

**Investment Dealers Association of Canada
Response to the Recommendations of the
Alberta Securities Commission**

**2003 ASC OVERSIGHT AUDIT REPORT
PRAIRIE REGIONAL OFFICE**

Action Items

SALES COMPLIANCE DEPARTMENT

1.0 REVIEW OF FINDINGS IN THE 2001 REPORT

1.1.1.2 Verification of Controls Over Suitability

report page 3

ASC Recommendation

ASC Staff believe IDA Staff should provide further documentation on resolution of suitability concerns noted. IDA Staff must be able to conclude, with documentation, that suitability problems they identify in their audits are unrepresentative for the Member. Otherwise, they should require the Member to implement supervision and control procedures to ensure that suitability is properly reviewed.

IDA Response

We agree that the purpose of sampling New Client Application Forms and comparing them to a small sample of the client's holdings is to determine whether or not there is a serious failure in the firm's supervision and control procedures. When circumstances indicate there is a serious failure, the firm is required to improve its procedures; correcting the documentation of the accounts selected is secondary.

We take into account the imprecision of the process when determining if there is a failure in procedure. We compare the holdings in an account to the investment objectives and risk profile of the client as recorded on the New Client Application Form. There are many reasons for discrepancies such as differing views of the risk categorization of each security or changing market conditions, which may have caused high risk securities to become a larger portion of the client's holdings than planned.

We will ensure that our Sales Compliance Officers are diligent and thorough in making their assessment.

1.1.2 Timely Completion of Sales Reviews

report page 5

ASC Recommendation

ASC Staff believe the IDA should document the following:



1. *Actions of the SC Department to address their failure to meet the national benchmark in 2001 and 2002.*
2. *An update on the status of the SC Department's ability to meet the benchmark in 2003.*
3. *A summary of the specific components of the examination letter preparation process that requires 15 weeks to complete.*
4. *The circumstances in which the SC Department would not meet the 15-week deadline.*

IDA Response

Until 2001, there was one manager responsible for both the financial and sales compliance departments. In order to deal with the increased work load, a new Sales Compliance manager was hired effective July 2001. The delay in file completion was caused by the transition period with the new manager taking over.

There are currently three sales compliance officers in the department, in addition to the manager.

The benchmark target is to complete 60% of examinations within 15 weeks from the end of the field work. In 2003, the Calgary office issued 58% of its reports within 15 weeks. We are always looking for ways to improve our benchmark performance. Completion of a sales compliance examination involves completing the file documentation, a review of the file by the Sales Compliance manager and meeting with the member to discuss the findings, culminating in finalizing and issuing the SC report to the member. Completion of the files can take longer than 15 weeks due to compliance officers being engaged on more than one assignment where priorities would be determined based on risks involved, among other factors.

As at August 2004, the Calgary office has met its 60% benchmark where the average completion of all reports was 13.7 weeks.

The circumstances under which we might not meet the 15-week benchmark include employee sickness, staff turnover, other pressing work projects, training needs and vacations.

1.1.3 Response Follow-up

report page 6

ASC Recommendation

ASC Staff believe IDA Staff should require Member responses to document the manner in which an issue will be resolved, the time period for resolution and, if the issue is significant, evidence of resolution.



IDA Response

We agree with the recommendation and believe that we currently operate in a manner consistent with it. We will ensure that evidence of resolution is obtained from members.

1.1.4. Branch Office Reviews

report page 7

ASC Recommendation

In order to increase review coverage of the branch offices, ASC Staff believe that the SC Department should, as part of its head office examinations, expand review of the Member's branch office review program. Increased review should include review of a sample of the Member's branch reviews.

IDA Response

The recommendation is consistent with our current practices. Our head office reviews do include an assessment of the firm's branch audit review program.

1.1.5. Sub-Branch Office Reviews

report page 9

ASC Requirement

ASC Staff believes the SC Department should implement RR interviews as part of the examination process.

IDA Response

We are implementing a sophisticated risk-based sales compliance model to help us objectively measure the risk of each firm. At the same time, we are analyzing data that we have been collecting since October 2003 about complaints, civil actions and/or criminal charges for individuals and firms. Our intention is to be able to identify high-risk firms, branches, sub branches and individuals and to tailor our oversight strategies accordingly.

We can see some value to interviewing individuals, which may uncover isolated examples of inconsistencies between the expectations of a firm's supervisor and the understanding of that individual. While representative samplings can be reasonably achieved, it would take several, time-consuming and logistically problematic RR interviews to produce comparably broad and actionable results. Consequently, used routinely, we think it would prove an inefficient method of collecting information.



We strongly prefer to direct our resources using the risk-based approach. If a branch is shown to be particularly high risk, as befits each situation, we will interview individuals of interest as part of either a sales compliance review or a full investigation.

1.1.6 Risk Assessments

report page 10

ASC Recommendation

The IDA should implement procedures for identifying and increasing examination coverage of areas with high risk.

IDA Response

We agree and believe that we partially adjust our review as is documented in the Risk Assessment completed prior to the review of any firm or branch. Among other things, our newly revised Sales Compliance Risk Assessment Model is helping to refine that process further.

1.1.8 RR's Operating In Provinces Where They Are Not Registered

report page 12

ASC Recommendation

ASC Staff believe that significant violations of securities laws uncovered in an audit, such as trading in jurisdictions in which a Member or an employee of a Member is not registered, should be included in the examination letter. IDA Staff should also consider referring these cases to the securities commission for enforcement action.

IDA Response

The Association and its staff are well aware of securities legislation in other provinces and the United States. The Association has led the efforts to get specific state exemptions for Canadian tax advantaged accounts: we have published a Notice on the topic, forced our Members to create US subsidiaries that comply with US law, and our Members have closed many US based accounts, and/or spent significant amounts of money and time to become registered there. We have also worked with another commission on an investigative matter to determine the interest of various American states in prosecuting one of our Members who does operate some American accounts. These accounts operate under exemptions, many of them supported by specific legal opinions by US lawyers.



We will continue to discipline if there is clear evidence of a wilful and widespread violation of registration requirements or if a registration violation is part of a related disciplinary matter.

1.2 NEW EXAMINATION FINDINGS

1.2.1 Sample Size Selection and Documentation

report page 12

ASC Recommendation

Document of population size, determination of sample size, and the method of sample selection are necessary to have an adequately documented audit. ASC Staff believes that these should be included in the IDA's audit files.

IDA Response

We agree and will amend our review procedures to ensure the sampling process is well documented.

1.2.2 Identifying the Same Deficiency During a Subsequent Examination

page 13

ASC Recommendation

The SC Department should ensure that they are documenting their review of previous examinations. Deficiencies repeated from a previous Member examination should be clearly identified as such in the examination report.

IDA Response

We agree. It is our practice to list all of the previous deficiencies in the Risk Assessment prepared before the next audit commences. In this way, the Sales Compliance officers who prepared the review are well aware of the firm's past failings. We may need to improve our documentation by making it clear that the matter was followed up and there was no finding.

FINANCIAL COMPLIANCE

2.1 REVIEW OF FINDINGS IN THE 2001 REPORT

2.1.1.2 Timely Issuance of Field Examination Reports

report page 16

ASC Recommendation

ASC Staff believe the IDA should document the following:



1. *An update on the status of the FC Department's ability to meet the benchmark in 2003.*
2. *Outline the circumstances in which the FC Department would not meet the eight-week deadline.*

IDA Response

1. Five examination letters were issued between September 30, 2003 and December 31, 2003. The average number of weeks to issue a report to the Member was 6.4 weeks. In addition, three biennial letters were sent between September 30, 2003 and December 31, 2003.
2. We did not exceed the eight-week deadline in any of the remaining reviews. We may miss deadlines due to employee illness, or staff departures or unexpected problems uncovered during an exam. We are always rotating through our firms so an examiner is in the field while a firm is responding to a report. If a serious matter arises in the field, the examiner may be necessarily distracted from completing earlier review. Findings involving possible deficiencies or contested and crucial findings can cause a significant number of unbudgeted hours to be spent.

2.1.1.3 Timely Follow-up of Examination Responses

report page 18

ASC Recommendation

The IDA should develop a policy about when to issue second response letters to ensure that such letters are issued in all appropriate circumstances.

IDA Response

We are implementing an automated work paper system as a national initiative and one outcome of this will be timely follow-up to response letters in the workflow process. Although we agree that a follow-up is important, major issues are pursued and resolved and in the rare case where a more minor issue is not resolved, we check in the subsequent audit that the prior year queries have been addressed.



2.2 NEW EXAMINATION FINDINGS

2.2.1 Sample Size Selection and Documentation

report page 23

ASC Recommendation

Documentation of population size, determination of sample size, and the method of sample selection are necessary to have an adequately documented audit. ASC Staff believe that these should be included in the IDA's audit files.

IDA Response

We agree and will ensure that better documentation is kept.

2.2.2 Review of PDO's Accounts

report page 23

ASC Recommendation

The FC Department should ensure that a significant sample of PDO accounts are reviewed and that the working papers clearly document the review as a PDO account review.

IDA Response

We agree.

2.2.3 Risk Assessments

report page 24

ASC Recommendation

IDA Staff should look at repeated errors as a possible indication of systematic problems with the Member. Changes in risk ratings of a Member should include consideration of errors in the Member's submissions.

IDA Response

We agree.



REGISTRATION

3.1 REVIEW OF PREVIOUS AUDIT FINDINGS

3.1.1.1 Review Procedures of Staff

report page 27

ASC Recommendation

The Registration Manager should randomly select applications for review to ensure that they are being handled appropriately.

IDA Response

We agree.

3.2 NEW EXAMINATION FINDINGS

3.2.1 Quarterly Exemption Reporting

report page 30

ASC Recommendation

The IDA should develop procedures to ensure that the quarterly exemption report is accurate and complete.

IDA Response

We agree.

3.2.2 Branch Manager

report page 31

ASC Recommendation

A sub branch file, for which supervision is not provided by an Alberta Branch Manager, must contain IDA Staff's explanation as to why they concluded that the supervision procedures were adequate.

IDA Response

We agree. The IDA has procedures in place to evaluate the supervision arrangements for a sub-branch, based on the current responsibilities of the supervisor, frequency of visits to the sub-branch office by the supervisor and compliance with IDA Policy 2.



3.2.3 Exemption Applications

3.2.3.1 Branch Manager

report page 31

ASC Recommendation

The IDA should train staff and develop procedures to ensure that applicants in the same fact situations receive the same regulatory results.

IDA Response

We agree. Since the audit period an on-line procedures manual for the Calgary office has been implemented. Use of the manual should reduce any inconsistencies found between Registration Officers' reviews.

3.2.3.2 District Council Review

report page 32

ASC Recommendation

The IDA should ensure District Council members understand that the delegation of registration authority should not be used to subvert the application of securities laws.

IDA Response

We understand that the issue related to an individual who was granted an exemption from the full time employment requirement by two District Council members because they believed that the rule was outdated. We will have the Regional Director raise the matter at a District Council meeting.

MEMBERSHIP PROCESS

4.1 REVIEW OF PREVIOUS AUDIT FINDINGS

4.1.1 Quality of New Member Applications

report page 35

ASC Recommendation

The final review before granting membership should ensure that all checklists have been completed and that all membership requirements have been met.

IDA Response

We believe that the checklists were contained in a Registration file. We agree that the new Member file should contain a copy of those checklists and amend our procedures.



ENFORCEMENT DEPARTMENT

5.1 EXAMINATION FINDINGS

5.1.1 Communication

report page 36

ASC Recommendation

ASC Staff recommend that formal department meetings for CCB and Investigations should be implemented going forward. Suggestions for agenda items should be considered from all employees. Managers could pass on relevant information from their management meetings. Perhaps the VP Western Canada Member Regulation could attend these meetings periodically to foster two-way communication between senior management and individual employees within the Enforcement Department.

Please indicate what steps the IDA will take to address this recommendation.

IDA Response

Subsequent to the Audit period, regular CCB team meetings were implemented. Investigations staff and Enforcement Counsel have met bi-weekly throughout 2004.

5.1.2 Key Performance Indicators for the Central Complaints Bureau report page 37

ASC Recommendation

ASC Staff recommend that the IDA consider either modifying the objective of resolving 80% of complaints within 75 days for ComSet files. Two possibilities include having the time allowed to investigate start once the CIO receives a response from the Member firm, or increasing the timeframe applicable to ComSet files to 100 days.

Please indicate what steps the IDA will take to address this point.

IDA Response

Senior IDA Staff are constantly reviewing our KPI's as part of our annual business planning process. We recognize that the 75-day response is more difficult for ComSet files. However our benchmark requires us to make the 75-day timeframe 80% of the time and the remaining 20% accommodates ComSet and other files. We will continue to monitor the KPI and if it becomes a problem, we will consider an amendment.



5.1.3 Files Closed because the Respondent is no longer a Registrant report page 38

IDA Response

It is the Enforcement Department's policy to pursue disciplinary action against individuals who are no longer registered where the misconduct is serious. The investigation referred to had a unique circumstance in that the conduct dealt with a personal matter - cheque kiting. Our reference to "weakness of the facts" was the anticipated difficulty in presenting sufficiently clear and convincing evidence of cheque kiting to a disciplinary panel. In determining whether to pursue formal disciplinary action we considered that the conduct was unrelated to the securities business, would be difficult to present clearly to a panel, did not result in any loss to the individual's bank, and resulted in a loss of employment for the individual. These factors combined with the fact that the individual was no longer a registrant led us to our conclusion. Since the conduct was outside of the firm's business, we were satisfied that there were no internal control failures at the firm.

5.1.4 Referrals to Sales Compliance report page 40

IDA Response

We agree that there are circumstances when enforcement action is not possible or inappropriate yet the information should be passed on to Sales Compliance. We have supplied information informally to Sales Compliance before and we do not believe there is any loss of key information. Nonetheless, our initiatives to implement a Sales Compliance Risk Model and the sophisticated analysis of patterns and trends garnered from ComSet data, will formalize the process. We will shortly be able to detect firms, branches and sub branches that have an abnormally large number of complaints regardless of our own disciplinary action(s).

5.1.5. Supervision report page 41

ASC Recommendations

ASC Staff recommends that, like investigations, CCB comments on adequacy of supervision on every report.

Staff recommends that a ComSet check also be done on the branch involved to identify any systemic supervision or internal control problems.

Please comment on these recommendations.



IDA Response

We agree that CCB staff should always be cognizant of supervision failure when reviewing a file. The Enforcement Department's most important strategic initiative for 2004/05 is to develop criteria and enhance methodologies to investigate systemic supervision failure. Your recommendations will be considered in developing this strategic initiative.

5.1.6 Closing Files in CTS Prior to File Completion

report page 41

ASC Comments

Please confirm what action has been taken to ensure compliance with the IDA policy.

IDA Response

We agree with the observations of ASC Staff and will inform our staff that a case should not be closed until closing correspondence has been sent. There appears to have been some confusion on whether the decision to close the file was sufficient to close a case in CTS or whether the final caution and/or closing letters are required to have been sent.

5.1.7 Exhibit Log Policies

report page 41

ASC Comments

Expected practice in this area should be clarified and IDA policy changed as necessary. The decision on this matter needs to be clearly communicated to local management and employees.

Please confirm what action will be taken to address this point.

IDA Response

The Exhibit Policy is currently being revised. The revised policy will indicate that the investigator is responsible for completing exhibit reports.



5.1.9 Regional Director's Job Description

report page 42

ASC Recommendation

Please ensure that this job description is updated.

IDA Response

We agree.