



## NOTICE AND REQUEST FOR COMMENT

### SASKATCHEWAN LOCAL INSTRUMENT 32-501 *DEPOSIT AGENTS*

#### **Introduction**

The Saskatchewan Financial Services Commission (the “Commission”) is publishing for comment proposed Saskatchewan Local Instrument 32-501 *Deposit Agents* (the “Local Instrument”).

#### **Purpose of the Local Instrument**

The purpose of the Local Instrument is to regulate intermediaries who trade in guaranteed investment certificates.

#### **Background**

##### **The Deposit Agent Rules**

The Local Instrument is intended to replace the Business Practice Rules set out in the decision of the Commission dated March 18, 1993 (“the Deposit Agent Rules” or “Rules”) that govern trades in GICs by intermediaries referred to as deposit agents. The Commission adopted the Deposit Agent Rules in response to the thefts of over \$1 million by individuals purporting to collect money from investors for the purchase of GICs and to transmit the money to financial institutions. The Rules were developed with the intention of minimizing the opportunity for fraud or theft by those acting as deposit agents.

##### **Why we are proposing Local Instrument 32-501**

The Deposit Agent Rules have been in place for over 10 years, and they have been reasonably successful in reducing instances of fraud or theft by deposit agents. However, the Commission is of the view that it is time to replace the Deposit Agent Rules with the Local Instrument. The Rules need to be updated and written in more clear language. They should also be put on a more sound legal footing. The Rules are guidelines, and if they are not complied with, it is difficult to take direct enforcement action. In cases where an individual deposit agent has misappropriated investors’ money, the Rules provide no clear means of recourse for investors.

The provisions in the Local Instrument are an attempt to remedy these shortcomings. The Local Instrument requires a deposit agent to register as a dealer and to be responsible for the actions of its officials and salespersons. The Local Instrument also requires a deposit agent to obtain insurance for losses resulting from the dishonest or fraudulent acts of its officials, salespersons and employees. Insurance coverage will provide the deposit agent with the means of compensating investors who suffer loss from the wrongful actions of its officials and salespersons. Because deposit agents, their officials and salespersons are registered, the enforcement provisions of the Act will apply.

## Summary of the Local Instrument

The following is a summary of the provisions of the Local Instrument:

- Section 1 defines terms used in the Local Instrument. “Deposit agent” is defined as a person who or company that trades in GICs, including accepting, receiving or soliciting money from an investor for transmission to a financial institution for investment in a guaranteed investment certificate. “Official” is defined as an individual who is a partner, director or officer of a registered deposit agent and who trades in GICs on behalf of the deposit agent. “Salesperson” is defined as an individual, other than an official, that is employed or engaged by a registered deposit agent to trade in GICs on behalf of the deposit agent.
- Section 2 removes the registration exemptions in clauses 39(2)(a)(iii), (b) and (j) of *The Securities Act, 1988* (the “Act”) for deposit agents, their officials and their salespersons.
  - Subclause 39(2)(a)(iii) provides an exemption for trades in bonds, debentures and other evidence of indebtedness of or guaranteed by specified financial institutions.
  - Clause 39(2)(b) provides an exemption for trades in certificates or receipts issued by trust companies for moneys received for guaranteed investment.
  - Clause 39(2)(j) provides an exemption for trades in securities issued by a credit union.
- Section 3 prohibits anyone from acting:
  - as a deposit agent unless they are registered as a dealer in the category of deposit agent;
  - as an official of a deposit agent unless they are registered as such; and
  - as a salesperson of a deposit agent unless they are registered as such.

Section 3 also prohibits individuals from acting as deposit agents.

- Section 4 grants certain exemptions from the registration requirement in section 3.
- Section 5 prohibits an official of a deposit agent from acting as a deposit agent on his own account or on behalf of any other deposit agent.
- Section 6 prohibits a salesperson of a deposit agent from acting as a deposit agent on their own account or on behalf of any other deposit agent.
- Section 7 prohibits a deposit agent from engaging unregistered salespersons or officials.
- Section 8 prohibits agreements between deposit agents, officials and salespersons that limit the liability of the deposit agent for the actions of an official or salesperson.
- Section 9 prescribes the form of application for registration as a deposit agent, official or salesperson.
- Section 10 exempts a deposit agent from the requirements in Part IV *Registration of The Securities Regulations* except for sections 15 [*prohibits interest in other registrants*] and 16 [*permits the Commission to prescribe additional conditions*].
- Section 11 requires a deposit agent to maintain insurance in the form of a financial institution bond that covers specified losses.

- Section 12 requires deposit agents to give notice when there is a change of control of the deposit agent.
- Section 13 requires deposit agents to maintain effective compliance systems.
- Section 14 requires deposit agents to report annually to the Commission.
- Section 15 requires a deposit agent's officials and salespersons to hold themselves out only under the name of the deposit agent when they carry on deposit agent business.
- Section 16 requires a deposit agent that operates a trust account to annually file a report of an auditor on the operations of the trust account.
- Section 17 requires deposit agents to maintain books and records to record their business transactions.
- Section 18 imposes conditions on deposit agents who do not have a place of business in Saskatchewan.
- Section 19 requires deposit agents to complete an application form when its officials or salespersons receive money from an investor for investment in a GIC. The application form must contain specified information, and be executed and distributed in a specified way. The application form must be approved by the financial institution with whom the money is invested.
- Section 20 sets out the circumstances in which an official or salesperson may sign an application form on behalf of an investor.
- Section 21 sets out the manner in which officials and salespersons may accept money from investors for investment in GICs.
- Section 22 requires salespersons and officials to pay over all money received for investment in a GIC to the deposit agent immediately upon receipt for the money.
- Section 23 prohibits a deposit agent from pooling money received from investors with money received from other investors.
- Section 24 provides that deposit agents, officials and salespersons shall hold money they receive from investors in trust.
- Section 25 specifies rules for how a deposit agent must operate its trust account.
- Section 26 specifies how a deposit agent must send money received from investors to a financial institution.
- Section 27 prohibits financial institutions from accepting money for the purchase of GICs from deposit agents, officials or salespersons unless they are registered.
- Section 28 requires a financial institution to have a contract with a deposit agent before its accepts money for investment in GICs from the deposit agent. The section specifies provisions that the agreement must contain.

- Section 29 specifies the manner in which a financial institution must make payment to investors for money due under GICs.
- Section 30 requires financial institutions to send confirmation notices to investors within 15 days of receiving an investor's money for investment in a GIC.
- Section 31 requires financial institution to report certain events to the Commission, including the names of new deposit agents, and the names of terminating deposit agents.
- Section 32 requires financial institutions to send annual reports to the Commission.
- Section 33 permits the Commission or Director to grant exemptions from the Local Instrument.

### **How Local Instrument 32-501 differs from the Deposit Agent Rules**

Most of the provisions of the Local Instrument are the same as those in the Deposit Agent Rules. The Local Instrument does not impose capital requirements on deposit agents or proficiency requirements on officials and salespersons. The fees payable under the Local Instrument will be the same as the fees now paid under the Deposit Agents Rules. However, there are the following differences:

1. The Deposit Agent Rules set out business practice rules for those who trade in GICs under the exemptions in clauses 39(2)(a)(iii), (b) and (j). The Rules indicate that if someone doesn't follow them, the Commission may have a hearing to determine whether to remove the right of that person to use the exemptions. The Local Instrument removes the right for deposit agents to trade GICs under these registration exemptions, and instead requires deposit agents to register as dealers.
2. Under the Deposit Agent Rules a deposit agent is required to obtain the Commission's approval before it can use sub-agents. There has been uncertainty about who is a sub-agent and who is an employee of a deposit agent. Under the Local Instrument all persons trading in GICs on behalf of a deposit agent are required to register as salespersons. Administrative and clerical staff are exempt from the registration requirement.
3. Officials of a deposit agent are required to register if they trade in GICs. Officials are partners, officers and directors.
4. Trades in GICs by officials and salespersons of mutual fund dealers that are members of the Mutual Fund Dealers Association are exempt from the requirements of the Local Instrument. This is provided that the trade is for the mutual fund dealer's account and through the mutual fund dealer's facilities. Trades by officials and salespersons through their own businesses are not exempt. This is because MFDA rules, and the insurance required under those rules, apply to a trade through a MFDA member firm. MFDA rules will not apply to trades in GICs for the salesperson's own business, and the provisions of the Local Instrument will apply.
5. The Local Instrument requires deposit agents to have insurance to cover such things as fraud or theft by its employees, salespersons and officials. The new requirement replaces the requirement under the Deposit Agent Rules for deposit agents to have a surety bond as a condition of the Commission's granting approval of its sub-agency arrangement.

6. The Local Instrument contains the following new provisions:

- a prohibition of agreements between deposit agents and its salespersons and officials that the deposit agent will not be liable for their actions;
- a requirement for deposit agents to have compliance systems and to supervise their salespersons;
- a requirement for salespersons and officials of deposit agents to hold themselves out under the name of the deposit agent; and
- a requirement for salespersons to turn money over to the deposit agent.

The table of concordance attached as Appendix A compares the provisions of the Local Instrument and the Deposit Agent Rules.

### **Authority**

The Commission has the power to make regulations adopting the Local Instrument pursuant to the following provisions:

- Clause 154(1)(a) of *The Securities Act, 1988* (the “Act”) authorizes the Commission to make regulations prescribing categories of persons and companies and the manner of allocating persons and companies to categories, including permitting the Director to make those allocations.
- Clause 154(1)(b) of the Act authorizes the Commission to make regulations prescribing requirements respecting applications for registration and the renewal, amendment, expiration or surrender of registration and respecting suspension, cancellation or reinstatement of registration.
- Clause 154(1)(c) of the Act authorizes the Commission make regulations to prescribing categories or sub-categories of registrants, classifying registrants into categories or sub-categories and prescribing the conditions of registration or other requirements for registrants or any category or sub-category, including:
  - (i) standards of practice and business conduct of registrants in dealing with their customers and clients and prospective customers and clients;
  - (ii) requirements that are advisable for the prevention or regulation of conflicts of interest; and
  - (iii) requirements with respect to membership in a self-regulatory organization.
- Clause 154(1)(d) of the Act authorizes the Commission to make regulations requiring unregistered directors, partners, officers, salespersons and employees of registrants to comply with all or any requirements prescribed pursuant to clause (c).
- Clause 154(1)(f) of the Act authorizes the Commission to make regulations prescribing requirements respecting the disclosure or furnishing of information to the public or the Commission by registrants.
- Clause 154(1)(h) of the Act authorizes the Commission to make regulations prescribing requirements respecting books, records and other documents that market participants shall keep, including the form in which and the period for which the books, records and other documents shall be kept.
- Clause 154(1)(oo) of the Act authorizes the Commission to make regulations exempting any person, company, trade or security from all or any provision of this Act or the regulations, including prescribing any terms or limitations on an exemption and requiring compliance with those terms or limitations.
- Clause 154(1)(qq) of the Act authorizes the Commission to make regulations removing any exemption

granted by this Act or the regulations, including prescribing any conditions or restrictions on removal of the exemption.

**Request for Comment**

We welcome your comments on proposed Local Instrument 32-501. Please submit your comments in writing on or before **November 15, 2004**. The Commission is sensitive to the additional cost that the insurance requirement will impose on deposit agents, and it is particularly interested in receiving comments on this point.

If you are not sending your comments by e-mail, you should also forward a diskette containing the submissions (in Windows format, Word).

Deliver your comments to Saskatchewan Financial Services Commission to the attention of:

Barbara Shourounis  
Director, Securities Division  
Saskatchewan Financial Services Commission  
6<sup>th</sup> Floor – 1919 Saskatchewan Drive  
Regina, SK S4P 3V7  
phone: (306) 787-5842  
fax: (306) 787-5899  
e-mail: bshourounis@sfsc.gov.sk.ca

We may not be able to keep submissions confidential because of the provisions of *The Freedom of Information and Privacy Act*.

**Dated September 7, 2004**

**APPENDIX A - TABLE OF CONCORDANCE**

<b>Local Instrument 32-501</b>	<b>Deposit Agent Rules</b>
Section 1 – Definitions	Definitions
Section 2 – Exemptions removed	New
Section 3 – Registration required	New
Section 4 – Exemptions from registration	Section 13
Section 5 – Officials to act for deposit agent only	New
Section 6 – Salespersons to act for employer only	Clause 12(a)
Section 7 - Engaging unregistered officials and salespersons prohibited	New
Section 8 – Non-liability agreement prohibited	New
Section 9 – Initial application for registration form	New
Section 10 – Exemption from registration requirements	New
Section 11 – Insurance	New
Section 12 – Change of control	New
Section 13 – Compliance systems	New
Section 14 – Annual reporting requirement	Section 9
Section 15 – Holding out	New
Section 16 – Trust compliance report	Section 9(g)
Section 17 – Business records	New
Section 18 – Business office	New
Section 19 – Application forms	Section 3
Section 20 – Deposit agent signing application	Section 5
Section 21 – Manner of payment	Section 6
Section 22 – Requirement to turn over money to deposit agent	Section 7 in part
Section 23 – Pooled money prohibited	Section 1
Section 24 – Deposit agent holds deposits as trustee	Section 2(g)
Section 25 – Trust accounts	Section 8
Section 26 – Remitting money to financial institution	Section 7
<b>PART 6 – FINANCIAL INSTITUTIONS</b>	
Section 27 – Dealing with registered entities	New
Section 28 – Contract with deposit agent required	Section 11(a)
Section 29 – Payments to investors	Section 10
Section 30 – Confirmation notice	Section 4
Section 31 – Reporting to Commission	Section 11(c)
Section 32 – Annual reporting	Section 11(c)
Section 33 – Exemption	New