

Alternative Proposal

DISCUSSION PAPER -CLIENT RELATIONSHIP MODEL -PROPOSED RELATIONSHIP DISCLOSURE DOCUMENT and ANNUAL PORTFOLIO REVIEW - ESTABLISHMENT OF ALTERNATIVE POLICY 12

OVERVIEW

This is an alternative model to the one developed by the IDA to implement the key Client Relationship Model (formerly Fair Dealing Model) disclosure recommendations and performance reporting recommendations.

This alternative proposal is based on content included in the sample Relationship Disclosure Document reviewed and commented on by approximately 370 registered advisors who participated in the IDA sponsored 11 city broadcast consultation held on August 16, 2006. However, it should be noted that this alternative model provides an access approach and not a mandated client acknowledgement which was troublesome to those participants.

This alternative model relates to account relationship disclosure, which also sets out an annual portfolio review as an alternative to the previous performance reporting recommendations. This proposal will require the same disclosures for managed, advisory and order-execution service account types.

OBJECTIVE

The objective of this policy is to enable clients and firms to be better informed about the following aspects of their account relationship:

- . The type of account relationship they have entered into;
- . The roles and responsibilities of the Member firm / advisor and the client; and
- . The disclosures the client will be provided up-front, at time of transaction and on an ongoing basis.

The policy will require that every Member firm provide its clients with or with access to a Relationship Disclosure Document (RDD). The RDD will inform the client of:

- . A general description of the types of products and services offered by Members;
- . The Member firm's obligation to assess investment suitability at time of trade and whether or not the Member firm will undertake an annual portfolio review at the option of the client;
- . The investment risk factors clients must consider when making investment decisions;
- . Any Member firm conflicts of interest;
- . A statement of the need for clients to meet with their advisor to discuss their account holdings and investment strategy, if a client wishes;
- . The responsibility of clients to advise the Member firm of material changes in personal circumstances or investment objectives.

The purpose of the RDD is to assist clients in understanding the nature of the services that will be provided by the Member firm / advisor and what the client should do to ensure a satisfactory ongoing relationship.

Each Member firm will provide to, or make available to clients a standardized industry disclosure document set out in an attached Schedule A to proposed Policy No. 12 or may create its own version of this disclosure document, which will not replace new account opening requirements and guidelines (revised versions of Form No. 2 New Client Application Form).

EFFECT AND BENEFIT

This alternative model would have many benefits over the IDA RDD including:

- a simplified and more concise document in that there is one policy instead of three and it applies to all clients and all types of accounts
- avoiding the multiplicity of documents for clients who have multiple types of relationships
- reducing costs in supervision, record-keeping and mailing

- as clients sign-off is not required, no contract is created thus the RDD truly becomes an education disclosures tool, therefore including the industry in the education function
- the access constitutes delivery concept would also result in client education as clients would discover additional disclosures and information when they go to industry websites to access their RDD
- no ongoing amendments other than if the generic document is altered, but it is still accessible to clients by notice. It is then left up to the firms to deal with in terms of the products and services that they provide, which is a marketing and competition issue, as is currently the case.

DETAILED ANALYSIS

1) PROPOSED POLICY and STANDARDIZED RELATIONSHIP DISCLOSURE DOCUMENT

Alternative Policy No. 12 simply requires that a standardized RDD, attached as Schedule A, be provided or be made available to all clients regardless of the type of account relationship. Thus this RDD would be used for advisory, order-execution service and managed accounts. The advantage of a standardized document is that it creates one single document which avoids customization to the types of clients and services, thereby avoiding the multiplicity of documents for clients who have multiples types of relationships.

Each Member firm will use this industry standardized version of the RDD. However, Members have the option to create its own version of the RDD, which must be in a form acceptable to the Association and approved by a partner, director, officer or branch manager. The RDD will not take the place of “know your client” forms, account agreements or disclosure documents.

The standardized RDD is not a contractual arrangement and therefore does not prescribe supervisory requirements such as audit trails and approvals by partners, directors, officers or branch managers. Further, the standardized RDD does not require a client signature or acknowledgement. The removal of client sign-off would avoid having to mail it to clients and thereby reduce mailing costs. Furthermore, because there would be no client signature or acknowledgement required, contract issues would be removed from the equation, and the RDD would truly be an education disclosure tool and hopefully spark interested clients to ask the questions which are prompted in the document.

The standardized RDD should be thought of as an arrangement between the client and advisor which outlines the level of service a client should expect. This would level the playing field between the client and the advisor by ensuring the client is engaged in the relationship and is encouraged to be an active participant.

The RDD would be sent by mail or via a notice to clients that the RDD is available upon request. This notice would be provided by mail, on a client account statement or by other means chosen by the firm. Clients would be instructed that the RDD is available, for example, on the Member’s website. Members would provide notice of the availability of the RDD when an account is first opened and make the RDD available on an annual basis for existing clients.

The access constitutes delivery concept also provides additional benefits in that if clients are required to go to their firm’s website or that of a regulator or securities commission to receive the RDD, it would result in clients being exposed to other types of documents and disclosures. Consequently, client education and awareness would occur.

Characteristics of the Standardized Relationship Disclosure Document

The RDD that is provided to or made available to a client must:

- Contain certain core information, however, the form and presentation of a non-industry standardized document will not be prescribed;
- Be written in plain language;
- Include a description of the roles and responsibilities of the Member firm under the terms of the relationship established with the client;

If a non-industry standardized version is used, be in a form acceptable to the Association;
If a non-industry standardized version is used, be approved by a partner, director, officer or branch manager;
If the Member wishes, an audit trail may be maintained that evidences its delivery to or accessibility to all clients;
Describe the account relationship;
Describe the services offered by a firm;
Describe the account types available generally;
Describe the products that are available generally;
Describe investment risk factors and types of risk to be considered when making investment decisions.
Describe the “know your client” information to be collected to properly assess suitability;
Inform you of your option to meet with your advisor for an annual portfolio review;
Describe conflicts of interest in accordance with applicable by-laws, rules, and regulations;
Describe fees and service charges generally;
Describe the frequency of account reporting;
Describe the client responsibilities;
Itemize account documents the client must receive; and
Describe the methods of communication with the firm and contact points.

Additional Information

In addition to the items listed above, Members may elect to attach the following appendices to the standardized RDD:

Products – a detailed description of the products offered by the Member;
Conflicts of Interest Management – a detailed description of any conflicts of interest that the Member may have; and
Fees and Service Charges – a customized fee schedule.

Annual Portfolio Review

The annual portfolio review is not a contractual requirement but a service level arrangement. This service level arrangement outlines the mutual expectations of both parties. It does not require a formalized supervisory framework. If a Member chooses, they could develop supervisory and audit policies around this annual portfolio review or could develop a client satisfaction survey to determine if advisors are providing the services that clients have indicated that they wish to receive. Alternatively, a Member could execute random samplings as a means of supervising their advisors.

This annual portfolio review replaces the concept of a periodic suitability review and annual account performance reports. The costs of implementing a periodic supervisory review would be onerous as new supervisory processes would need to be developed.

With respect to annual account performance reports, there are significant operational difficulties in terms of the data that would need to be imputed and the lack of accuracy and consistency surrounding the results. The SRO Operations/Technology Subcommittee outlined the systems and technology difficulties for the types of performance reports recommended by the SRO drafting group. It would be an incredibly complex undertaking as there are numerous variables in producing the reports that would complicate implementing a standardized requirement. Systems and technology problems would lead to differences among results, especially due to the differing expectations, needs and wants of clients. As a result, rather than having the account statements outline performance reporting results, these matters should be discussed and explained in the context of a meeting between a client and advisor. The client would determine with the advisor the frequency of these meetings

(annually or more often). This portfolio review would examine the performance of the account/portfolio, the account holdings and on going investment strategy.

2) NEW CLIENT ACCOUNT OPENING REQUIREMENTS and GUIDELIENS FOR RETAIL CLIENTS

The IDA proposal requires three different policies for advisory, order-execution service and managed account clients. As part of these policies, the New Client Account Opening Requirements and Guidelines were included as Part 2. However, under the new alternative model, a determination remains to be made as to where in the IDA Rulebook these know-your-client documents would reside.