

**MUTUAL FUND DEALERS ASSOCIATION OF CANADA
AND
MFDA INVESTOR PROTECTION CORPORATION
Suite 1600
121 King Street West
Toronto, Ontario
M5H 3T9**

November 15, 2004 (revised)

Stephen P. Sibold, Q.C., Chair
Alberta Securities Commission
300 – 5th Avenue S.W.
4th Floor
Calgary, Alberta T2P 3C4

The Secretary to the Commission
Ontario Securities Commission
20 Queen Street West
Suite 1900, P.O. Box 55
Toronto, Ontario M4S 3S8

Ms. Brenda Leung
Executive Director
British Columbia Securities Commission
P.O. Box 10142, Pacific Centre
701 West Georgia Street
Vancouver, B.C. V7Y 1L2

Barbara Shourounis
Executive Director
Saskatchewan Securities Commission
800 – 1920 Broad Street
Regina, Saskatchewan S4P 3V7

Donald G. Murray, Chair
Manitoba Securities Commission
1130 - 405 Broadway Avenue
Winnipeg, Manitoba
R3C 3L6

Secretary to the Commission
Securities Commission of Newfoundland
P.O. Box 8700
2nd Floor, West Block
Confederation Building
St. John's, Newfoundland A1B 4J6

H. Leslie O'Brien, Q.C., Chair
Nova Scotia Securities Commission
Joseph Howe Building
P.O. Box 458, 2nd Floor
1690 Hollis Street
Halifax, Nova Scotia B3J 3J9

Dear Sirs/Mesdames:

**Re: Mutual Fund Dealers Association of Canada and
MFDA Investor Protection Corporation**

This letter sets out the revised application of the Mutual Fund Dealers Association of Canada ("MFDA") and the MFDA Investor Protection Corporation/Corporation de protection des investisseurs de l'ACFM (the "IPC" or "MFDA IPC") to the British Columbia Securities

Commission, the Alberta Securities Commission, the Saskatchewan Securities Commission, the Manitoba Securities Commission, the Ontario Securities Commission and the Nova Scotia Securities Commission (collectively the "Commissions") for approval, designation or consideration, as the case may be, of the IPC as a protection plan for customers of mutual fund dealers which are members of the MFDA pursuant to the applicable securities legislation (the "Legislation"). Reference is made to (i) Section 110 of the regulation under the *Securities Act* (Ontario), Section 23 of the Rules made under the *Securities Act* (British Columbia) and Section 27 of the Regulation under the *Securities Act* (Nova Scotia), and (ii) to the respective recognition orders relating to the MFDA referred to herein. Included with the application for such approval in connection with IPC is the application of MFDA for approval of certain new and amended Rules and policies of the MFDA pursuant to such recognition orders relating to MFDA.

Revised Application and CIPF

This letter revises and replaces the application of the MFDA and MFDA IPC to the Commissions dated November 14, 2002 (the "Initial Application"). The Initial Application was based on an application filed with the Commissions in August 2001 which was not published but which was the basis for discussions between MFDA IPC and the Commissions. The Initial Application was published for public comment including in the Ontario Securities Commission Bulletin, Issue 25/48 on November 29, 2002. The public comment period expired in January 2003 and a number of comments were received. Most commentators questioned whether an investor protection fund for MFDA members was necessary at all in view of the facts that the risks were relatively low and a high percentage of client assets were held in client versus nominee name, i.e. the customer's claim for property was directly against the mutual fund manager and not the dealer. The Commissions have confirmed that having no fund at all would not be acceptable. On that basis, commentators on the MFDA IPC proposal questioned whether the coverage available should be similar to that provided by Canadian Investor Protection Fund ("CIPF") and, consequentially, whether there should be two separate investor protection funds or whether MFDA members could participate in CIPF.

The Board of the MFDA considered the responses to the publication of the proposal for MFDA IPC and concluded, subject to certain conditions, that the prospect of MFDA participating in CIPF should be pursued. Accordingly, in the spring of 2004, discussions were commenced with the board and management of CIPF. The MFDA was (and continues to be) of the view that the businesses of mutual fund dealers are different in significant respects from those of investment dealers and, accordingly, the insolvency risks are different. As a result of the initial discussions, a formal working group consisting of representatives of both CIPF and MFDA was established to study the differences between the MFDA Rules and CIPF Minimum Standards as well as the general differences in the operations and risks of both mutual fund dealers and investment dealers. The significant differences included capital requirements, client reporting, the assessment base, distribution structures and client versus nominee holdings.

At the conclusion of the review process described, it was apparent that many of the differences identified between the businesses and risks of MFDA members and investment dealers could be resolved. However, there remained some matters that required further consideration and the view of CIPF was that a transition period would be required before MFDA members could fully participate in CIPF. This transition period would provide time for amending the rules of both

organizations as well as to permit the organizations to gain experience with the risks relevant to the businesses of MFDA members.

The Board of Directors of MFDA has carefully considered the circumstances described above and has decided to proceed with the establishment of MFDA IPC as soon as possible. However, the proposal is that the customer loss coverage to be offered by MFDA IPC would be similar in substance to that of CIPF, namely that all financial products held by an MFDA member would be eligible for coverage and that the amount of coverage per separate account (as defined in the coverage policies) would be \$1 million. In order to provide such coverage, the MFDA Board is satisfied that an initial fund containing liquid financial assets of at least \$30 million would be adequate.

Based on the foregoing conclusions of the MFDA Board, it was determined that the application of MFDA IPC to the relevant members of the CSA would be amended and resubmitted for approval. In addition, MFDA and MFDA IPC expect that within a reasonable period of time MFDA members would participate in CIPF on terms that are appropriate for MFDA members and the public interest. The intent is that customers acquiring financial products from Canadian investment dealers and mutual fund dealers could look to one customer protection fund, i.e. CIPF. In order to achieve this objective, MFDA and MFDA IPC will continue to review what changes to both MFDA and CIPF requirements may be necessary and appropriate to permit MFDA to participate in CIPF. CIPF has indicated that it looks forward to an opportunity to welcome MFDA as a sponsoring SRO of CIPF.

Approval Criteria

The MFDA has been recognized as a self-regulatory organization by order of certain of the Commissions under the Legislation and such orders contemplate that a compensation or contingency trust fund will be established for customers of members of the MFDA. IPC is to be established for this purpose and is applying for approval as a protection plan. The Commissions have identified seven proposed criteria ("Criteria") to be satisfied by IPC in this regard and draft terms and conditions ("Terms and Conditions") to any order so approving the IPC. For convenience this application is divided into the following sections and sections 2 to 8, inclusive, set out the proposed Criteria together with a description of how IPC satisfies the Criteria as well as the draft Terms and Conditions:

1. Background
2. Corporate Structure and Purpose of IPC
3. Corporate Governance
4. Funding and Maintenance of IPC
5. Client Protection
6. Financial and Operational Viability (Including Risk Management)
7. Reporting to Securities Commissions

8. Rule Making
9. Submissions

Submitted with this application are the following supporting documents:

1. the Letters Patent of IPC issued pursuant to Part II of the *Canada Corporations Act* (Exhibit A);
2. draft By-law No. 1 of the IPC (Exhibit B);
3. draft policy relating to IPC customer coverage (Exhibit C);
4. proposed MFDA advertising Rule with commentary regarding the proposed amendments (Exhibit D);
5. proposed MFDA advertising policy relating to IPC coverage (Exhibit E).

The documents referred to in items 2, 3, 4 and 5 above have been revised from the versions submitted with the Initial Application.

1. BACKGROUND

The establishment of the MFDA was the result of certain industry studies and commentary that were spurred by the explosive growth and popularity of mutual funds in the late 1980s and throughout the 1990s. The concerns of some of the Commissions which were members of the Canadian Securities Administrators (the "CSA") in promoting the establishment of the MFDA included concerns relating to investor protection for mutual fund investors. Some of these concerns were articulated in the report by Ontario Securities Commissioner, Glorianne Stromberg, entitled: "Regulatory Strategies for the Mid-1990's: Recommendations for Regulating Investment Funds in Canada" (the "Stromberg Report"), published in 1995 and that Report, as well as initiatives of the CSA, assumed that an investor protection plan similar to CIPF would be established or that CIPF would provide the coverage. CIPF provides investor protection to eligible customers of insolvent securities dealers who are members of self-regulatory organizations such as the IDA and the Canadian exchanges.

The Stromberg Report referred to the fact that certain Provinces of Canada (British Columbia, Ontario, Quebec and Nova Scotia) had established protection plans for customers of registrants in those provinces but that the coverage available was limited to amounts of \$2,500 to \$25,000 depending upon the province. Further, these plans did not provide the amount of protection that reasonably represents the financial risk that consumers of mutual fund securities doing business with mutual fund dealers may be exposed to.

As part of the early development of the MFDA, a number of industry committees were established to accumulate mutual fund industry experience and make recommendations on a number of subjects including an investor protection plan and matters relating to prudential regulation of members. The Board of Directors of the MFDA and its staff reviewed the reports and recommendations of the industry committees referred to above and assessed them in the context of available resources and what were perceived to be the regulatory objectives. A

preliminary review of the role and functions of IPC according to the MFDA Board was published for comment in its recognition application to the Commissions. The purpose and operations of IPC have been refined as a result of the work of the committees, the MFDA Board, the first IPC directors, comments by the public and MFDA members in respect of the Initial Application and consultations with the Commissions. This revised application is submitted on the authority of the Board of Directors of both the MFDA and the IPC.

2. CORPORATE STRUCTURE AND PURPOSE OF THE IPC

CSA Criteria

The MFDA IPC has the appropriate legal authority to carry out its objective of providing protection to clients of the members of the MFDA if the client property held by such members becomes unavailable as a result of the insolvency of such members, in accordance with established rules, regulations or policies of the MFDA IPC.

2.1 Corporation

The IPC has been established as a non-share capital corporation under Part II of the *Canada Corporations Act* (the "CCA"). This form of organization was based on an assessment of several considerations including a review of the structure of other financial services investor protection plans such as the Canadian Investor Protection Fund ("CIPF"), Canadian Deposit Insurance Corporation ("CDIC"), The Canadian Life and Health Insurance Compensation Corporation ("Compcorp") and The Property and Casualty Insurance Compensation Corporation ("PACICC"). The MFDA is itself a corporation established under Part II of the CCA.

The implications of adopting a not-for-profit corporation structure relate to the governance of the IPC, requirements to comply with certain statutory requirements, financial and income tax considerations and legal responsibilities. The MFDA and the IPC are of the view that the functions and role of the IPC can be best accommodated with the proposed corporate form.

2.2 Letters Patent

A non-share capital corporation under Part II of the CCA is created by a grant of letters patent by the federal government (Crown) on application to Industry Canada. The letters patent describe the objects of the IPC, its first directors and other basic characteristics. A copy of the letters patent of IPC is filed with this application as Exhibit A.

2.3 By-Laws

The main procedural documentation by which the affairs of the IPC will be governed are its by-laws. For the most part, the by-laws govern the procedures by which the IPC will conduct its activities including provisions for meetings of directors and members, the appointment of officers, indemnities and insurance, and other administrative matters. The by-laws of the IPC as a Part II CCA corporation, and certain amendments, must be approved by Industry Canada before becoming effective. A copy of the by-laws of IPC, included in draft in the Initial Application, is filed with this application as Exhibit B. Certain amendments to the by-laws of IPC are anticipated by this application. These by-laws are binding on the directors and members

of IPC but not directly on members of the MFDA. However, by agreement between MFDA and IPC and the effect of MFDA's by-laws which bind its members, those members are bound to the extent necessary including the obligation to pay assessments: see MFDA By-law 15.1.3.

2.4 Income Tax Status

The IPC, as a non-share capital corporation under Part II of the CCA, is structured so that it will qualify as being exempt from income tax under the *Income Tax Act* (Canada) and corresponding provincial income tax legislation. This status will require that the IPC operate exclusively on a not-for-profit basis and that no part of its net income be payable to or available for the benefit of any members.

2.5 Purpose of the IPC

The primary purpose of the IPC is to provide protection to eligible clients of the MFDA members if client property held by such members is unavailable as a result of the insolvency of the member. The role of the IPC in providing customer protection to clients of MFDA members is in the public interest. This parallels the MFDA's own public interest mandate. In recognition of the IPC's responsibilities to the public, the IPC and its operations have been structured to ensure that it will be responsive to the concerns and needs of the investing public. The proposal described for MFDA and IPC to pursue the possibility of MFDA members participating in CIPF is consistent with IPC's role. IPC is not an insurer and IPC coverage is not insurance and, accordingly, provincial insurance regulations do not apply to IPC or its coverage.

2.6 MFDA Member Insolvency

In the event of insolvency of a member of the MFDA, the IPC shall respond quickly and decisively, in accordance with its established rules, regulations or policies for assessing claims. The IPC shall also co-operate and provide reasonable assistance to the MFDA, a trustee in bankruptcy or securities regulators in administering an insolvency.

3. CORPORATE GOVERNANCE

CSA Criteria

- (a) The arrangements with respect to the appointment, removal from office and functions of the persons ultimately responsible for making or enforcing the rules of the MFDA IPC, namely, the governing body, are such as to ensure a proper balance between the differing interests of the MFDA members participating in the MFDA IPC, and in recognition that the protection of the public interest is a primary goal of the MFDA IPC, a reasonable number and proportion of directors are independent of the MFDA and its members in order to ensure diversity of representation on the Board of Directors.**
- (b) Without limiting the generality of the foregoing, the MFDA IPC should provide for:**

- (i) **fair and meaningful representation on its governing body, in the context of the nature and structure of the MFDA IPC, and any governance committee thereto, including the audit committee, and in the approval of rules, regulations and policies;**
- (ii) **appropriate representation of persons independent of the MFDA or any of its members or of any affiliated or associated company of such member on any executive committee or similar body; and**
- (iii) **appropriate qualification, remuneration, conflict of interest provisions and limitation of liability and indemnification protections for directors and officers and employees of the MFDA IPC generally.**

3.1 General

The manner in which the affairs of IPC are governed is critical to its ability to achieve its objectives and fulfil the purposes and functions expected of it. There are a number of interests that are to be reflected in the activities of IPC and which will require, to a greater or lesser degree, some participation in the governance of IPC. These interests include the members of the MFDA, customers of such members, the MFDA itself, the CSA and the public at large.

3.2 Members

As a non-share capital corporation under the CCA the IPC has members rather than shareholders. The members of the IPC are to be the same persons who are the directors. This is for ease of administration as it is impractical for a broader membership to be appointed. Accordingly, there will be one class of members, all of whom will be voting members. The primary role of members is to appoint the auditor of the corporation and confirm by-laws. The members must meet at least annually although there are provisions for members to act by instrument in writing if all or a specified majority of members sign a resolution affecting any particular business.

3.3 Board of Directors

The constating documents of the IPC provide that its Board will have a maximum size of 11 directors and a minimum size of 3 directors. The Board of the IPC shall be composed of an odd number of directors, the minority of which would be nominees of the MFDA (industry directors) and the majority would be public directors elected by the Board. Since the IPC is intended to protect customers of the members of the MFDA, the most appropriate representatives of the industry are representatives of the members or the MFDA. Although the initial by-laws provide that industry directors cannot be removed from office without the consent of the MFDA, this provision is to be deleted. In addition, the initial by-laws will be amended to provide that all industry directors shall be nominated by MFDA, but the election or appointment of such nominees as directors will be by the IPC Board or members. The definition of "Industry Directors" and "Public Directors" is set out in By-law 4.1 of the IPC constating documents (Exhibit B-2). By-law 4.2 sets out the details of the qualifications of the directors (both public and industry) including geographical considerations and the criteria established by the Board in

appointing or nominating the directors. The initial by-laws are also being amended to conform (in general terms) the definition of Public Directors with the corresponding term in the by-laws of MFDA.

By-law 4.7 lists a series of events giving rise to the automatic termination of office of a director. A retiring director shall remain in office until the dissolution or adjournment of the meeting at which such retirement is accepted and a successor is elected.

In addition, there will be a Chair who will be appointed by the directors from one of their number and who could be either an industry director or a public director. This approach reflects the IPC view that the Chair should be the best person for the position, and is consistent with good industry and corporate governance. This structure would be reflected in whatever size the Board may be, provided that a majority of the Board is always independent or public directors. The term of office for all directors will be limited to two three-year terms which will be staggered to ensure appropriate continuity and experience. The current directors of the IPC are Mr. Lawrence A. Wright (public and Chair), Mr. Donald H. Page (public) and Mr. W. David Wood (industry). Public directors will be recommended by a nominating committee of the Board composed of an equal number of MFDA appointees and public directors (four in total when the size of the board permits). The Board of the IPC will appoint the public directors.

The President may be the chief executive officer or chief operating officer of the IPC. The rights and duties of the president are outlined in By-law 11.2 of the attached constating documents.

3.4 Conflicts of Interest

By-law 5.1 establishes procedures in dealing with conflicts of interest of the directors and disclosure requirements.

3.5 Liability and Indemnity of Directors

The By-laws of the IPC stipulate that any director or officer will not be held liable for any act, receipt, neglect or default of any other director, officer or employee for any loss described in Section 6.1 of the By-laws, while acting as a director or officer for the IPC. Indemnities by IPC to directors and others are provided for in Section 7.1. In addition, IPC is authorized to purchase insurance in respect of acts and omissions of its directors and officers and intends to do so prior to IPC protection being available. Sections 6 and 7 of the By-laws are to be amended to conform to the corresponding provisions of the MFDA by-laws.

3.6 Remuneration of Directors

Directors of the IPC will receive remuneration in a manner similar to comparable organizations.

3.7 MFDA

The MFDA has proposed that the IPC be a separate organization with separate assets and governance. However, there will be close interaction between the MFDA and the IPC and the terms of this relationship will be defined in the by-laws and by way of operating agreements. Of immediate concern during the initial phase of the IPC is the need for funding of the IPC's start-up costs through the MFDA and to date MFDA has advanced funds to IPC which are to be repaid

by IPC. The IPC and the MFDA are in the course of determining the appropriate terms of this relationship. The interests of the MFDA dealer members will be represented through the MFDA's participation in IPC governance.

3.8 CSA

In certain provincial jurisdictions of members of the CSA, it is a requirement of registration as a securities or mutual fund dealer that it be a member of an investor protection plan that has been approved by the applicable securities commission, executive director or delegated authority. The IPC is applying for approval in such jurisdictions for that purpose. The securities commissions in some or all of these jurisdictions will have regulatory oversight over the activities of the IPC.

3.9 Customers (Public)

The primary beneficiaries of the IPC are the customers of insolvent members of the MFDA. Customers, as the investing public, will primarily be represented by the public directors on the Board of Directors of the IPC as well as the oversight of members of the CSA. In addition, the IPC will be expected to be responsive to public comment and enquiries.

3.10 Audit Committee

The IPC will create an audit committee as a committee of the Board. The IPC Board will be responsible for selecting the audit committee members. The audit committee will be composed of three or more directors, the majority of which will be public directors. The audit committee shall be responsible for the review of the Corporation's annual financial statements and such other functions as the Board shall determine by resolution. The IPC will be required to appoint an auditor to prepare a report on the annual financial statements. The role and performance of the auditor will be monitored by the audit committee.

3.11 Other Committees

The Board may also appoint an executive committee and shall appoint a nominating committee and any other committee subject to By-law ss. 8.2, 8.4 and 8.5. The executive committee, if appointed, requires an equal number of industry and public directors. The initial By-law Section 8.4 provides that the nominating committee is to be composed of two public and two industry directors; this Section will be amended prior to commencement of IPC coverage to refer to an even number of industry and public directors. However, the Board which appoints the other committees (and is always comprised of more public than industry directors) can be expected to ensure that appropriate balance in representation is maintained. When, or if, the Board increases in size, consideration may be given to fixing other committee composition in the by-laws.

4. FUNDING AND MAINTENANCE OF IPC

CSA Criteria

- (a) Any and all assessments imposed by the MFDA IPC on the MFDA members to finance the MFDA IPC are equitably allocated. Assessments do not have the effect of creating barriers to becoming members of the MFDA. The assessments must also be balanced with**

the criteria that the MFDA IPC has sufficient revenues to satisfy claims in the event of insolvency of an MFDA member and has sufficient financial resources to satisfy its operational costs.

- (b) The MFDA IPC's process for setting assessments is a fair and reasonable method of establishing equitable assessments for each MFDA member's contribution, including, among other things, rules, regulations or policies that govern the contributions of affiliates and subsidiaries of MFDA members.**
- (c) The MFDA IPC provides the Commission with a current copy of the method of assessments and notifies the Commission 30 days prior to making any changes to the method of assessing MFDA members.**
- (d) The Board determines the appropriate level of assets for the MFDA IPC and ensures that the level of assets of the MFDA IPC is adequate. Any material adverse change in the level of MFDA IPC assets, or upon becoming aware of the potential for any material adverse change, is immediately reported to the Commission by the MFDA IPC.**
- (e) The MFDA IPC implements an appropriate accounting system, including a system of internal controls for maintaining the MFDA IPC. The MFDA IPC appoints an independent auditor for the purpose of conducting an audit of the MFDA IPC's annual financial statements in accordance with generally accepted auditing standards.**
- (f) Moneys in the MFDA IPC are invested in accordance with rules, regulations and policies approved by the Board. These rules, regulations and policies shall be provided to the Commission and the MFDA IPC shall also inform the Commission of any changes in these rules, regulations or policies.**

4.1 Fund Size

The MFDA and IPC have agreed that an initial fund size of not less than \$30 million is appropriate to permit IPC commence operations and to provide coverage of up to \$1 million per separate account for eligible claims (with no deductible). The actual and target size of the fund will be reviewed by the IPC Board periodically and appropriate changes to fund size will be recommended. The funding and assessment proposals by way of member assessment and borrowings are described in the following section. Any change proposed by IPC in the target size of the IPC's assets shall be made only after consultation with MFDA. If IPC and MFDA are unable to agree on the proposed change, the disagreement will be immediately reported to the appropriate members of the CSA. Additional amounts may be required each year depending on losses paid or the IPC's operating expenses to the extent that income from the fund size is not sufficient to cover such expenses (including start-up costs). The first year of coverage would commence in April, 2005 or as soon thereafter as regulatory approvals permit. The size and appropriate level of assets in the IPC is a function of several considerations including the predicted risk of loss, the amount of coverage to be provided and the financial ability of

members to immediately fund the IPC. IPC, MFDA and the various sources they have consulted have not been able to determine any accurate or experience-based formula for initial fund size. The proposed initial size of \$30 million appears to be reasonable in view of the proposed coverage of \$1 million per customer and the member assessments required.

Where the size of the fund becomes less than its target size at any time or the eligible claims on the fund exceed the IPC's immediately available assets, the IPC will be able to make assessments to replenish the fund to its target size or to satisfy such claims and MFDA will undertake to assess its members accordingly. The MFDA and the IPC will cooperate in seeking funds by assessment, third party borrowings or other appropriate sources.

Any material adverse change in the level of the IPC's assets would be reported immediately to both the MFDA and members of the CSA. In addition, the summarized annual audited financial statements of the IPC will be available to the public and full audited statements will be provided to the MFDA and members of the CSA.

4.2 General Funding

The overriding principle of the IPC's funding is that the MFDA members collectively are to be responsible for the payments of client losses arising as a result of the insolvency of an MFDA member. The IPC has considered various sources of funding for IPC (member assessments, third party financing, use of interest accumulated in member trust accounts, integration with other industry protection plans, the current provincial protection plans and other risk funding mechanisms) and has concluded that the MFDA member assessments should be the long-term method of funding the IPC. This approach is consistent with similar insolvency protection plans such as CIPF, CDIC, Securities Investor Protection Corporation ("SIPC") and the Deposit Insurance Corporation of Ontario ("DICO") and plans approved by certain CSA members for securities and mutual fund dealers.

The short term method of funding the IPC for start-up costs has been by advances from the MFDA which will be required to be repaid. Thereafter funding will be by way of (i) assessments of MFDA members which are required to contribute to the IPC the amounts assessed; (ii) the establishment of a line of credit (or similar facility) with one or more institutional lenders in an aggregate amount of not less than \$25 million; and (iii) contributions of assets by MFDA or other persons. On the commencement of coverage (planned for April 1, 2005) IPC will have cash assets of not less than \$2.5 million (from (i) and (iii)) and the line of credit referred to in (ii). Contributions by MFDA members through assessments become the property of the IPC and members will no longer have any proprietary interest in the contributions. If the IPC is terminated, the property held by the IPC after payment of its obligations would be distributed to an organization with like objects in connection with Canadian capital markets and the public interest.

4.3 Assessments

The IPC may impose or prescribe fees, levies, assessments or other charges on or in respect of persons who are members of the MFDA. The IPC may make arrangements for the notification and collection of the fees, levies or assessments either directly or indirectly through the MFDA. The amount, nature and basis of any fee, levy or assessment is determined by the Board in its

sole discretion subject to consultation with MFDA as described. The liability for such fees, levies and assessments is that of the members and not the MFDA itself.

The initial assessment methodology to be adopted by the IPC including the annual assessment amount, maximum permitted annual assessments and any special or penalty assessments has been agreed to by the MFDA and is described below. MFDA member assessments are to be the long-term method of funding the IPC. The initial basis for assessments is to be based on assets under administration (AUA) as determined for MFDA fee purposes. The best judgment of the boards of both the MFDA and the IPC is that the AUA model is an appropriate proxy for the risks to be covered by the IPC. An assessment at the annual rate of \$22-24 per million of AUA (depending on the then current industry AUA) is scheduled to be made in 2005 (subject to approval of IPC by the relevant Commissions) which would be payable by members in quarterly instalments in June, September and December, 2005 if coverage were to commence April 1, 2005. Thereafter, annual assessments of \$22-24 per million of AUA will be made for a period of five years. This annual assessment will be made and be payable quarterly in equal instalments to coincide with the payment of MFDA membership fees. The Board of IPC will review annually the foregoing basis of assessments to determine that it is appropriate in accordance with a variety of relevant factors such as fund size targets, economic and mutual fund industry conditions, interest rates and fund loss experience.

The foregoing assessment schedule and amounts are subject to change if MFDA members participate in CIPF as discussed above. In this regard, it is noted that corresponding assessments of members of CIPF are based on gross revenues of members.

The mechanism for determining and collecting MFDA members' assessments will be refined but the working premise is that the IPC Board will review the assessment methodology, annual assessment amount, any maximum permitted annual assessments and special penalty assessments. Any changes from the initial assessment basis described in the preceding paragraph will be made in consultation with the MFDA and if IPC and MFDA are unable to agree on such changes the matter will be immediately reported to the relevant members of the CSA. The IPC shall provide the relevant CSA members with a current copy of the method of assessments and notify such members 30 days prior to making any changes to the method of assessing MFDA members. The basis on which the IPC will operate and co-ordinate its affairs with the MFDA will be governed by an agreement(s). This agreement will contemplate a dispute resolution mechanism (prior to reference to the CSA) which will be a formal, non-binding procedure to facilitate a fair and efficient resolution of any issues that may arise.

4.4 Line of Credit

IPC will establish a line of credit or similar facility with one or more institutional leaders in an aggregate amount of not less than \$25 million. This amount together with funds available to IPC from MFDA and member assessments will ensure that the initial aggregate funding available to IPC will not be less than \$30 million. MFDA and IPC expect a credit facility to be available for the commencement of coverage. The credit facility may be secured by a general security interest in respect of the assets of IPC in favour of its lender(s). In addition, MFDA will guarantee the obligations of IPC to its lenders and undertake to assess its members as required in order to permit IPC to meet its borrowing obligations. The obligations of MFDA to the lenders will be secured by an assignment of any assessment receivables from members that may be required or

made. The credit facility will be available for a period not to exceed 364 days but will be extendable at the option of the lenders on sufficient notice periods to permit IPC to establish replacement credit facilities if all or a portion of the initial facility is terminated. As indicated in section 4.1 the size of the fund maintained by IPC will be reviewed on a periodic basis. As the size of the funds maintained by IPC increases by way of assessments over the next few years – thereby increasing the total resources available to IPC for coverage – the continued need for all or a portion of the credit facility will also be reviewed.

4.5 Investment of IPC's Funds

The directors of the IPC may invest and re-invest all cash, securities and other property belonging to the IPC that, under their uncontrolled discretion, they consider advisable. The Board will adopt investment policies for the management of the IPC's assets. Professional investment management advice may be retained. The general parameters of the investment policy are expected to include safety of principal and reasonable income while at the same time ensuring that sufficient liquid funds are available at any time to pay claims.

An investment committee to oversee the investment of the IPC assets will be considered if and when the size of the Fund assets warrants, there is a perceived need for the function to be delegated to a special committee or there is an advantage to the IPC by such management. The IPC does not expect any of these circumstances to arise for some time for a number of reasons. The IPC Board will in any event set the investment guidelines and the small size of the Board would likely render a separate committee unnecessary and duplicative. The policies will be conservative and will not likely require active management. For example, a high proportion of the IPC assets will be tiered according to maturity in high grade government debt securities and simply rolled over on maturity.

4.6 Auditors

The IPC will implement an appropriate accounting system, including a system of internal controls for maintaining the IPC. The IPC members will appoint an independent auditor to audit the annual financial statements in accordance with generally accepted auditing standards. The auditor shall hold office until the next annual meeting, provided that the directors may fill any casual vacancy in the office of auditor. The remuneration of the auditor will be fixed by the Board. At every annual meeting of members, the report of the directors, the financial statement and the report of the auditors will be presented and auditors appointed for the ensuing year. The role and performance of the auditor will be monitored by the audit committee.

5. CLIENT PROTECTION

CSA Criteria

- (a) The MFDA IPC provides fair and adequate coverage for eligible customers of the MFDA members, and any other eligible customers that are agreed upon by the MFDA IPC and the Commission, regardless of the jurisdictions where they reside;**
- (b) The MFDA IPC establishes and maintains fair and reasonable rules, regulations or policies for granting claims made under the MFDA IPC**

and pays eligible customer claims made pursuant to these policies, including, but not limited to:

- (i) The MFDA IPC establishes and maintains rules, regulations or policies whereby persons not dealing at arm's length with the insolvent MFDA member, or who the MFDA IPC determines are, in whole or in part, responsible for the insolvency of the MFDA member, will not be covered by the MFDA IPC as eligible customers;**
- (ii) The MFDA IPC establishes within its rules, regulations or policies a fair and reasonable internal appeals mechanism whereby eligible customer claims that are not accepted for payment by the MFDA IPC staff, or by an appointed committee, are to be reconsidered by the Board of Directors;**
- (c) The MFDA IPC's rules, regulations or policies described in paragraph (b) above do not prevent an eligible customer from taking legal action against the MFDA IPC, where the eligible customer has exhausted the MFDA IPC's internal claim review process and appeals process.**
- (d) The MFDA IPC adequately informs customers of MFDA members of the principles and policies on which coverage will be available, including, but not limited to, the process for making a claim and the maximum coverage available per customer.**
- (e) The MFDA IPC, in cooperation with the MFDA, establishes advertising guidelines within the MFDA's general advertising by-law that clearly establishes the parameters for advertising in order not to mislead the public.**
- (f) In the event of an insolvency of a member of the MFDA, the MFDA IPC shall respond quickly and decisively, in accordance with its established rules, regulations or policies for assessing claims. The MFDA IPC shall also co-operate and provide reasonable assistance to the MFDA in administering an insolvency.**

5.1 Extent of Protection

As indicated in this application, the primary purpose of IPC is to provide protection to eligible customers of MFDA members if securities, cash and other property held in their account with a member are not available as a result of the member's insolvency.

The coverage principles in this respect will be similar in kind to that of the CIPF in Canada. Although the protection provided by the IPC is not insurance, many of the underwriting risks associated with insurance products are relevant to the IPC. Accordingly, the nature and extent of coverage must be related to the nature of the operations of MFDA members, the degree and kind of regulation to which they are subject and the financial resources available to pay for losses that

may arise. As in the case of CIPF, the risk is insolvency risk. This means that the direct cause of the loss must relate to the insolvency of the MFDA member and not to other causes such as change of market values. In addition, the losses must relate to the customer account activity of the customer and not commercial relationships with the MFDA member that would not be considered normal customer account transactions. For instance, a person who provides financing to the member would not be eligible for IPC coverage. It must also be established that the person claiming coverage has sufficient connection with the member to be considered a customer for regulatory purposes. The reason for this requirement is that the industry regulations primarily relate to customer account relationships and one of the ways in which the IPC will assess and underwrite risks is on the basis of such regulations being in effect and properly enforced. Eligibility criteria have been developed by the IPC and are attached as Exhibit C. The criteria are expected to be similar to those adopted by CIPF and pursuant to the *Bankruptcy and Insolvency Act*. A draft policy setting out the criteria is attached as Exhibit C and the final form and any amendments would be published by IPC from time to time for customer reference.

Coverage under the IPC will be for all eligible customers of an MFDA member regardless of the jurisdiction in which they reside (including whether or not it is a recognizing jurisdiction). The foregoing basis of coverage assumes that the IPC and MFDA will be able to assess risks and regulate the operations of members in every jurisdiction where they carry on business. If such regulatory oversight is not possible, coverage will not be available to customers of those members in the jurisdictions where suitable regulation by the MFDA cannot be assured. In Canada, MFDA is able to fully and directly regulate the business of its members to the extent of its by-laws and Rules in all provinces and territories except Quebec.

In Quebec, MFDA has negotiated a Co-operative Agreement with the Autorité des marchés financiers ("Autorité") and the Chambre de la sécurité financière. The agreement provides for the basis on which the Autorité, Chambre and MFDA will co-operate in the regulation of MFDA's members in Quebec, particularly in respect of prudential matters that relate to the solvency of members. MFDA and IPC are satisfied that the Agreement provides for a satisfactory basis on which MFDA and IPC can be assured that MFDA members will be regulated according to MFDA's Rules while respecting at the same time the jurisdiction of the Autorité and Chambre in Quebec. A separate application has been made by MFDA to members of the CSA for approval of the agreement.

Although MFDA expects to be able to conduct prudential regulation of its members in Quebec under the Co-operative Agreement, MFDA IPC coverage for customers with accounts in Quebec of MFDA members will not be provided initially. One of the specific stated premises of the agreement is that there be co-ordination of MFDA member customer protection between the parties as well as the Autorité (formerly the Fonds d'indemnisation des services financiers and the body in Quebec that provides compensation to financial consumer victims of fraud, fraudulent tactics or embezzlement by a Quebec registrant with whom they dealt). A separate agreement is contemplated for this purpose but discussions as to the effect and content of the agreement have not been completed. In the event of an insolvency of an MFDA member carrying on business in Quebec and elsewhere and which has customers with accounts in Quebec who have incurred losses, arrangements between MFDA IPC and the trustee in bankruptcy as to the co-ordination of the administration of the member's estate under the *Bankruptcy and Insolvency Act* (Canada) will have to be made.

Assessments will be collected on the basis of MFDA being able to regulate in the expected jurisdictions where its members carry on business. If MFDA is not able to regulate in all such jurisdictions and members withdraw from membership in MFDA or separate their businesses, assessments in respect of coverage prior to commencement of MFDA IPC coverage will be returned to members on an equitable basis. As indicated above, coverage to customers with accounts in Quebec will not be available initially and, accordingly, IPC assessments will not be made in respect of assets under administration in Quebec attributable to such customers.

MFDA and MFDA IPC expect to continue discussions with the Autorité in 2005 to co-ordinate their respective customer protection for MFDA members operating in Quebec. For the purposes of defining whether a customer dealing in Quebec with a member is eligible for IPC coverage, the location of the customer's account with the member is expected to be determinative. The actual residency of the customer and the jurisdiction in which the member holds the customer's assets may be irrelevant.

5.2 Type of Loss Covered

The experience of CIPF and other comparable compensation plans has been that while many losses can readily be determined as eligible for coverage, there are many claims that are less certain. It is important, therefore, for the IPC to state clearly to members and the public the principles and policies on which coverage will be available.

As in the case of the provincial plans that have been referred to above and CIPF, coverage is discretionary in the sense that the directors of the IPC have the ultimate discretion to determine whether a claim should be paid or not according to the circumstances. If the claim is squarely within the criteria proposed, it would be expected that the IPC would readily make payment. However, there may be extenuating circumstances wherein a claim might be technically eligible but it would be unfair or abusive to make payment. The MFDA and IPC are satisfied that an independent board with public representation can be relied upon to make such decisions.

The losses which the IPC will expect to cover are to be all securities, cash and other property held by a member in a customer account and which are not available to the customer as a result of the member's insolvency. In the Initial Application, it was proposed that coverage be restricted initially to mutual fund securities and cash related to the purchase and sale of such products. Other products were to be considered and recommended for coverage, as appropriate. MFDA and IPC are of the view that it is in the best interests of the public and MFDA members that expanded coverage be provided from that proposed in the Initial Application. There are a number of reasons for this view including the desire of members that coverage be similar to that of CIPF and the fact that participation in CIPF will be more easily accomplished if the coverages are similar. The review and comparison of the businesses and risks of MFDA members and investment dealers described in the introduction to this letter has satisfied MFDA and IPC that the increased coverage can be provided with the size of the fund increased to \$30 million as discussed in Section 4.1.

The securities or property to be covered by IPC must actually be held by the member in order for the coverage to apply. For instance, in the case of mutual fund securities, the securities are often held directly by the customer (i.e. in "client name") and the IPC would not protect that asset even though it may have been sold by the member to the customer. In such case, any loss to the customer of his or her property would not be caused by the insolvency of the MFDA member

because it is not responsible to account to the customer for the property. On the other hand, if the member holds the securities (which usually means that they are registered in its name) and reports to the client that it is holding the investment for the customer, the IPC would be expected to compensate the customer for any loss if the investment were not available on the insolvency of the member. A member may hold property for a customer that relates to a client name investment such as cash intended to acquire a mutual fund to be held in client name or the proceeds of the sale of such a fund. Property held in that circumstance by a member would usually be accepted to be covered by IPC because the member is responsible for the property while it is in its possession.

In the course of their operations, MFDA members may hold different kinds of assets for their customers and all such property held at the relevant date of insolvency will generally be entitled to coverage. Cash held by a member may rise from transfers by a customer to the member for specific purchases, proceeds of sales of securities, interest payments on GICs and other distributions. MFDA members primarily deal in mutual fund securities but other securities may also be held by a member for its customers such as government incentive securities, government bonds, partnership units and other so-called exempt securities. Examples of other kinds of property held by a member for a customer include segregated funds (insurance contracts), bank deposits and receivables from third parties such as depositories. All such cash, securities and other property held by a member for a customer is generally eligible for coverage regardless of the authority or registration of the member to hold it.

5.3 Non-Mutual Fund Affiliates

Many members of the MFDA have affiliates which distribute financial services and products such as insurance policies, deposit instruments, tax planning services, financial planning and others. The obligations of these affiliates to their customers, including customers who are also customers of the MFDA member, are not covered by IPC. Members will be required to ensure that records, advertising and servicing activities differentiate for their customers the entity they are dealing with and the fact that IPC coverage only applies to business resulting in customer assets being held by the MFDA member.

5.4 Limits on Compensation

The limit on IPC coverage per customer account is \$1 million. Each customer's accounts will be aggregated as one general account to the extent the accounts are held in the same capacity and circumstances. Registered plan accounts such as RRSPs, RIFFs, LIRAs, etc. are separate accounts and not aggregated with a customer's general account, but are aggregated themselves. Accordingly, the coverage limits per customer would be \$1 million each for the customer's aggregated general and aggregated registered plan accounts: see draft IPC policy attached as Exhibit C for details.

5.5 Exclusions from Coverage

The IPC will establish and maintain policies whereby persons not dealing at arm's length with the insolvent MFDA member, or who the IPC determines are, in whole or in part, responsible for the insolvency of the MFDA member, will not be covered by the IPC as eligible customers: see draft IPC policy attached as Exhibit C for details.

5.6 IPC Adequacy

The target size of the IPC assets has been determined by agreement between the MFDA and the IPC (see section 4 above). Annually the IPC directors will review and consult with the MFDA Board as to the adequacy of the IPC assets and recommend to the MFDA Board any changes it considers necessary or advisable.

5.7 Publicity

The IPC will be expected to make known to the public the existence and limits of the coverage that it provides. One aspect of this kind of publicity is to ensure that customers are clear as to the kind of coverage available and that they are not under the impression that protection is available when in fact it is not. In particular, advertising requirements and restrictions will be developed and imposed by MFDA Rule on members pursuant to which clear disclosure will be made of the facts that organizations associated with the member or using a similar name may not be covered by the IPC. MFDA's proposed Rule in this regard is attached as Exhibit D. This Rule will be supplemented by an MFDA policy describing the basis on which members may refer to IPC coverage: see Exhibit E. In addition, the fact of the IPC's coverage and dissemination of public information in that regard enhances the mutual fund industry and is generally regarded as being beneficial and in the public interest.

The IPC will be expected to provide brochures describing its coverage to the public as well as publishing any of its coverage policies and criteria and other information available. These publications may be available through members or on a website maintained by the IPC and/or MFDA. The IPC is expected to work with MFDA members to ensure that the existence of the IPC and the scope of its coverage is accurately understood by the public, MFDA members and customers of MFDA members.

5.8 Claims Process

The IPC will establish policies that provide for a fair and reasonable internal appeals mechanism whereby eligible customer claims that are not accepted for payment by the IPC staff, or by an appointed committee, are to be reconsidered by the Board of Directors. An eligible customer is not precluded from taking legal action against the IPC where the eligible customer has exhausted the IPC's internal claim review process and appeals process.

The insolvency of mutual fund dealers is often administered by a trustee in bankruptcy or court appointed receiver and the IPC would expect to have procedures that could be co-ordinated with the statutory or court ordered process. Initial decisions as to coverage for particular claims may be made either by IPC staff, designated agents or by the directors individually or by sub-committee. Customers will be entitled to have initial decisions denying coverage reviewed by directors, individually or in sub-committee, who were not involved in the prior decision. As long as the number of IPC directors is three, it is expected that a single director (in consultation with staff or a trustee in bankruptcy) will make initial determinations of claims, with the other two directors being available for a review or appeal. All decisions will be objective and consistent with previous IPC decisions according to the policies and coverage procedures from time to time. The directors may determine that the review is to be on a written record or permit attendance in person by the claimant.

6. FINANCIAL AND OPERATIONAL VIABILITY (INCLUDING RISK MANAGEMENT)

CSA Criteria

- (a) The MFDA IPC has sufficient financial resources for the proper performance of its functions.**
- (b) The MFDA IPC shall ensure that is it satisfied with the process to assess and contain risk of insolvency of MFDA members, taking into account the size of its assets and the level of assessments. Such process may include, but is not limited to, the following:**
 - (i) maintenance of minimum standards in the areas of: capital requirements; customer accounts; audits and questionnaires; field examinations; books and records; internal controls insurance; segregation; early warning system; reportable conditions; and most stringent rules; and**
 - (ii) monitoring and assessing the MFDA's process in ensuring that its members are in compliance with prudential regulations and any established minimum standards, and the MFDA's process in monitoring the on-going financial condition of its members. Such monitoring and assessment may include conducting examinations of the MFDA's process and examinations of members of the MFDA.**

6.1 Funding

The funding and assessment plans of IPC as described in Sections 4.1 and 5.6 of this application are designed to ensure that IPC will have sufficient financial resources for the proper performance of its functions.

6.2 Operations and Risk

In conducting its operations and managing insolvency risks of MFDA members, the IPC will rely primarily on the adequacy of the MFDA's prudential regulation and oversight of the CSA members which have recognized it or exert jurisdiction over its activities. The MFDA will agree not to change its prudential standards without prior notice to the IPC and providing the IPC an adequate opportunity to comment. The MFDA will advise the IPC on the MFDA's member review methodology and procedures. In addition, the MFDA will report to the IPC any circumstances involving a member that may be in financial difficulty.

The IPC believes that establishing minimum standards and conducting oversight of the MFDA's review of its members with respect to compliance with such minimum standards is not initially a necessary risk management tool for IPC. Under the arrangements with the MFDA, IPC will be able to carryout member reviews in certain circumstances.

The IPC will rely both on information provided by the MFDA and knowledge of circumstances otherwise obtained to determine that an MFDA member is in financial difficulty. The

circumstances in which a member may be in financial difficulty can vary widely, but both the IPC, the MFDA and their respective staff and advisors have experience in identifying certain conditions or activities that may indicate financial difficulties. In particular, the MFDA has implemented an early warning system which will require members to report information relating to their financial condition that will alert both the MFDA and the IPC. In addition, the IPC will require that the MFDA provide immediate notice to the IPC of certain conditions in respect of a member that may affect IPC and the fund.

6.3 Member Reviews

While the IPC will usually rely on the MFDA to conduct reviews of MFDA members for IPC purposes, the IPC reserves the right to conduct reviews of MFDA members in particular situations where IPC has concerns about the integrity of the fund or possible claims. The IPC Board will be entitled to conduct reviews for the purposes described above, but efforts will be made not to duplicate the functions of the staff of the MFDA. The IPC Board would request the MFDA staff or independent advisors to perform such reviews according to the criteria of the IPC and to report to the Board. Depending on the circumstance the degree of expertise may vary, but if there is the prospect of member insolvency, it may be necessary to rely on qualified professionals or other regulators in order to respond quickly and decisively as necessary. The ability of the IPC to conduct such member reviews will be provided for in an agreement to be made between MFDA and IPC and the By-laws of the MFDA.

6.4 Information Sharing Arrangements

The IPC will require information to assess not only whether the prudential standards and operations of the MFDA are appropriate for the coverage provided and risks incurred by the IPC, but also to deal with particular members which may be in financial difficulty. With respect to the former, the agreement(s) between the MFDA and the IPC will address general risk containment and the directors of the IPC may initiate discussions with the MFDA on any relevant subject. With respect to the latter specific risks to individual members, the IPC will have access to quarterly (or monthly) financial filings by members, information on early warning notices under MFDA Rules, meetings with MFDA staff and notice from the MFDA if any member may be in financial difficulty. This information collectively is expected to enable the IPC to assess whether the risks incurred by the IPC are adequately addressed by the MFDA and its Rules. If changes are necessary as a result of experience in the initial years of the IPC's operations and the MFDA as a self-regulatory organization, discussion can be initiated between the IPC, the MFDA, members of the CSA and other interested parties including MFDA members representatives. The risk assessment by the IPC is based in large part on the standards for members as set out in the by-laws and rules of the MFDA which have been (and will continue to be) reviewed and approved by members of the CSA. The MFDA will agree that any such by-laws or rules that relate to prudential standards for members will not be changed without prior notice to the IPC and the opportunity for the IPC to comment.

Information sharing arrangements between the MFDA and the IPC will be negotiated and entered into on the basis that their terms will ensure that IPC can fulfil its mandate and manage risks to the public and Plan assets on a reasonable basis. There are no legal constraints to the kind and amount of information that can be made available to the IPC by the MFDA. MFDA By-law 24 authorizes the MFDA to enter into information sharing arrangements of the kind

contemplated and all relevant information in respect of the operations and business of MFDA members is permitted to be provided to the IPC. Such permission is expected to constitute consent for the purposes of any relevant privacy legislation. The content of information anticipated to be provided will relate primarily to the prudential regulation of MFDA members and risks to the public and the IPC as a result of member insolvency. It is expected that certain core relevant information will be provided as a matter of course by the MFDA to the IPC, but the IPC or its directors and staff will be able to request access to any other relevant information available to the MFDA. Such requests may be made on a "spot" basis or when the IPC is aware of circumstances where the public and the IPC assets may be at risk because of the activities or financial condition of a member. The MFDA will agree to immediately inform the IPC in the event that a member is in financial difficulty.

6.5 Administration

The adopted roles and functions of the IPC will require administrative support. The intention is to minimize the administrative burden but certain minimum functions will have to be performed and at times, as in the case of a member insolvency or participation in the development of regulatory policy, the administrative demands will be high.

The primary responsibility for the management of the affairs of IPC as a corporation rests with the Board of Directors. The role of the Board, however, is to set policy direction for the IPC and to oversee senior management. The initial establishment of the IPC will likely require that the directors play a more active role in the conduct of the affairs of the IPC than they may do when the IPC is well established with mature operations. It has been proposed that a member of the Board, who may be the Chair, would dedicate more day-to-day management time to the initial operations of the IPC and as a public spokesperson for the IPC.

The IPC, as a corporation under the CCA, may appoint officers including the Chair of the Board, a president and possibly others such as a secretary. However, these roles are not expected to require full time attention. The initial recommendation for the IPC is that it contract the services of the MFDA for certain functions such as secretarial and those of a controller with the intention that within two or three years at least one dedicated staff employee may be hired by the IPC, if needed. The need for further staff will be assessed over time.

The IPC may retain as needed professional advice including legal, actuarial and other consulting services. In addition, the IPC will be required to appoint an auditor to audit and report on annual financial statements which have been prepared by management. The role and performance of the auditor will be monitored by the audit committee. In addition, the auditor may provide staff and administrative services as required.

The administration of member insolvencies including the review and payment of eligible customer claims is potentially the greatest administrative role IPC and its board will have. In the event of an insolvency, it is necessary that actions be taken promptly and decisively and technical expertise and experience is required. In such circumstances, IPC would expect to retain assistance from trustees in bankruptcy, legal and accounting advice and, likely, support from other organizations such as CSA members and CIPF.

7. REPORTING TO SECURITIES COMMISSIONS

CSA Criteria

- (a) The MFDA IPC provides the Commission with reports, documents or information, as reasonably requested by the Commission or their staff. The Commission and the MFDA IPC may review and revise such reporting requirements as necessary on an on-going basis.**
- (b) The MFDA IPC immediately notifies the Commission of:**
 - (i) any Reportable Conditions (as defined below) with respect to a MFDA member of which the MFDA IPC has been notified. Such Reportable Conditions mean any conditions which in the opinion of the official designated by the MFDA to be responsible for prudential regulation could give rise to payments being made out of the MFDA IPC, including any conditions which have contributed substantially to or, if appropriate corrective action is not taken, could reasonable be expected to:**
 - (1) inhibit an MFDA member from promptly completing securities transactions, promptly segregating clients' securities as required or promptly discharging its responsibilities to clients, other MFDA members or other creditors;**
 - (2) result in material financial loss;**
 - (3) result in material misstatements of the MFDA member's financial statements; or**
 - (4) result in violations of the minimum record requirements to an extent that could reasonably be expected to result in the conditions described in paragraphs (1), (2) or (3) above.**
 - (ii) any MFDA member who has withdrawn or has been expelled from participation in the MFDA IPC.**
- (c) The MFDA IPC files with the Commission, within 90 days after its fiscal year-end, its financial statements for the fiscal year prepared in accordance with Generally Accepted Accounting Principles, and a report by an independent auditor on its financial statements in accordance with generally accepted auditing standards.**
- (d) The MFDA IPC cooperates with the Commission and the MFDA, as reasonably requested, by sharing information regarding the MFDA IPC and MFDA members.**

7.1 General

The IPC will provide the appropriate members of the CSA with the information referred to in the Criteria.

8. RULEMAKING

CSA Criteria

- (a) **The By-laws, rules, regulations, policies, procedures, practices and other similar instruments (the “Rules”) of the MFDA IPC are designed to:**
 - (i) **ensure the going concern of MFDA members;**
 - (ii) **ensure reasonable funding of the MFDA IPC and assessments to MFDA members, without creating significant barriers to the mutual fund dealer industry and without compromising investor protection;**
 - (iii) **ensure the maintenance of a reasonable Plan size to afford protection for clients of MFDA members;**
 - (iv) **ensure that its business is conducted in an orderly manner so as to afford protection to investors.**
- (b) **The Rules of the MFDA IPC shall not :**
 - (i) **be contrary to securities legislation;**
 - (ii) **permit unreasonable discrimination between customers of MFDA members and between MFDA members; or**
 - (iii) **impose any burden on competition that is not necessary or appropriate in furtherance of securities legislation**
- (c) **The Rules of the MFDA IPC ensure that its business is conducted in an orderly manner so as to afford protection to investors.**

8.1 General

The rules, regulations and policies of the IPC will relate to investor protection and the means of raising and maintaining funds to pay losses. They will not govern the affairs of members directly as that function is primarily the responsibility of the MFDA and the members of the CSA. However, the MFDA will not change its rules relating to prudential regulation without giving the IPC the opportunity to comment. The IPC’s requirements and criteria relating to such matters as coverage, amounts, eligibility, size of funds, kinds of losses, etc. will all be developed in consultation with, or with the approval of, the MFDA and, where appropriate, the CSA. As a practical matter, the process of making Plan policies will be consultative and involve MFDA

Board and staff, MFDA members directly, staff of the CSA, and the IPC Board members. This process is familiar in the development of self-regulatory organization rules in Canada.

9. SUBMISSIONS

The IPC and MFDA respectfully submit that the proposed structure, policies and operations of IPC satisfy the proposed Criteria and draft Terms and Conditions and request that the IPC be approved as customer protection plan under the applicable securities legislation referred to at the beginning of this letter. The IPC and MFDA consent to the publication of this application for public comment by any of the Commissions.

Yours very truly,

signed "L.A. Wright"

Chair

MFDA Investor Protection Corporation

"L. Waite"

President and Chief Executive Officer

Mutual Fund Dealers Association of Canada