All Shook Up

Earlier this month, Prime Minister Justin Trudeau bested President Donald Trump in an epic contest of wills (and arm strength) in the handshake that was seen around the world. After Japanese Prime Minister Shinzo Abe and US Supreme Court nominee Neil Gorsuch were thoroughly unprepared for (and possibly injured by) Trump's bizarre handshake style, Trudeau held his own in what has been heralded as one of the biggest displays of dominance in Canadian history.

Though we don't have anything this dramatic to offer in this month's Bulletin, we do hope you will find it illuminating in any event!

In this bulletin

In Brief: Hefty FINTRAC Penalty Target Revealed ● CRM2 Investor Website

1. Annual CSA Enforcement Report – No Contest

The Canadian Securities Administrators (CSA) released its 2016 Enforcement Report late this month, reporting a drop in both the number of new enforcement cases initiated as well as the number of cases concluded in 2016.

Despite this decline in overall enforcement activity, the CSA reported a significant increase in the amount restitution, compensation and disgorgement ordered in 2016, from $111,651,429 in 2015 to a whopping $349,654,379 in 2016. The historic amount of compensation ordered in 2016 was attributed largely to four Ontario Securities Commission (OSC) "no-contest" settlements totaling $299,243,586.

The OSC's use of no-contest settlements has become a powerful tool in the OSC's enforcement arsenal. No-contest settlements were first introduced in 2014

In Brief

Hefty FINTRAC Penalty Target Confirmed

The mystery surrounding a $1.15 million penalty levied last year by the Financial Transactions and Reports Analysis Centre of Canada (FINTRAC) has been solved. Manulife Financial Corp. has confirmed that its banking unit was disciplined for failing to comply with certain anti-money laundering rules.

The penalty is the largest imposed by FINTRAC to date, and the first time that a bank has been penalized since FINTRAC was given authority to impose monetary penalties in 2008.

In a written statement, Manulife referred to the infractions as "administrative lapses", and assured the

through OSC Staff Notice 15-702: *Revised Credit For Cooperation Program* with the goal of achieving a more efficient and timely resolution of enforcement matters. The defining feature of these settlements is that respondents can agree to settlement terms without any admission of wrongdoing. Critics of no-contests settlements decry this feature as creating a lack of transparency, and have voiced concerns that that the goal of deterrence cannot be met without accountability (and the accompanying risk of civil liability).

We will be taking a closer look at the OSC's use of no-contest settlements, from their 2014 inception to present day, in next month's AUM Law Bulletin. Stay tuned…

2. MFDA 2016 Year in Review – Out with the Old and In with the New

The Mutual Fund Dealers Association of Canada (MFDA) recently released its 2016 Year in Review and 2017 Initiatives Bulletin (the Bulletin). While the entire Bulletin is well worth the read, the Initiatives portion is particularly instructive in identifying the top areas of focus for the MFDA in the year to come.

Cybersecurity is unsurprisingly a central area of focus for the MFDA. The Bulletin references an upcoming mandatory cybersecurity risk assessment questionnaire for dealers, to be administered by an external cybersecurity consultant. As the CSA recently conducted a similar cybersecurity risk assessment, IIROC has issued report cards, and regulators of all stripes have issued cybersecurity guidance galore, firms should familiarize themselves with these initial regulatory expectations and ensure they are in compliance.

The MFDA Bulletin also confirms that suitability and know your client questions, as well as specific testing focused on the new CRM2 cost and performance reporting requirements will continue to be central areas of focus for the MFDA in their compliance exams, as will an assessment of internal controls for fee-based accounts.

Finally, in contrast to the CSA, the MFDA confirmed that 2016 was a record year for MFDA disciplinary proceedings. In particular (and as noted in a recent MFDA Notice), the practice of falsifying client signatures, whether done with the client's consent or not, will continue to be a key focus.

Please contact a member of our Regulatory Compliance Group if you would like to discuss any aspects of this Bulletin further.

3. New OSFI Deadline for Margin Requirements

Under OSFI Guideline E-22, *Margin Requirements for Non-Centrally Cleared Derivatives*, most Federally Regulated Financial Institutions (FRFIs) are subject to the mandatory exchange of variation margin beginning on March 1, 2017. On February 24, 2017, OSFI announced some limited relief from this deadline, citing the desirability of a globally harmonized implementation of the variation margin requirements in order to ensure a level playing field and a stable derivatives market for Canada.

For FRFIs transacting with counterparties that do not present a significant exposure to them, OSFI now expects those FRFIs to meet the variation margin requirements by no later than September 1, 2017. Investment funds and investment fund managers that have OTC derivatives agreements with FRFI counterparties (e.g., forward agreements, interest rate swaps, etc.) will therefore likely have a bit more time to complete and exchange the required documentation.

If you have any questions regarding either the new deadline or the new margin requirements generally, please contact your usual lawyer at AUM Law.

In Brief cont'd

public that the company had not enabled or facilitated money laundering.

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CRM2 Investor Website Launch

As part of the second phase of the client relationship model (CRM2) changes, the OSC has launched a new website to help investors navigate their new annual reports, which now include information about the performance of an investor's portfolio, and investment fees.

Investors can visit InvestmentReporting.ca for a breakdown on these changes.

4. Transacting in the Exempt Market?

If you are considering capital raising in the exempt market, talk to us! We can advise on the entire transaction from beginning to end and assist in reviewing or drafting the core documents of your deal, including a "bullet-proof" Exempt Market Distribution Agreement (EMD Agreement).

When drafting an EMD Agreement, it is especially important to do the following:

- clearly set out fees, payment terms and any non-monetary compensation;
- obtain important representations and warranties in order to "process hard-wire" the relationship through the EMD Agreement;
- include referral arrangement provisions in the EMD Agreement if being compensated for non-fund distributions such as managed accounts, or alternatively enter into a separate Referral Agreement;
- ensure that the limitation of liability clauses in the EMD Agreement comply with the standard of care imposed by the regulators for the registered entity; and
- ensure the EMD Agreement can be used as a tool to assist the EMD in meeting its know your product obligations.

Please contact your usual lawyer at AUM Law if you would like to discuss further.

5. Working From Home – Not Always a Casual Affair

Do you work from home regularly? Do you meet clients or conduct dealing or advising activities from home? Do you maintain records at home that are not duplicated at your firm's office? These are all questions to consider when addressing other business locations in your compliance policies and procedures.

The Investment Industry Regulatory Organization of Canada (IIROC) recently issued guidance to clarify their approach and expectations relating to work from home arrangements. NI 33-109 *Registration Information* defines "Business Location" as a location where the firm carries out an activity that requires registration, and includes a residence if regular and ongoing activity that requires registration is carried out from the residence or if records relating to an activity that requires registration are kept at the residence. The IIROC guidance sheds light on how other regulators may determine whether a residence should be reported as a Business Location and serves as a reminder to our clients that it is important to have appropriate compliance policies and procedures in place in place for other Business Locations.

Please call us and we can help you develop an appropriate compliance plan with respect to any other Business Locations you may have.

6. CSA's New Regulatory Sandbox

Following similar initiatives by provincial regulators, (including the OSC's LaunchPad), the CSA have announced the launch of their own, cross-Canada "regulatory sandbox", that will allow financial services firm to test leading edge products and services without regulatory burden. Firms with innovative business models such as online platforms, cryptocurrency, artificial intelligence, or regulation technology ventures can apply for leeway in the form of, for example, time-limited registrations or limited-audience testing.

The CSA will require applicant firms to submit a business plan detailing investor benefits and safeguards to minimize risk, and may also require firms to undergo live environment testing.

Please contact us if you would like to further discuss this initiative.

Frequently Asked Questions

> Is there a requirement to carry out a KYC/Suitability assessment for ongoing transactions under an automatic DRIP program?

Under section 13.3 of NI 31-103, a know your client (KYC)/suitability assessment is required when a registrant makes a recommendation to or accepts an instruction from a client.

With automatic dividend reinvestment plans or DRIPs, this suitability assessment should take place when the plan is set up initially and only made again if there is a further recommendation. Ongoing automatic transactions under a DRIP do not in our view constitute recommendations.

Despite this, however, it is important to keep in mind the requirement for ongoing updating (at a minimum once annually) as per CSA Staff Notice 31-366.

News & Events

Speaking Engagement

Susan Han will present at the upcoming Ontario Mortgage Investment Companies Association's Member meeting this Thursday, March 2.

Susan will be giving an update on certain securities law developments of interest, in particular (1) some myths (and the more complex and nuanced reality) surrounding the so-called 10% concentration rule for exempt products for EMDs; and (2) the jurisdictional reach of the securities regulator under the law (or, No, Actually, You Can't Tell OSC staff to "Come Back With a Warrant" if they begin asking questions about the operations of your MIC).

ONMICA
Ontario Mortgage Investment Companies Association

Upcoming Event

We are excited to announce that on **May 9, 2017**, we will be holding our **1st Annual AUM Law Conference**, where we plan to discuss salient issues prevailing in the marketplace that impact our clients. Though seating will be limited, we will do our best to ensure access to all Conference materials. Stay tuned for further details!

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