, the OSC Blanket Order provides an exemption from the underwriting conflicts disclosure requirements in NI 33-105 if:

- the distribution is made under an exemption from the prospectus requirement

[6] See the definition of "DAP/RAP trade" in section 1.1 of NI 24-101.

- the distribution is of a security that is an "eligible foreign security" as defined in NI 33-105
- each purchaser in Ontario that purchases a security pursuant to the distribution through such person or company is a "permitted client" as defined in section 1.1 of NI 31-103.

The OSC issued the OSC Blanket Order following discussions between CRR and Corporate Finance staff and various institutional investors who advised staff that the underwriting conflicts disclosure requirement in NI 33-105 created barriers that prevent institutional investors in Ontario from participating in global offerings on a timely basis.

The Rule causes the blanket relief provided in the OSC Blanket Order to be in force for an additional 18-month period from August 18, 2022 to February 17, 2024. OSC staff are continuing to review options for a more permanent solution and may propose an amendment to NI 33-105 at a later date.

Part 4: Acting on registrant misconduct

4.1 Annual highlights and trends

The Registrant Conduct Team is responsible for investigating conduct issues involving individual and firm registrants, recommending regulatory action where appropriate, and conducting opportunity to be heard (**OTBH**) proceedings before the Director.

Before a Director of the OSC imposes terms and conditions on registration, refuses an application for registration, or suspends a registration, an applicant or registrant has the right under section 31 of the Act to request an OTBH before the Director. A registrant or applicant may also request a hearing and review by the Capital Markets Tribunal (the **Tribunal**) of a Director's decision under section 8 of the Act.

Identifying and acting on registrant misconduct

Potential registrant misconduct is identified through compliance reviews, applications for registration, disclosures on NRD, and by other means such as complaints, inquiries or tips. CRR staff also identifies registrant misconduct through background and solvency checks on individual registrants or individual applicants, responses to the RAQ, and referrals from SROs and other organizations.

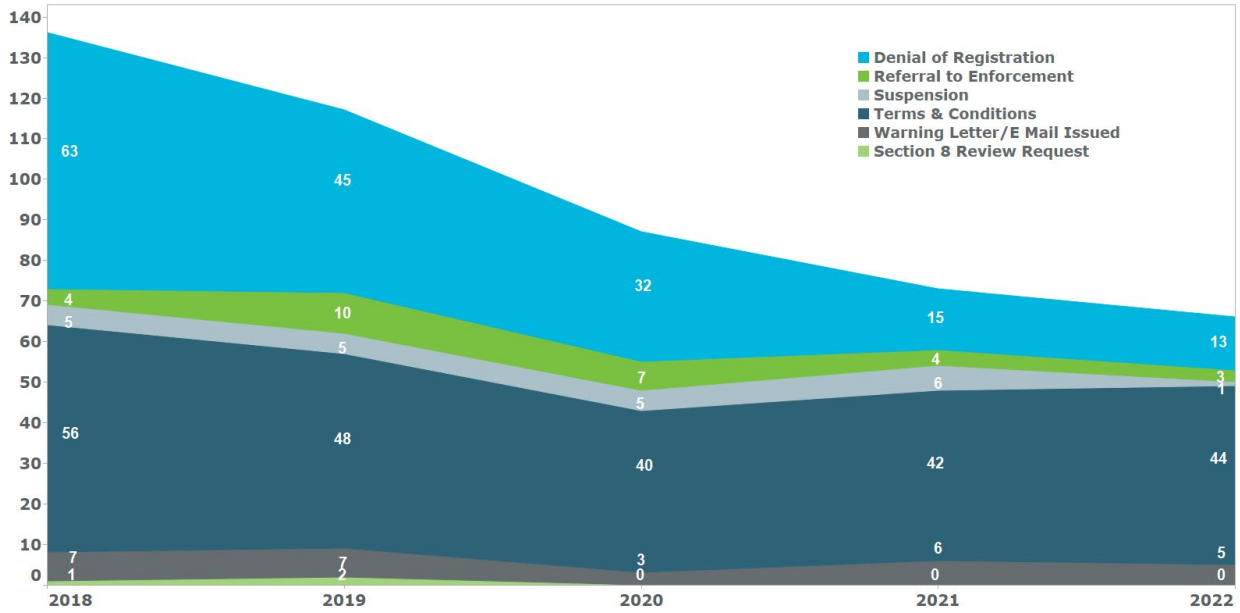
Acting on registrant misconduct matters is central to effective compliance oversight. It also promotes confidence in Ontario's capital markets, both among the investing public and among the registrants who make best efforts to comply with Ontario securities law. Registrants must remain alert and monitor for potential misconduct by enacting and implementing appropriate policies and procedures, and ensuring that controls are in place to detect and address instances of misconduct.

The Registrant Conduct Team is also responsible for overseeing terms and conditions on registered firms and individuals as a result of a regulatory decision, including a Director's decision or Tribunal Order (formerly, Commission Order). For registered firms, terms and conditions might require them to engage an independent compliance consultant or restrict business activity that is not compliant while remediation takes place. Terms and conditions might also require specific reporting by registered firms to the OSC.

In cases where there appear to be issues with an application that could bear on the individual's suitability for registration, such as past misconduct or untrue or misleading information given in the application itself, the file may be referred by the Registration Team to the Registrant Conduct Team for further investigation, requiring a longer review time. Each phase in the registration process when applications transition from the Registration Team to the Registrant Conduct Team are illustrated in this process chart.

The following chart summarizes the regulatory actions taken by CRR staff against firms or individuals engaged in registrant misconduct or serious non-compliance with Ontario securities law.

CRR Regulatory Actions FYE 2018 - 2022[7]



The chart illustrates that CRR makes use of regulatory actions along the compliance-enforcement continuum, the action being commensurate with the magnitude of misconduct or non-compliance in a given situation. Terms and conditions, denials of registration, and suspensions or revocations of registration are all tools available to CRR staff to address serious non-compliance.

While most categories of CRR regulatory actions have remained fairly constant, there were fewer denials of registration and suspensions in fiscal 2021-2022. For firms, staff will sometimes use business restrictions and other terms and conditions to permit a firm which engaged in significant non-compliance to remediate its deficiencies. For individuals, sponsoring firms will occasionally make a business decision to dismiss registered individuals when they become aware of misconduct being investigated by staff. Ultimately, staff remains committed to taking timely and effective regulatory action where misconduct is identified, and will recommend suspension or revocation of registration, subject to a registrant's right to request an OTBH before the Director, when warranted.

Staff continued to identify non-disclosure of material information by applicants and registrants, including instances where solvency events such as bankruptcies, requirements to pay and consumer proposals were not disclosed. Under the amendments to NI 33-109, we have updated our forms to further clarify that consumer proposals are among the financial events that are required to be disclosed, and that any relevant solvency events must be disclosed regardless of

[7] Figures for 2020 have been revised to correctly include the regulatory actions for the 2019-2020 fiscal year.

how long ago they occurred. We anticipate that these updates will reduce the number of undisclosed solvency events in registration applications.

Although the most common concern with individual applicants and registrants is non-disclosure of material information, a significant number of files were opened based on dismissals for cause or other identified misconduct by individuals while registered with former sponsoring firms. In these cases, staff do not pre-judge applications, but will make inquiries of both the applicant and the former sponsoring firm to determine whether the identified conduct bears on the applicant's suitability for registration. Typically, staff will conduct an interview of the applicant before making a recommendation. The timely co-operation of registered firms in these investigations is both appreciated and vitally important (see section 4.3).

Referrals are made to the Enforcement Branch in cases where the appropriate tool is a power that can only be exercised by the Commission (now, the Tribunal). In fiscal 2021-2022, there were three referrals to the Enforcement Branch.

4.2 Prompt and effective regulatory action

Where appropriate, staff will recommend that terms and conditions be placed on the registration of a firm where staff has identified an inadequate compliance system, or an error or oversight that creates undue risks or losses for its clients. These are situations where a firm is not unsuitable for registration such that staff will recommend suspension, but where terms and conditions are nonetheless necessary to protect investors and remediate identified compliance deficiencies.

Over the past fiscal year, staff obtained, on consent, several sets of innovative terms and conditions designed to address complex compliance concerns. These terms and conditions have been drafted to increase the likelihood of compliance remediation succeeding, to the benefit of present and future clients; while promoting fairness in the capital markets.

Some examples of novel terms and conditions imposed on consent include:

- **Addressing unregistered advising:** A firm partnered with unregistered entities to provide portfolio management services. Terms and conditions were imposed which required the registered firm to execute new agreements with its partner firms clarifying that registerable activities, marketing, trade names and fee schedules would be handled solely by the registered firm and its registered individuals.
- **Addressing unregistered dealing:** A firm dealt with Canadian clients through a non-Canadian affiliate before becoming registered in Canada. Terms and conditions were imposed upon the firm being registered that required the firm to contact Canadian clients to ensure that they transferred their accounts to the registered firm, or closed the accounts by either

liquidating the account's assets or transferring the assets to another registered dealer in Canada.

- **Addressing inadequate documentation of client-directed trades:** A firm improperly relied on client-directed trades. Terms and conditions, requiring a consultant and monitor, specifically required the criteria for compliant client-directed trades to be adequately documented before the trades would be permitted to proceed.
- **Addressing repeat deficiencies:** Repeat compliance deficiencies were identified at a firm, despite a compliance consultant already revising the firm's policies and procedures. Terms and conditions were imposed which required the firm's UDP and CCO to both personally sign a monthly attestation on the firm's compliance in areas where the deficiencies were identified.

4.3 Timely cooperation with staff information requests

When individuals seek to reactivate their registration, staff considers the circumstances under which the individual ceased working for their prior sponsoring firm. In particular, terminations or departures following allegations of misconduct, whether or not the individual was dismissed for cause, can give rise to integrity and proficiency concerns. In those cases, the Registrant Conduct Team needs to examine the circumstances of a past termination or departure, in order to assess possible concerns and provide all the relevant information to the Director before a decision is made with respect to the individual's registration.

In addition to reviewing the information in the Notice of Termination, staff may seek additional details relating to the Notice of Termination, supporting documents or, in some cases, an opportunity to interview a firm's representative.

Staff expect registered firms to make reasonable efforts to ensure that the information included in Notices of Termination filed through NRD are truthful and complete. For example, for individuals that were dually employed by a registered firm and a parent financial institution or an affiliate insurance firm, the Notices of Termination sometimes include disclosure that an individual was terminated by the parent bank or the affiliate, with no further details provided. Firms are required to make reasonable efforts to obtain additional details from the relevant parties and include them in the Notices of Termination.

Furthermore, it is important for firms to provide timely cooperation with staff's requests for further information and documents relating to a formerly sponsored individual's termination or departure. Failure by firms to cooperate can delay the review of applications for registration. Staff generally requests that the relevant information be delivered by a specified deadline, taking into consideration the nature and volume of information sought. All registered firms would benefit from firms promptly delivering requested information about formerly sponsored

individuals, so as to avoid unnecessary delays in reviewing present and future registration applications.

Staff acknowledges that firms may have privacy-related concerns with respect to providing personal information about formerly sponsored individuals. However, by submitting Form 33-109F4, applicants for registration consent to the collection by staff of personal information relevant to their application and their fitness for registration, including employment records and information obtained from an employer.

When staff is authorized to collect personal information, it is for the purpose of carrying out its duties and exercising its powers under securities legislation and/or derivatives legislation (including commodity futures legislation). The collection, use and disclosure of personal information are done in accordance with applicable freedom of information and privacy legislation.

We request that firms voluntarily provide termination information with respect to formerly sponsored individuals. However, staff can compel this information, if necessary, under authority provided in the Act. For example, the Director has broad authority under section 33.1 of the Act to require information to be submitted by a registrant within a specified time. In addition, section 19 of the Act requires market participants, including registered firms, to keep various books, records and other documents and to deliver them to the OSC at the specified time.

4.4 Director's decisions and settlements

Director's decisions on OTBH proceedings are published in the OSC Bulletin and on the OSC website at Opportunity to be heard and Director's decisions, where they are presented by topic and by year. Director's decisions can be used as an important resource for registrants, as they highlight matters of concern to the OSC, as well as the regulatory action that was taken as a result of misconduct and non-compliance. The publication of Director's decisions also ensures that CRR's response to serious misconduct is visible to market participants and investors.

Four Director's decisions were published in the fiscal year 2021-2022 on registrant conduct issues. There were no contested OTBHs. One decision was issued where the registrant did not request an OTBH, and three decisions approved settlement agreements between staff and the registrant. A settlement agreement typically contains an agreed statement of facts and a joint recommendation to the Director. Proceeding by way of a settlement agreement with staff allows the registrant to participate in setting out the factual narrative that becomes the basis for the Director's decision.

A summary of all Director's decisions and settlements by topic published since the decisions and settlements included in last year's summary report follows.

Firminvest Asset Management Canada Inc. and David Ratcliffe (February 25, 2022)

Topics: Compliance system and culture of compliance; Duty to supervise

Firminvest Asset Management Canada Inc. (Firminvest), a PM firm, through its UDP/CCO/sole AR David Ratcliffe, entered into a memorandum of understanding (MOU) with a Swiss asset manager with clients in Ontario and elsewhere in Canada. Pursuant to this MOU, the Swiss entity introduced its Canadian clients to Firminvest for discretionary portfolio management services in return for a stipulated fee. Through the MOU, the Swiss firm purported to retain the client-adviser relationship with all introduced clients. A partner of the Swiss firm became registered as an AAR with Firminvest and advised the introduced clients without appropriate oversight by Ratcliffe. In a settlement agreement approved by the Director, Firminvest's registration is to be revoked after an appropriate transition period, and Ratcliffe's registration as UDP/CCO was suspended for 4 years, but he was permitted to continue as an AR under the supervision of a different registered firm. In the settlement agreement, Ratcliffe admitted that he did not discharge his suitability obligations or his obligations as UDP/CCO.

Gross Securities Corp. (October 15, 2021)

Topic: Failure to comply with Director's summons

The UDP of Gross Securities Corp. (Gross) was served with a summons issued by the Director requiring him to attend an examination under oath regarding bankruptcy proceedings involving an entity related to Gross. Staff sought to conduct this examination because certain allegations were relevant to the firm's ongoing suitability for registration. Counsel for the UDP informed staff that he had concerns about the UDP attending the examination because, among other reasons, the examination might elicit testimony regarding issues relating to the bankruptcy proceedings, but that testimony was not the subject of any statutory confidentiality protection. The Director suspended Gross on the basis that the firm's ongoing registration was objectionable since the proposed examination did not occur.

John Kodric (September 2, 2021)

Topics: KYC, KYP, and suitability; Outside business activity (including off-book dealing); Rehabilitation of fitness for registration; Trading or advising without appropriate registration

John Kodric applied to reactivate his registration as a mutual fund dealing representative. In 2015, the Director issued a decision with respect to Kodric's prior application to reactivate his registration. In that decision, the Director refused the registration but also found that Kodric may be suitable for registration in the future subject to: (a) terms and conditions (including strict supervision by Kodric's sponsoring firm and prohibiting the use of leverage); (b) Kodric demonstrating remorse for the misconduct set out in the 2015 Director's decision; and (c) Kodric demonstrating that he has taken courses to better understand his obligations as a registrant.

Staff found that Kodric met the specified requirements and recommended that his registration be granted subject to terms and conditions of strict supervision and prohibiting the use of leverage, consistent with the 2015 Director's decision. Kodric consented to the recommended terms and conditions of registration.

Michelle Kamerman (June 14, 2021)

Topic: Conflicts of interest

Michelle Kamerman was a mutual fund dealing representative working in a financial planning office owned by John Doe[8], another dealing representative. Kamerman's primary responsibility was to assist John Doe in the management of his book of business. John Doe engaged in personal financial dealings with some of his mutual fund clients, and Kamerman facilitated some of those dealings and did not report them to John Doe's firm. John Doe and Kamerman resigned from their sponsor firm and applied to reregister with another firm. The Director approved a Settlement Agreement pursuant to which Kamerman would not be registered for a period of six months and would be subject to certain supervisory terms and conditions upon her re-registration.

Ardenton Financial Inc. (March 15, 2021)

Topic: Compliance with securities laws of foreign jurisdictions

Ardenton Financial Inc. (Ardenton Financial) was registered under the securities laws of all of the provinces of Canada. The British Columbia Securities Commission (BCSC) was its principal regulator. On March 8, 2021, the BCSC suspended the firm's registration with Ardenton Financial's consent, after the firm reported to the BCSC that it had ceased conducting registrable activities because a related firm, Ardenton Capital Corporation, the source of Ardenton Financial's income, had petitioned for protection from its creditors under the Companies' Creditors' Arrangement Act on March 5, 2021.

Staff recommended to the Director that the firm also be suspended in Ontario due to the regulatory action taken by the principal regulator. The firm advised staff that it had no objection to the proposed regulatory action and the Director suspended the firm on the basis that it would be objectionable for the firm to remain registered in Ontario when its registration was suspended in all other Canadian jurisdictions where it was registered.

[8] For privacy reasons and in the published Director's Decision, this individual was referred to as "John Doe" to protect their identity.

OSC ONTARIO SECURITIES COMMISSION

Contact us

OSC Inquiries and Contact Centre

8:30 a.m. to 5:00 p.m. Eastern Time, Monday to Friday

1-877-785-1555 (Toll-free)

416-593-8314 (Local)

inquiries@osc.gov.on.ca

You can also use our online form located on the Contact us webpage on the OSC website:

www.osc.ca

If you have questions or comments about this report, please contact:

Lisa Piebalgs

Accountant

Compliance and Registrant Regulation

lpiebalgs@osc.gov.on.ca

(416) 593-8147