Submission of the Investment Dealers Association of Canada

(IDA)

to

the Commission des finances publiques (Committee on Public Finance)

Within the framework of its order of initiative entitled
“La protection des épargnants au Québec” (The Protection of Investors in Québec)

National Assembly of Québec

January 2006

Commission des finances publiques

Order of Initiative

"Protection of Investors in Québec"

Mr Chairman:
Mr. Vice-Chairman:
Committee Members:

The Investment Dealers Association of Canada (the "IDA") is pleased with the continuing interest shown by the Québec National Assembly's Committee on Public Finance ("the Committee") in the functioning of the financial sector and capital markets. The Committee's work attests to the importance it assigns to this sector of the industry which is directly related to Québec's economic growth and development.

The IDA also applauds the Committee's constant concern for all issues related to the savings of investors, their investment activities and the recourses available to them.

Before addressing more specifically each of the "Issues to Be Debated" in the Consultation Document (the "Document") prepared by the Committee, allow us to make a few comments on the regulation of the financial sector.

The Committee, taking note of the recent episodes on our markets, has focused on the mutual funds sector.

The IDA regulates its members, unrestricted practice dealers, and, as such, it regulates their activities in the mutual funds sector. It does not regulate the mutual fund companies themselves–since the creation of the Mutual Fund Dealers Association ("MFDA"), in which it participated–but rather the sale of these products by its members.

What is important to note, however, is that the topics chosen by the Committee can be addressed on a broader basis than that of the mutual funds sector alone. Indeed, whether we are talking about regulation, supervision, penalties or governance, reference to what exists and any differences that can be highlighted are likely to support the Committee's reflection and provide some possible solutions.

Compensation Mechanisms

The Document refers to the Canadian Investor Protection Fund ("CIPF"). We feel that it would be useful to provide you with more information on its structure and functioning.

Indeed, the history and evolution of the CIPF are closely related to the evolution of our financial markets. The CIPF (called the National Contingency Fund ("NCF") at the time) was created in 1969 as a response to the self-regulating organization ("SRO") structure that the industry had created for itself, and to protect clients from a member's financial failure. Also, since firms could be members of different SROs at that time (in addition to the IDA, the Stock Exchanges had this status), the industry considered it essential to govern this issue from a Canada-wide perspective and offer the same protection to all clients wherever they were located.

In the 50s, for example, the total equity debt of clients was calculated based on the "delivery" date, whereas the bond sector characterized itself by interest rate risk. The creation of the NCF made it possible to standardize the regulatory capital of some 200 member firms of the IDA or of an Exchange ($150,000 of minimum capital, increased to $250,000 in 1990).

Over the years, there also developed the notion of "principal jurisdiction" of the SRO supervising a member and that of the "most severe rule", again with a view to ensuring that the minimal rules and resulting protection were the same everywhere.

In the 70s, after the computerization of the back-office systems in the 60s, weaknesses in these systems appeared due to the proliferation of new products, notably options and futures, hence the occurrence of new risks.

This is when another financial control was developed, namely the "Quarterly Operational Questionnaire", and risk quantification rules were adopted.

The 80s were marked by acquisitions, market globalization and dematerialization of securities. The capital formulas had to be changed to base them on the risks and responsibilities related to the firms' activities.

The 90s saw the development of "Wealth Management", the creation of Clearinghouses and numerous mergers. In an environment of increasing the returns on investment, the increased return had to be considered in relation to the increased risk. Here again, the new activities brought with them new operational risks.

It was, in fact, in 1990 that the NCF changed its name to the Canadian Investor Protection Fund ("CIPF"), in the wake of the Bean and Cherry Reports that

followed the bankruptcy of Osler Inc. in 1987 (30 million that dropped to 15 after the collection procedures). In the wake of these changes, internal control and documentation requirements were developed to monitor trading and ensure that the members maintain the various safeguards at all times.

The 2000s are witnessing big technological changes with the switch to “T + 1” for transaction settlement. These years should therefore open up new regulatory approaches. In particular, what is needed is a proactive approach based on knowledge of the market and its inherent risks. For a number of years, the IDA has been developing approaches and tools in this regard: standardized examination programs, technological systems that can combine and analyze globally the data collected on members activities, as well as a new assessment of the risk presented by each of the members, enabling the Association to target those more deserving of review or monitoring. This “Risk Report Trend” also allows better allocation of resources. All the rules and monitoring also promote the development of a strong compliance culture among the member firms.

At the moment, the minimum financial compliance standards cover the following aspects:

1. Capital: Requirements
    - Risk-adjusted capital maintained at all times (Joint Regulatory Financial Questionnaire and Report “JRFQ&R”)
    - Monthly calculation of capital position on the Monthly Financial Report “MFR”
    - Details of any capital deficiency identified and monitored

2. Client accounts
    - Account opening forms
    - Minimum margin amounts

3. Audits and questionnaires
    - Audits of JRFQ&R by external auditor
    - Review of external auditors’ worksheets

4. On-site examination
    - Always “surprise” visits
    - Reconciliation of financial documents
    - Review of classification of balances of counterparties
    - Review of valuation of securities and their negotiability for large positions
    - Review of partners and shareholders accounts – cash and margin rules
    - Review of client accounts
    - Review of operating controls and records

5. Written records – description – assessment of control systems

6. Books of account
    - Working copies of transactions
    - Order and confirmation files
    - General Ledger
    - Stock Record and Position Report
    - Clients' statements

7. Internal controls
    - Capital adequacy
    - Insurance
    - Segregation of clients' securities
    - Safeguarding of securities and cash
    - Pricing of securities
    - Derivative risk management

8. Segregation
    - Segregation of securities and cash – free credit balance ratio

9. Early warning system

The CIPF is an organization that is independent from the IDA, even though it was created by IDA member firms and is totally funded by them. The CIPF has its own Board of Directors with 12 members, 5 of whom represent the public. It also has its own staff who work regularly with IDA staff. The CIPF is a signatory in a "Coordination and Supervision Agreement", approved by the Regulators in 2001, which describes the examinations and controls that the IDA must apply and the reports to be submitted to these Regulators, including the AMF in Québec.

The CIPF currently relies on $325 million and $100 million in the form of lines of credit.

All IDA members must offer this protection to their clients who could suffer financial losses as a result of the bankruptcy or insolvency of a "dealer", i.e. of an IDA member firm. In addition, Québec regulations require that unrestricted practice dealers participate in an acceptable contingency fund (Securities Regulation c.V-1.1, r.1, Sect. 215). The principle underlying this protection is that the client can be reimbursed for any combination of cash and securities held in his account. It is, as it were, reimbursing the client for the contents of his account. If, for example, the insolvency were to occur as the result of fraud committed by a dealer member, the CIPF's protection would apply. This protection is for 1 million per account and could go as high as 2, 3 or 4 million depending on the number of accounts. The CIPF can consolidate some accounts for purposes of applying the coverage (cash, margins, Canadian – US dollars, RRSPs). It is also important to clarify that this one million-dollar coverage per account applies to the loss of value of the account which reduces the client's risk of loss even further.

This explains the importance that the IDA accords, in its member regulation and supervision activities, to the members' financial position and to maintaining constant risk adjusted capital, as well as to all the other financial compliance standards that it has developed jointly with the CIPF over the years. In addition to an annual financial compliance examination, the IDA exercises monthly controls (JRFQ&R) over its members' financial position.

Any breach of these rules automatically triggers corrective measures and additional controls which can even be daily, as well as sanctions that include financial penalties to which may be added the suspension of trading privileges or even ban. For instance, the early warning system, when it is triggered by a member, is financially costly and also entails a disciplinary measure.

This description of the protection provided to clients of IDA members is not clearly protection against fraud, but it does not exclude it if the bankruptcy or insolvency results from fraud or if this insolvency results from culpable defaults on the part of the officers.

Among the CIPF's major interventions since 1998 (Essex, Rampart and Thompson Kernaghan), two were the result of fraud.

In terms of client protection, the insurance covering the member's operations should also be reviewed. Under its rules, IDA members are required to have insurance covering a number of fields of operation. This insurance does not cover clients' losses that may result, but it does restore a firm's financial position and thus help to return it to where it is able to meet its obligations to these clients. The following excerpts describe the content of this insurance established by Regulation 400:

“400.2. Financial Institution Bond - Every Member shall, by means of a Financial Institution Bond or Bonds (with Discovery Rider attached or Discovery Provisions incorporated in the Bond), effect and keep in force insurance against losses arising as follows:

Clause (A) - Fidelity - Any loss through any dishonest or fraudulent act of any of its employees, committed anywhere and whether committed alone or in collusion with others, including loss of property through any such act of any of the employees;

Clause (B) - On Premises - Any loss of money and securities or other property through robbery, burglary, theft, hold-up or other fraudulent means, mysterious disappearance, damage or destruction while within any of the insured's offices, the offices of any banking institution or clearing house or within any recognized place of safedeposit, as more fully defined in the Standard Form of Financial Institution Bond (herein referred to as the "Standard Form");

Clause (C) - In Transit - Any loss of money and securities or other property (exceptions to be contained in a list to be approved by the Investment Dealers Association); while in transit, whether negotiable or nonnegotiable, shall be covered by insurance. The value of securities in transit in the custody of any employee or any person acting as a messenger shall not at any time exceed the protection provided under this clause;

Clause (D) - Forgery or Alterations - Any loss through forgery or alteration of any cheques, drafts, promissory notes or other written orders or directions to pay sums in money, excluding securities, as more fully defined in the Standard Form;

Clause (E) - Securities - Any loss through having purchased or acquired, sold or delivered, or extended any credit or acted upon securities or other written instruments which prove to have been forged, counterfeited, raised or altered, or lost or stolen, or through having guaranteed in writing or witnessed any signatures upon any transfers, assignments or other documents or written instruments, as more fully defined in the Standard Form.“

Thus, certain thefts or operational losses arising from crooked dealings committed by representatives or employees of member firms are covered by the insurance that the IDA requires its members to purchase. In addition, if the firm is no longer able to cover its clients' assets in any situation that creates insolvency, then the Fund's coverage will apply. The result is a mechanism that covers the scheming of both the firm and the individuals.

This description of the existing measures to protect the clients of IDA members does not mean that all their clients are protected against all fraud. The recent events mentioned in the Document reveal a level of plotting that may well set us wondering about the mechanisms protecting investors.

Our sole objective in this exercise is rather to clearly identify what exists in our industry, in order to identify some possible solutions, as desired by the Committee.

We are talking about protection against the fraudulent conduct of firms or individuals. It is important to identify the type of fraudulent conduct against which protection is being contemplated. In the universe of the IDA members, a loss of market value of an investment is not covered, even if this loss of value results from fraud. BreX is an eloquent example of this.

Some remedies will however be available to investors, when the investments do not match their investment objectives. Not only will the representative and the firm, if applicable, be liable for disciplinary action, but the client has a right of recourse to receive compensation. Depending on the circumstances, many IDA member firms will want to keep their good reputation and settle complaints of this nature. The IDA understands that exercising the right of recourse, even though it is available, is not always easy. This is why, in fact, it has developed alternative methods for resolving disputes.

The first method is arbitration, to which IDA member firms have been required to submit at a client's request since 1996. The time and fees involved ($3,000-$5,000) to obtain a final decision are considerably lower, compared to the traditional recourse in the courts of law. The maximum amount of a claim is $100,000.

Since 2001, the Ombudsman for Banking Services and Investments ("OBSI") has offered a free conciliation service for client claims of up to $350,000. In the same spirit of facilitating the process for clients, the service is optional for the client, but obligatory for the members. The Ombudsman publishes an annual report and statistics.

Based on these activities and the recent events that have drawn the attention of the Committee, it is evident that the risk of "issuers" for certain products is neither

regulated nor supervised. This could explain what seems to be a void with respect to investor protection, let alone the notion of redress.

As an example, the emphasis in the mutual fund sector is on the distribution of products rather than on their development. In Canada, the Canadian Mutual Fund Dealers Association (MFDA) created the Investor Protection Corporation (Fund) in 2002, the objective of which is to protect the clients of MFDA member firms in the event of bankruptcy. The terms of coverage and protection are fairly similar to those of the CIPF. The protection provided by the Fund began on July 1, 2005.

All the regulations of the CSA that explicitly address the mutual fund sector also deserve attention, from the standpoint of improving control over activities and seeking investor protection mechanisms.

The penalties

When addressing the issue of penalties, the Document reflects comments regarding the deterrent effect that they may have.

At the moment, when talking about cases of fraud, it is not only the securities legislation that should be reviewed but also, and especially, the Criminal Code.

As a SRO, the IDA applies a disciplinary process. It is with this concern for a deterrent effect that the IDA published, in January 2003, “Disciplinary Sanction Guidelines” aimed at informing the public and, particularly the representatives and its members, of the staff’s orientations with respect to breaches of the IDA’s rules. In these “standards”, the approach is to combine more substantial financial penalties with restrictions of practice ranging from supervision to temporary suspension, to banning from practice, for instance in the case of repeated behaviour with respect to several clients.

These “Guidelines” are currently being revised to adjust them to the nature of the infractions and to the decisions of both the IDA’s Hearing Panels and the Courts.

One of the interesting elements of the “Document” is the integration of the notion of “disgorgement”, namely the restitution of sums acquired in contravention of the law. The size of these amounts is a factor considered by the IDA in its representations with respect to penalties. However, this does not directly result in reimbursement of the client.

A first measure available to parliamentarians is certainly the secondary market civil liability regime. The Ontario legislature implemented such a system in December 2005 and we know that the AMF and the Ministère des finances are considering proposing it, a move we can only support.

When we speak of penalties, we must also speak of the means available for obtaining these penalties. The IDA has been requesting means to support its disciplinary actions and to better enforce the resulting penalties since 2002. The means of action sought by the IDA are the following:

Investigative Powers as SRO

The IDA draws its authority for enforcing its rules from the contractual relationships arising from the "membership" of its member firms. As such, the rules stipulate the duties to cooperate and produce documents, both for the individuals and for the firms themselves, and the failure to cooperate may render them subject to disciplinary penalties.

However, the disciplinary process is based on the evidence that is gathered during the investigations and which must be demonstrated. This evidence often requires that documents held by third parties be available for introduction as evidence (e.g.: non-member securities custodian, a professional or a financial institution). The IDA cannot demand the production of often necessary documents, if the documents are not held by a member.

This is why the IDA recommends that the "Investigative Power of a SRO" be recognized for purposes of enforcing its regulatory "corpus", enforcing securities laws or assisting in the enforcement of these laws.

This could take the form of an open "Order" to IDA staff, as can currently be the case for a Regulator.

This could enable the SRO as well as these Regulators to focus on investigations related to their fields of jurisdiction and the underlying content, resulting in better distribution of expertise for penalizing breaches of the rules and protecting the public. Formal approval through an "Order" would provide the necessary checks and balances that an investigative power under our legal system implies.

Witnesses

A second power requested by the IDA is the power to compel witnesses to participate in the disciplinary process. In many proceedings against a representative or a firm, the testimony of the wronged client is often crucial to obtaining a conviction and penalty. The IDA sometimes has to close files because it does not have the evidence, which is dependent on the goodwill of the clients or third parties concerned, who the IDA cannot compel to testify. Only the Alberta Securities Act has such a provision in this regard (Sect. 53.42).

While happy when the client wins and obtains financial compensation, the IDA considers that this “reparation” in no way excuses the regulatory breach that may have been the cause and that this breach should be penalized, particularly if we want to have the desired deterrent effect. In this regard, the penalty is important, as is the public nature of the IDA’s disciplinary process.

Two years ago, the IDA modified its web site to create an “Investor” section where investors can view the disciplinary history of professionals or firms with whom they deal.

We are not saying that a breach of a rule means that there was fraudulent behaviour with respect to a client. Yet, all of the rules made and supervised by the IDA are aimed at establishing among its members a strong culture of compliance which can only be of benefit to their clients.

To illustrate, an important breach observed from the consumer complaints that are received relates to the “suitability of investments”, namely investments that match the client’s objectives.

Whenever it has the opportunity, the IDA reiterates that this notion can only be established through open dialogue between the client and the representative and especially through regular updating and monitoring on both sides. We deplore the client who complains about a single transaction three years later, having benefited from it all these years.

Enforcement of decisions

A third power requested by the IDA is the power to enforce the decisions of the Hearing Panels that apply its disciplinary process as though they were decisions by a court of law.

Indeed, irrespective of the size of the monetary penalties that may be obtained, their deterrent effect is greatly reduced if they are not enforced. It has become too easy for an individual or a firm to stop doing business and sidestep the law.

The legislative precedents here, as well, are the Alberta Securities Act (Section 53.43 (2)), and the Québec Securities Act which includes a homologation power (Section 320.1) for the decisions of the AMF or a person exercising a delegated power.

Among the powers delegated to the IDA by the AMF, that of having its decisions homologated, pursuant to the Québec Securities Act (Section 320.1), was granted on July 13 and approved by the Minister on August 11, 2004. However, by virtue of the principle of "Delegatus non potest delegare", the homologation power delegated to the IDA by the AMF does not include that of obtaining the enforcement of disciplinary judgments, since this disciplinary power does not fall under the authority of the AMF, but rather under the Bureau de décision et de révision (Act respecting the Autorité des marchés financiers, R.S.Q. c.A-7.03, Sect. 93.10 and S.A., R.S.Q., c. V-1.1, Sect. 323.10). We very respectfully submit that this provision should be reviewed to give full effect to it. The IDA might have some proposals to submit on the basis of discussions with the AMF and the Bureau de révision et de décision en valeurs mobilières.

Monitor

The fourth of the IDA's legislative requests is the option to appoint a monitor. On the basis of the known precedents in Québec, what we are aiming at here is not the same: it is not a "trustee in bankruptcy" or a "trustee", since the CIPF can take action in the case of the insolvency of a member firm. What the IDA is looking for is more of an in-between approach in which the objective is to continue doing business while making corrections and supervising the implementation of these corrections.

Such an approach could be necessary, for example, following a major reorganization. The appointment of a monitor can provide some measure of comfort, in the form of an opinion by an experienced third party, that management is acting in compliance with the rules and in the best interests of the clients.

Such an approach could also be useful, for instance, following an examination that uncovers major shortcomings in the administration of client accounts. It would be up to the monitor to establish and supervise a plan of action with the management.

The objective here is to recognize a problem situation relating to a firm's compliance or the protection of its clients, and effect a "turnaround" with regard to a windup or liquidation.

IDA By-law 20.46 contains a similar measure. It found application with a member firm in 2005, as it concerned a joint approach undertaken therefore with the

member's consent. In the event that a member firm refuses to give such consent, the power to impose a monitor would be a way of protecting the investors.

Immunity

Finally, another measure that can strengthen the IDA's disciplinary action is statutory immunity. This type of protection is similar to what is found in the laws respecting persons who perform regulatory functions, such as the Regulators in Canada and the AMF in Québec.

Audit functions and whistle blowing

We feel that the Ordre des comptables agréés du Québec is best qualified to address this issue. We can say that, in the course of its supervision activities, the IDA works closely with the accounting firms that perform audit functions. The IDA has even drawn up a list of "accredited" firms for the receipt of certain financial statements. The motive is very simple: ensuring that these firms have industry expertise. In addition, each year, the IDA organizes information sessions for these firms, which include updates, presentations on what's new, and discussions on various problems encountered during the year.

We feel it is important to maintain this expertise for the protection of investors.

Collaboration

With respect to collaboration, the IDA can but support the idea that all parties operating in the financial sector be able to work together when necessary, according to their expertise. More specifically with regard to the AMF, participation on the Integrated Market Enforcement Team (IMET) appears desirable because of the additional intervention capacity. It is up to the AMF to determine the cases where this could be useful, just as the IDA itself already does.

As stated above, the IDA performs disciplinary functions which it would like to carry out as effectively as possible. In this context, the IDA can but rejoice and hope that the collaboration between it and the AMF will not only continue, but intensify. The previously mentioned legislative powers would thus prevent the IDA from having to "transfer" certain files to the AMF, on the sole grounds that the IDA does not have, for instance, the power to compel a witness. Such an approach would enable the IDA and the AMF to use their powers and their resources in the arenas where their respective specialties are the most advanced in order to produce the desired results as quickly as possible. The deterrent effect of the penalties is also dependent on a certain time proximity.

Independence and governance

As already mentioned, particularly for the mutual fund sector, the CSA have proposed various standards aimed precisely at assuring independence and governance. These measures could be strengthened if need be, but they offer elements of solution that approach the Committee's objectives.

On May 18, 2005, the IDA published a study entitled "Regulatory Analysis of Hedge Funds". This study was initiated by the IDA Board of Directors, more specifically, the "Member Regulation Oversight Committee", in the face the development of these funds. The study's first objective was thus to estimate the use of the products by the members. Fortunately, it appeared that less than 3% of the products related to Portus had been sold through IDA member firms.

The IDA concluded the study by formulating some recommendations, for itself with regard to strengthening certain practices, as well as for the CSA, on these notions of independence.

> **"Lack of Independence of Stakeholders and Weaknesses of Governance"**
>
> **"Provincial Securities Regulations"**
> Hedge fund products, including related products directed at the retail market such as PPNs are exempt from most regulatory requirements (such as securities registration and distribution by securities registrants). As securities, they fall within the ambit of IDA regulations as to suitability, but not all Members have that obligation in all situations. Furthermore, even in pursuing due diligence on hedge fund products, dealers will have to contend with the risks resulting from conflicts of interest, complex fees structures, lack of disclosure requirements, lack of controls on pricing and valuation and all the other problems introduced by the lack of direct regulation of highly complex products.
>
> The IDA believes that there should be a review of provincial laws, regulations and approaches and, if the regulatory tools are not already available, development of amendments that will bring hedge fund products being offered to the retail investor fully within the regulatory system. That review could include such matters as the exempt product status given to PPNs issued by banks and similar products to ensure a standard of fair dealing; distribution of hedge fund and other exempt products, particularly to non-accredited or retail investors; definition of referral arrangements to determine whether some are

> acts in furtherance of a trade; conflicts of interest of hedge fund managers that act directly or through affiliates as a manufacturer, advisor, custodian and distributor of hedge funds and hedge fund products with a view to implementing requirements to control such conflicts; and registration of hedge funds and their managers and oversight of their activities."

Among the recommendations directed at its own rules, the IDA reminded all its members of the prohibition against off-book transactions, which were the source of previous and recent events. These principles should apply to all transactions.

The IDA also proposes developing industry guidelines regarding acceptable practices for referral arrangements. Québec, along with British Columbia, has local regulations, but we believe that the sharing of commissions for client referrals should be reviewed: these guidelines are aimed at strengthening the interpretation of the rules relative to "secret commissions".

The IDA also proposes reminding its members of their responsibility to conduct due diligence on products recommended to clients. The investment suitability rule can only apply if the firm has sufficient knowledge of the products offered to the client. This is a way, we believe, of giving even more weight to this suitability rule.

Finally, the IDA proposes reviewing all guidelines or standards regarding disclosure of information to clients, conflicts of interest and internal controls for IDA members acting as developers, managers or distributors of hedge funds or pooled funds and determining whether such standards need amendment.

Another aspect that the IDA wishes to put forward is prohibiting its members from conducting investment activities through an affiliate with a limited market dealer registration when such activities could be conducted by the member itself.

We hope that the rule changes, if any, that result from these reviews will be accepted by the Regulators.

Other aspects

Among the possible solutions put forward by some observers, another element that looks "easy" to identify, but which may have some practical impacts that will need to be assessed, is that of the plurality of functions performed by the same person. Both in the mutual funds and securities sectors, a separation of roles may seem to offer investors better protection. However, in smaller firms, the separation can generate substantial costs that might adversely affect their

viability. In larger institutions, separate management teams has its merits, but also its costs which will be passed on to the investors.

A good approach certainly, but one which should be weighed in terms of the real impacts. Where fraud is involved, this strict separation could also be nothing more than a sham.

Elsewhere, regarding the issue of proximity of SRO staff with the staff of the member firms, reality must also be taken into account.

For instance, the IDA is aware that its staff may attract firms that want to build themselves an effective compliance department. The IDA may be perceived as a good training “school” that benefits the firm, but at the same time, the IDA also benefits in terms of the development of this expertise and a compliance culture among its members.

The critics who propose a delay of a few years bump up against two realities: firstly, the speed and the nature of regulatory changes and, secondly, the fact that it may be difficult to prevent a person from earning a living for several years.

In this regard, we submit that disclosure, along with certain measures related to the decision-making autonomy of the people concerned, in certain types of positions, could provide a sufficient counterbalance.

With respect to independence and governance, allow us to inform you of the IDA’s latest decisions with regard to its organizational structure.

Indeed, with a view to responding to the various issues that have arisen over the years with regard to the appearance of conflicts of interest between its SRO functions and its sector representation activities, the IDA members voted, last December 15, in favour of a proposal to divide these two functions into two separate entities.

The IDA had indicated a number of times that it felt that, like various professional bodies, these two mandates could coexist within the same entity by relying on “Chinese walls” and a structure of governance and supervision by the Board of Directors to ensure that these functions were carried out separately.

The decision to go ahead with an even more marked separation is an indication that the IDA is thinking along the same lines as the Committee.

The various Regulators in Canada, including the AMF in Québec, through its President and Chief Executive Officer, have approved this decision. In this “new” context, any action that might be taken by the AMF in order to improve cooperation can but benefit the market and investor protection.

Issues to be debated

Some issues relate more specifically to the IDA's fields of expertise and activities.

Exchange of information and cooperation

This point can be lumped in with everything to do with the AMF's ability to exchange information or collaborate with other entities that have the same investor protection objective.

Joint exchanges or investigations are likely to favour more complete and, by the same token, more efficient or speedier investigations. Such exchanges would, in particular, allow all the organizations who have powers in this regard to focus on their particular field of expertise. Legislative amendments are necessary.

It is with this end in mind that we submit recommendations to further support the role of the SRO:

- Investigative powers as a SRO
- Powers to compel witnesses
- Enforcement of disciplinary decisions
- Appointment of a monitor
- Immunity

On a different subject, but from this same standpoint of cooperation and on a subject of concern to the Committee, the IDA is pleased to have signed an "Agreement" with the AMF last December, regarding its members' consumer complaints reports. This Agreement is an illustration of how efforts can be pooled to achieve the same objective.

We hope that this Agreement will make it possible to better identify consumer issues and support education efforts, in particular.

Conflicts of interest and governance

As already indicated, these issues go beyond the mutual fund sector alone. The courses of action identified by the IDA following its "Analysis of Hedge Funds" were determined in this spirit.

The CSA and the AMF are currently working on these issues; we can but support them.

Penalties

A number of observers have mentioned that penalties may have a deterrent effect. The IDA agrees with this line of thought, while pointing out that, although requiring more severe penalties, it often faces problems with enforcing its disciplinary decisions and this is why it is emphasizing enforcement and is requesting legislative amendments.

Task Force to Modernize Securities Legislation in Canada

This independent Task Force was created by the IDA in June 2005 and is funded by it.

As mentioned by the Association President when he announced its creation, the Task Force's mandate is:

> "…to examine and make recommendations to modernize securities legislation for the 21st century. … the Task Force will examine issues related to investor protection, access to capital, corporate governance, regulatory burden, enforcement, proficiency and registration. "
>
> "This initiative has the potential to form the basis of dynamic, modern securities legislation that draws on the best thinking in regulation and that challenges some fundamental precepts that are no longer functional for the realities of the marketplace and investor behaviour. The Task Force will address questions such as: Is regulation addressing investors' real concerns? Are voluminous and virtually impenetrable disclosure documents the most effective way to communicate with individual investors? Can enforcement be more effective? Do corporate governance rules have the balance right for small issuers? Should harmonization with the US be more narrowly focused on larger issuers? Are we at the optimal point on the continuum between rules and principles? …"

The aim? Regulatory content that

> " …deals with the critical issues - balancing investor protection with efficiency and competitiveness, the regulatory burden and its potential anti-competitive implications, harmonization with foreign jurisdictions, regional concerns especially regarding small and medium size enterprises (SMEs), access to capital, risk-based

> regulation, enforcement policy, governance and consumer redress..".

Schedule A presents the complete mandate and the list of 28 research studies that have been initiated since. The Task Force intends to receive Written Submissions and to hold meetings across Canada to inform its process and support its recommendations, which should be known in November 2006.

Schedule B

IDA web site: http://www.ida.ca/

Rule Book:
http://www.ida.ca/Files/BulletinsNotices/RuleBook/RuleBook_en.pdf
(Includes By-law 20 and Regulation 400)

Hedge Fund Analysis:
http://www.ida.ca/files/compliance/regulatoryanalysishedgefunds_en.pdf

Disciplinary Sanction Guidelines:
http://www.ida.ca/Files/Enforcement/PenaltyGuidelines_en.pdf

Canadian Mutual Fund Dealers Association: http://www.mfda.ca/

Coverage policy: http://www.mfda.ca/ipc/policies/IPC-coverage-policy.pdf

Brochure: http://www.mfda.ca/ipc/forms/IPC_brochure.pdf

Canadian Investor Protection Fund – CIPF: www.cipf.ca

Ombudsman for Banking Services and Investments: www.obsi.ca