

# IIROC NOTICE

## Rules Notice

## Request for Comments

## Dealer Member Rules

*Please distribute internally to:*

Legal and Compliance

Operations

Senior Management

Retail

## Comments Due: July 8, 2016

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**16-0052**  
**March 10, 2016**

## Re-Publication of Proposed IIROC Dealer Member Plain Language Rule Book

### Executive Summary

IIROC has undertaken a project (the **PLR Project**) to rewrite, reformat, rationalize and reorganize its Dealer Member Rules in plain language. The following are the intended benefits of the PLR Project:

- (i) improving the clarity and understanding of the Dealer Member Rules;
- (ii) streamlining the Dealer Member Rules by focusing on core requirements and moving non-essential details to guidance;
- (iii) eliminating obsolete, duplicative and unnecessary requirements;
- (iv) reorganizing the rule structure in a more logical fashion; and
- (v) clearly stating the objective of each rule.

The primary objective of the PLR Project is to develop rules that are organized, clearer and more concise, without changing the substance of the Dealer Member Rules themselves. However, during the course of the PLR Project, a number of existing Dealer Member Rules were identified that also required substantive revisions in order to update and improve regulatory policy and, in some instances, to conform to requirements under National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations (NI 31-103)*.

The PLR Project was initially drafted and published for comment in a number of discrete tranches. IIROC's current Dealer Member Rules were grouped into seven different series (described in section 1.2 below) to create the discrete tranches. We have now compiled the separately published tranches

to create the proposed IIROC Dealer Member Plain Language Rule Book (**proposed PLR Rule Book**) and are republishing for a 120-day comment period.

#### **How to submit comments**

Comments are sought on the proposed PLR Rule Book and should be made in writing. Two copies of each comment letter should be delivered within 120 days from the publication date of this Notice.

One copy should be addressed to the attention of:

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The second copy should be addressed to the attention of:

Market Regulation  
Ontario Securities Commission  
19th Floor, Box 55  
20 Queen Street West  
Toronto, Ontario, M5H 3S8  
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Those submitting comment letters should be aware that a copy of their comment letter will be made publicly available on the IIROC website ([www.iiloc.ca](http://www.iiloc.ca)) under the heading "Notices" and sub-heading "[Dealer Rules All – Request for Comments – Re-publication of Proposed IIROC Dealer Member Plain Language Rule Book](#)".

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## 1. Background

### 1.1 Consolidated Rules Project

Prior to the formation of IIROC in 2008, a project (the **Consolidated Rules Project**) was commenced by IIROC's predecessor, the Investment Dealers Association of Canada (**IDA**), with the objective of having one set of consolidated rules that govern the conduct of all the people and entities it regulates – Dealer Members and their Approved Persons, exchanges and alternative trading systems.

Currently, IIROC has three sets of rules that govern the people and entities it regulates comprising:

- Transition Rules (these rules dealt with transition issues upon the merger of Market Regulatory Services Inc. and the IDA in 2008);
- Dealer Member Rules; and
- Universal Market Integrity Rules (**UMIR**).

The Consolidated Rules Project has three phases.

- (i) The first phase is the consolidation and plain language rewrite of UMIR and Dealer Member Rules relating to:
  - enforcement, investigations and hearings, compliance examinations; and
  - registration-related regulatory approvals and reviews(referred to in this Notice as the **Consolidated Enforcement Rules**)<sup>1</sup>. The Consolidated Enforcement Rules will be added into the proposed PLR Rule Book upon completion of the PLR Project.
- (ii) The second phase is the PLR Project – discussed in detail below – which deals with all Dealer Member Rules, other than (1) those that were included in the Consolidated Enforcement Rules<sup>2</sup> and (2) current Dealer Member Rules which are the subject of discrete proposals that are currently ongoing (these are discussed in more detail in section 1.5).
- (iii) The third and final phase will combine the implemented versions of the proposed PLR Rule Book and the Consolidated Enforcement Rules with UMIR to form a single consolidated IIROC Rule Book.

### 1.2 PLR Project – structure of proposed PLR Rule Book

The proposed PLR Rule Book consists of seven series of rules as set out below. Please note that there are two additional series – Series 6000 and 8000 – that are reserved for UMIR and the

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<sup>1</sup> We expect to receive final approval of the Consolidated Enforcement Rules from the Canadian Securities Administrators (**CSA**) and to implement these rules by the 4<sup>th</sup> quarter of 2016.

<sup>2</sup> Dealer Member Rule 19, *Examinations and Investigations* and Dealer Member Rule 20, *Corporation Hearing Processes*.

Consolidated Enforcement Rules, respectively, as mentioned above, and do not form part of the proposed PLR Rule Book that is being republished for comment at this time.

<b>Series</b>	<b>Title and Description</b>
1000	<b>Interpretation and Principles</b> – a consolidated set of definitions applicable to both Dealer Member and market matters (when UMIR is incorporated)
2000	<b>Dealer Member Organization and Registration</b> – rules concerning Dealer Member ownership and structure, and approval and proficiency of individuals acting on behalf of the Dealer Member
3000	<b>Business Conduct and Client Accounts</b> – rules concerning business conduct (e.g. books and records), conflicts of interest, client accounts (e.g. account supervision), and dealing with clients (e.g. suitability obligations and complaints)
4000	<b>Financial and Operational Rules</b> – rules concerning Dealer Member financial and operational matters
5000	<b>Margin Requirements</b>
6000	<b>Reserved for UMIR</b>
7000	<b>Debt Markets and Inter-Dealer Bond Brokers</b>
8000	<b>Reserved for Consolidated Enforcement Rules</b>
9000	<b>Procedural Matters</b> – rules concerning alternative dispute resolution, and CIPF requirements

### **1.3 PLR Project – publication process**

The PLR Project was initially drafted and published for comment in a number of discrete tranches. IIROC's current Dealer Member Rules were grouped into seven different series (as described in section 1.2 above) and each series, or parts of a series (where the series was particularly large), was approved separately by the Board for publication, and was published as a separate tranche for a 90-day comment period (referred to as the previously published tranches in this Notice). The tranches were published between 2010 and 2012. In only a few instances was a tranche required to be republished for comment as a result of material revisions. **Appendix 1** sets out the content and publication details of each published tranche.

We have now compiled the separately published tranches to create the proposed PLR Rule Book which we are publishing for a 120-day comment period.

### **1.4 Guidance**

In some instances, draft guidance was published with a previously published tranche. We are not republishing any guidance at this time but are continuing to review our existing guidance in the context of the proposed PLR Rule Book to assess whether the guidance:

- (i) remains relevant and does not need to be amended;
- (ii) remains relevant but needs to be amended; or
- (iii) is no longer relevant and needs to be repealed.

There may also be instances where new guidance is required. The issuance of guidance will be coordinated with the implementation of the final PLR Rule Book.

### ***1.5 Dealer Member Rules that are the subject of separate rule amendment proposals***

There are some Dealer Member Rules that are the subject of proposed amendments that are independent of the PLR Project, and that are, or were, out for comment but have not yet been finalized (e.g. the proposed amendments relating to disclosure of membership in IIROC, and those relating to the personal financial dealing rules). We have not, in most cases, included these separate proposed amendments in the proposed PLR Rule Book. We intend to finalize these proposed amendments in the context of each of the separate proposals and will add them to the final version of the PLR Rule Book as they are completed.

### ***1.6 Tools to assist in reviewing material***

For ease of reviewing the proposed PLR Rule Book and related material, we have provided a number of helpful tools.

- (i) We have provided a chart in Appendix 1 which sets out the publication details of each previously published tranche. The plain language rules were originally published in a number of different tranches.
- (ii) We have provided a blackline of the proposed PLR Rule Book showing the revisions to the previously published tranches in **Appendix 2**. A clean version of the proposed PLR Rule Book is attached as **Appendix 3**.
- (iii) And finally, in the Table of Concordance (this document tracks the provisions of the proposed PLR Rule Book to the existing Dealer Member Rules), attached as **Appendix 4**, we have identified the substantive changes by highlighting those in yellow, and for all non-substantive changes we have indicated in the last column the nature of the change. Additional detail on the identification of substantive and non-substantive changes is set out in Section 2 below. We will also be providing the Table of Concordance in a downloadable excel format on the IIROC website which will allow readers to sort the document according to their needs.

## 2. Substantive and non-substantive amendments

### 2.1 Identification of substantive and non-substantive changes

As mentioned above, a small number of substantive changes to the existing Dealer Member Rules were made during the drafting of each previously published tranche. For purposes of classifying rule changes as being either substantive or non-substantive, the following types of changes were considered to be substantive:

- (i) the introduction of new mandatory rule requirements;
- (ii) the making of material changes to a current mandatory requirement that is not redundant; and
- (iii) the deletion of a current mandatory requirement that is not redundant, including instances where a current requirement will be addressed in future guidance.

The following types of changes were considered to be non-substantive:

- (i) the inclusion of non-mandatory rule provisions, including the inclusion of introductory provisions to rules; and
- (ii) the deletion of a non-mandatory or redundant current requirement, including instances where a current requirement will be addressed in future guidance.

The substantive changes that were made in the previously published tranches are discussed in detail in the public comment rules notice published for each tranche. These changes were made to:

- (i) eliminate unnecessary rule provisions;
- (ii) clarify IIROC's expectations with respect to certain rules;
- (iii) ensure that the rules reflected actual IIROC practices; and
- (iv) ensure consistency with other IIROC Dealer Member Rules and applicable securities legislation.

We have not repeated the discussion of the substantive changes that were made in the previously published tranches in this Notice, unless the context requires, but should you wish to reference them, we have included the IIROC Rules Notice reference numbers in Appendix 1. Also, all such changes are identified in the Table of Concordance (Appendix 4).

In response to comments received on each previously published tranche during the previous public comment period, and during subsequent internal reviews as we compiled the proposed PLR Rule Book, new substantive rule changes were made. Our responses to the public comments received on the previously published tranches are set out in **Appendix 5**.

In this Notice, we have limited our discussion to the key substantive changes. The blacklined version of the proposed PLR Rule Book in Appendix 2 identifies other changes made to the previously published tranches that we have not discussed in this Notice. Further, we have divided the

discussion of the key substantive changes into two parts: (i) those which relate to the plain language rewrite exercise, and (ii) those which relate to registration reform related amendments.

In addition to the substantive changes, we also made a number of non-substantive changes that are intended to:

- (i) re-introduce certain provisions which are contained in existing Dealer Member Rules, but were inadvertently omitted when the original tranches were published; and
- (ii) ensure the plain language drafting of a rule conforms to the corresponding existing Dealer Member Rule where no substantive changes were intended to be made to the rule.

We have not discussed the non-substantive changes in detail in this Notice but, as mentioned above, all such changes are identified in the Table of Concordance (Appendix 4).

## **2.2 Key substantive amendments relating to the plain language rewrite exercise**

### **2.2.1 PLR 2000 – Dealer Member Organization and Registration**

- (1) **PLR section 2102 – Definition of an industry investor:** The proposed definition of “industry investor” as published in the previously published tranche referred to as the “clean up tranche”<sup>3</sup> has been amended to include the requirement for IIROC approval. This was done to reflect existing IIROC practices.
- (2) **PLR section 2102 – Definition of “public ownership of securities”:** The term “public ownership of securities” is used in existing Dealer Member Rule section 5.11. We have identified Dealer Member Rule section 5.11 as an unnecessary rule provision<sup>4</sup>, and therefore proposed it be repealed. Accordingly, the defined term “public ownership of securities” has been removed from PLR section 2102.
- (3) **PLR section 2207 – Effective date of resignation:** Amendments to this section capture existing IIROC practices in which a Dealer Member requires IIROC Board approval before allowing a resignation to be final.
- (4) **PLR section 2485– Arrangements between a Dealer Member and a foreign affiliate dealer:** In the previously published PLR 2000<sup>5</sup>, IIROC introduced a new requirement which permitted Dealer Members to carry the client accounts of a foreign affiliate dealer if, among other things, the foreign affiliate dealer qualifies as a “regulated entity”. The requirement that the foreign affiliate dealer qualify as a regulated entity would have a significant negative impact on dealers’ existing and potential business arrangements in certain foreign jurisdictions. In particular, requiring foreign affiliates to qualify as regulated entities will effectively disqualify a

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<sup>3</sup> See IIROC Notice 12-0111.

<sup>4</sup> See IIROC Rules Notice 11-0061.

<sup>5</sup> See IIROC Rules Notice 11-0061.

significant number of existing arrangements that Dealer Members have executed with foreign affiliates and prevent the development of new business opportunities in numerous regions of the world. Furthermore, we believe that the existing IIROC Dealer Member Rules provide adequate oversight in circumstances where Dealer Members carry the client accounts of a foreign affiliate dealer. Therefore, we have revised PLR section 2485 to remove the requirement that the foreign affiliate qualify as a regulated entity. It should be noted, however, that Dealer Members should ensure that carrying the client accounts of a foreign affiliate dealer is not inconsistent with the rules of foreign affiliate dealer's home jurisdiction.

- (5) ***PLR section 2555– Business activities outside of the Dealer Member:*** Existing Dealer Member Rule 18.14 requires Registered Representatives (**RR**) and Investment Representatives (**IR**) to disclosure of outside business activities to their sponsoring Dealer Member and obtain pre-approval from the Dealer Member. However, all Approved Persons are subject to such disclosure requirements through the application of NI 33-109 *Registration Information* as well as the Companion Policy to NI 31-103 which discusses firm approval of outside business activities within the context of conflict of interest management rules. For the purpose of harmonization with industry practices and CSA expectations, the proposed amendments will codify the requirement for disclosure and approval of outside business activities for all Approved Persons.

#### **2.2.2 PLR 3000 – Business conduct and client accounts**

- (1) ***PLR subsection 3103(3) – Know-your-client:*** PLR subsection 3103(3) introduces a new provision that the responsibility for the relevant know-your-client requirements must not be delegated which reflects IIROC's long standing regulatory position on this matter.
- (2) ***PLR section 3150 (in previously published tranche) – Conduct and Practices Handbook:*** The requirement for all Approved Persons of a Dealer Member to have in their possession, and to have read and understood, the Conduct and Practices Handbook (**CPH**) and its updates has been repealed. Prior to the accessibility of the existing Dealer Member Rules through a website, the CPH was considered a valuable reference source for Dealer Members and their Approved Persons for our Rules. This policy rationale is no longer relevant in light of the availability of the existing Dealer Member Rules on the IIROC website and other services, such as IIROC's email alert service which provides real time notice of regulatory developments.
- (3) ***PLR subsection 3220(4) – Record keeping:*** A new requirement has been added requiring Dealer Members to keep a record of any individuals with trading authority over one or more client accounts. These amendments are intended to assist Dealer

Members in identifying anyone who may be carrying out registerable activities without being appropriately registered.

- (4) **PLR subsection 3240(4) – Order execution only account services:** The previously published PLR subsection 3240(4) reflected existing Dealer Member Rule 3200B which sets out the minimum requirements for Dealer Members offering both an advisory and an order execution only service. We deleted the corresponding provisions as the existing Rule is operationally difficult to interpret and apply, and consequently isn't used. A Dealer Member who offers both advisory accounts and order execution accounts can do so through separate divisions.
- (5) **PLR clause 3272(I)(iii) – Accepting a discretionary account; PLR clause 3273(I)(iv) - Discretionary account agreement:** These are new provisions restricting the renewal of discretionary authority. They complement the previously published provision restricting discretionary accounts to a twelve-month time period.
- (6) **PLR section 3284 – Conflicts of interest:** Currently, transactions between a client's managed account and a responsible person or an associate of a responsible person are permitted if client consent at the time of account opening is obtained. The amendments will enhance the client consent requirements by requiring client consent be obtained on a transaction-by-transaction basis.
- (7) **PLR section 3402 – Retail client suitability requirements:** The amendments are new provisions requiring a Dealer Member, when receiving an order from a client that is not suitable, to advise against proceeding with the order. This requirement conforms to section 13.3(2) of NI 31-103.
- (8) **PLR section 3406 – Delegation:** The amendment is a new provision that prohibits the suitability assessment obligation from being delegated. This reflects IIROC's long standing regulatory position on this matter.

### **2.2.3 PLR 5000 – Margin Rules**

- (1) **PLR section 5310 – Determining the basic margin requirement:** As previously stated in IIROC Rules Notice 12-0042, the main objective of PLR 5300 is to present the current margin requirements for equity and index securities "in a more organized fashion". In order to achieve this objective, one of the decisions taken was to revise the current requirements that apply to short positions in customer accounts so that they are consistently expressed as a margin requirement – currently they are expressed as a margin requirement in some instances and as a credit requirement in other instances within existing Dealer Member Rule 100.

In the case of PLR section 5310, the "credit required" calculation was changed to a "margin required" calculation through use of the following formula:

Credit required for short position = market value of short position +  
margin required on short position

This formula can also be re-expressed as follows:

Margin required for short position = credit required on short position -  
market value of short position

Below are the current credit requirements (set out in existing Dealer Member Rule subsection 100.2(f)) for short positions in listed equity securities, along with the equivalent current rule requirement expressed as a margin requirement:

	<b>Credit required for short positions under current Dealer Member Rule 100.2(f)</b>	<b>Equivalent current rule margin required for short positions</b>
All other positions with a market value of \$2.00 or more per share	150% of market value	50% of market value
Market value of \$1.50 per share to \$1.99 per share	\$3.00 per share	\$3.00 per share minus 100% of market value
Market value of \$0.25 per share to \$1.49 per share	200% of market value	100% of market value
Market value of below \$0.25 per share	market value plus \$0.25 per share	\$0.25 per share

Below is a comparison between the current margin requirements for long positions in listed equity securities (set out in existing Dealer Member Rule subsection 100.2(f)), along with the equivalent current rule margin requirements for short positions in listed equity securities:

	<b>Margin required for long positions under current Dealer Member Rule subsection 100.2(f)</b>	<b>Equivalent current rule margin required for short positions</b>
All other positions with a market value of \$2.00 or more per share	50% of market value	50% of market value
Market value of \$1.75 per share to \$1.99 per share	60% of market value	\$3.00 per share minus 100% of market value
Market value of \$1.50 per share to \$1.74 per share	80% of market value	\$3.00 per share minus 100% of market value
Market value of \$0.25 per share to \$1.49 per share	100% of market value	100% of market value

Market value of below \$0.25 per share	100% of market value	\$0.25 per share
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The above table illustrates that the effective long and short margin rates for listed equity securities are currently:

- the same for securities trading at \$2.00 and more per share;
- somewhat different for securities trading at \$1.50 per share to \$1.99 per share; and
- the same for securities trading at \$0.25 per share to \$1.49 per share.

The continuance of these margin rate differences can't be justified<sup>6</sup>, given that securities trading either higher or lower in price are to be margined at the same margin rate, irrespective of whether they are held long or short. We therefore have proposed to amend the short position margin rates for listed equity securities trading at \$1.50 per share to \$1.99 per share to conform to the current long position margin rates for long positions in the same market value per share range.

Below is a table illustrating how this proposed amendment has been reflected in PLR subsection 5310(1):

	Margin required for long positions	Margin required for short positions
All other positions with a market value of \$2.00 or more per share	50% of market value	50% of market value
Market value of \$1.75 per share to \$1.99 per share	60% of market value	<del>\$3.00 per share minus</del> 40% of market value
Market value of \$1.50 per share to \$1.74 per share	80% of market value	<del>\$3.00 per share minus</del> 40% of market value
Market value of \$0.25 per share to \$1.49 per share	100% of market value	100% of market value
Market value of below \$0.25 per share	100% of market value	\$0.25 per share

(2) **PLR section 5825 – Account guarantee agreement minimum terms:** It has been brought to our attention that article 2355 of the Civil Code of Quebec (“Civil Code”) prohibits a surety from:

- (a) waiving his or her right to information about a guaranteed debt (this is at odds with the minimum account guarantee agreement term set forth in PLR sub-clause 5825(1)(v)(a) as originally proposed, and

<sup>6</sup> The continuance of the margin rate difference at the below \$0.25 per share price level can be justified given the significantly higher percentage volatility of short positions trading at lower price levels.

- (b) waiving in advance his or her right of subrogation (this is at odds with the minimum account guarantee agreement term set forth in PLR sub-clause 5825(1)(v)(c) as originally proposed).

These prohibitions are at odds with the account guarantee agreement minimum term requirements set out in PLR sub-clauses 5825(1)(v)(a) and 5825(1)(v)(c) as originally proposed. Consequently, we have proposed to remove PLR sub-clause 5825(1)(v)(a) and revise PLR sub-clause 5825(1)(v)(c) (now renumbered as PLR sub-clause 5825(1)(v)(b)) to clarify that this provision, and its predecessor provision in existing Dealer Member Rule 100.15(h)(v)), has always been intended to prohibit the advance waiver of the right of subrogation, consistent with article 2355 of the Civil Code.

## **2.3 Registration reform related amendments**

### **2.3.1 Background**

In 2009, IIROC made amendments to its existing Dealer Member Rules in order to harmonize with NI 31-103. Since then, NI 31-103 has been amended by the CSA several times. Consequently, we have been working on further amendments to the Dealer Member Rules to correspond with the amendments made to NI 31-103. In addition, we are proposing amendments to address gaps and implementation issues identified in the existing Dealer Member Rules following the implementation of the 2009 amendments. Some of the gaps and implementation issues were identified by IIROC, while others are in response to issues identified by IIROC committees (particularly the Education and Proficiency Committee) that recommended specific amendments to IIROC's Continuing Education requirements. These proposed amendments are collectively referred to as the **registration reform related amendments**<sup>7</sup> in this Notice.

The registration reform related amendments had originally been undertaken as a separate project from the PLR Project on the expectation that the proposed PLR Rule Book would be finalized before the registration reform related amendments were finalized. As this is not the case, we considered whether to continue with the registration reform related amendments as a separate project and publish them for comment separately, or include them in the proposed PLR Rule Book and publish them together. In light of the passage of time since the NI 31-103 amendments, and the requirement for IIROC to have rules that are not inconsistent with CSA rules, we decided to combine the two projects and include the registration related reform amendments in the proposed PLR Rule Book. This approach will avoid the disruption to Dealer Members that would be caused by publishing for comment the proposed PLR Rule Book without the registration reform related amendments, and

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<sup>7</sup> The registration reform related amendments were not included in any previously published tranche.

then subsequently publishing for comment the registration reform related amendments either before the proposed PLR Rule Book was even finalized, or just as it was implemented.

### **2.3.2 Summary of the registration reform related amendments**

At a high level, the registration reform related amendments were made in the following areas:

- (1) **Interest in a Dealer Member**
  - (a) amendments relating to ownership of a Dealer Member's securities for harmonization with NI 31-103;
  - (b) new rules relating to purchasing assets of a Dealer Member, for harmonization with NI 31-103; and
  - (c) amendments to clarify the meaning of investor within the IIROC Dealer Member rules in response to drafting issues identified internally.
  
- (2) **Portfolio Managers and Associate Portfolio Managers**
  - (a) introduction of separate categories of Portfolio Manager (**PM**) and Associate Portfolio Manager (**APM**) to more closely mirror the NI 31-103 "Advising Representative" (**AR**) and "Associate Advising Representative" (**AAR**) categories.
  
- (3) **Requirements relating to designated Chief Compliance Officer, Chief Financial Officer, Ultimate Designated Person, Executives and Supervisors**
  - (a) amendments relating to the designation of the Chief Compliance Officer (**CCO**) and Ultimate Designated Person (**UDP**) for the purpose of harmonization with NI 31-103;
  - (b) new rules to codify detailed responsibilities of the Chief Financial Officer (**CFO**) in response to gaps identified internally and by Dealer Members; and
  - (c) new rules requiring the designation of specified positions (e.g. Executives), within the finance and operation related rules as being responsible for specified areas of significant risk.
  
- (4) **Proficiency related matters**
  - (a) various amendments have been made to the proficiency related requirements. Some of these are for the purpose of harmonization with NI 31-103 or to clarify current expectation and practices, while others are to address issues or gaps identified in our current structure. The registration reform updates include various amendments to the Continuing Education (**CE**) requirements and the course re-write requirements;
  - (b) amendments have been made to prescribe minimum experience; and requirements for CCOs for the purpose of harmonization with NI 31-103; and

- (c) amendments have been made to codify the current requirements under NI 31-103 with regards to a registrant's obligation to understand the features and risks associated with each security they recommend. We have also proposed amendments that will codify the expectations set out in the Companion Policy of NI 31-103 (**CP 31-103**) that firms have an obligation to conduct their own analysis of all securities they recommend to clients and provide product training to ensure their registrants have a sufficient understanding of the securities and their risks.
- (5) **Responsibility for areas of significant risk**
- (a) a key regulatory framework of IIROC is that, every area of significant risk within a Dealer Member should be addressed in the Rules in a manner that allocates responsibility for managing that risk to an Approved Person (i.e. someone who will be accountable) within the Dealer Member. Amendments have been made in the following areas to address the gaps that have been identified in our requirements where the key regulatory framework has not been addressed as follows:
    - (i) existing Dealer Member Rule 38 (Compliance and Supervision) – an Approved Person has not been specified as being responsible for the operations at a Dealer Member, and operations is a significant area of risk;
    - (ii) existing Dealer Member Rule 38 (Compliance and Supervision) – there are inconsistencies regarding the responsibilities of a CFO; and
    - (iii) PLR Rules 4100 through 4900 – an Approved Person has not been specified for many of the significant areas of risk at a Dealer Member. Those rules currently assign the responsibilities to the Dealer Member. In addition, to the extent that some of those rules do name an Approved Person (e.g. CFO) or the Approved Person's designate as being responsible for a particular function, the designate is not specified to be an Approved Person (e.g. Supervisor).
- (6) **Other**
- (a) consequential amendments to reflect the operational changes on the National Registration Database resulting from a new service agreement with CGI Information Systems and Management Consultants.

### 2.3.3 Discussion of the registration reform related amendments

(1) **Managing Significant Areas of Risk**

- (a) ***PLR 1500 - Managing Significant Areas of Risk:*** This rule contains a key regulatory framework for the proposed registration reform related amendments as discussed above. Specifically, it sets out (i) IIROC's expectation that, for every significant area of risk within a Dealer Member, an appropriate Executive(s) be responsible for managing these areas of risk, (ii) a list of specific significant areas of risk, and (iii) the requirements that relate to meeting IIROC's expectation. This is discussed below in the context of the substantive amendments to PLR sections 3905, 3909 and PLR Rules 4100 to 4900.

(2) **Approval process for acquiring an interest in a Dealer Member**

- (a) ***PLR section 2108 - Ownership of a significant equity interest and ownership of assets:*** For the purpose of harmonization with NI 31-103 and consistency with the proposed substantive amendment relating to Dealer Member asset purchases (as discussed below), the proposed amendments will impose a new process with regards to the existing requirement to obtain approval from the applicable District Council in order to own or acquire a significant equity in a Dealer Member. The new process requirement involves filing a written request for approval with IIROC, which must include a completed investor application form(s), at least 30 days prior to the proposed ownership change. Consistent with NI 31-103 sections 11.9 and 11.10, the proposed amendments also require Dealer Members to include all relevant facts regarding the ownership change sufficient to enable the District Council to determine if the ownership change is:
- (i) likely to give rise to a conflict of interest;
  - (ii) likely to hinder the Dealer Member in complying with IIROC requirements and securities legislation;
  - (iii) inconsistent with an adequate level of investor protection; or
  - (iv) otherwise prejudicial to the public interest.

In addition, the existing Dealer Member Rules do not include requirements relating to asset purchases of a registered firm or another Dealer Member by a Dealer Member. In order to harmonize with NI 31-103, PLR section 2108 introduces a new notice and approval process requiring a Dealer Member to give 30-days advanced notice to, and get the consent of, IIROC in order to acquire assets of another Dealer Member or registrant.

It should be noted that while the above-noted amendments to the IIROC Rules are intended to harmonize with NI 31-103, the “significant equity interest” definition proposed by IIROC is broader than the corresponding “direct or indirect ownership” term used in sections 11.9 and 11.10 of NI 31-103.

(3) **Dealer Member Executives**

- (a) **PLR sections 2505 and 2506 – CFO and CCO:** We have amended the language in PLR sections 2505 and 2506 to clarify that, in the event a CFO or CCO ceases to be employed by a Dealer Member (rather than simply vacating the position) the Dealer Member must immediately designate another qualified person or an Executive to act as the CFO or CCO, as the case may be, who has 90 days to satisfy the requisite proficiencies for the position (**Acting CFO/CCO**). This will assist the Dealer Member in determining the commencement of the 90-day period and helps to clarify the expectation for Dealer Members to have a succession plan in place in the event the Acting CFO/CCO does not upgrade their proficiencies within the 90-day period.
- (b) **PLR section 2506 – CCO:** PLR subsection 2506(1) has been revised by adding an experience requirement, which reflects the changes to existing Dealer Member Rule 2900, Part I proficiency and experience requirements. PLR subsection 2506(3) has been amended to replace the word ‘leaves’ with the word ‘ceases’ to accurately reflect that the CCO must no longer be employed with the firm in order for the firm to qualify for the 90-day timeline to find a replacement CCO.
- (c) **PLR section 2507 – UDP:** PLR subsection 2507(1) has been amended to replace the words ‘a director or executive’ with the words ‘an Executive’ as only an Executive can carry out this position within the firm. As well, for the purpose of harmonization with NI 31-103, the proposed amendments require Dealer Members to appoint a new UDP if the existing one ceases to meet the required criteria for being a UDP.

(4) **Know Your Product**

- (a) **PLR sections 2554 and 2602 – Approval of RRs and IRs, PMs and APMs and their obligations and Proficiency requirements for Approved Persons:** Section 3.4 of NI 31-103 prohibits registered individuals from performing an activity unless they have the education, training and experience that a reasonable person would consider necessary to perform the activity competently, including understanding the structure, features and risks of each security they recommend to a client. These obligations are

commonly referred to as the “know-your-product” obligation. PLR sections 2554 and 2602 contain amendments that codify the above noted proficiency requirement in NI 31-103 within the proposed PLR Rule Book.

Since NI 31-103 imposes a similar requirement on CCOs of firms, we have also proposed amendments specifically stating that CCOs must not perform an activity that requires IIROC approval unless they have the education, training and experience that a reasonable person would consider necessary to perform the activity competently. In addition to CCOs, we proposed an expansion of the requirements to include Supervisors on the same policy basis.

(5) **New Portfolio Manager and Associate Portfolio Manager Categories:**

- (a) ***PLR subsection 2552(2) – Individual Approval:*** The existing Dealer Member Rules do not recognize a PM or an APM as distinct approval categories but allow for a RR to have a business type of portfolio management, provided the requisite proficiency and experience requirements are satisfied. The APM and PM categories were eliminated with the implementation of registration reform amendments in 2009.

IIROC proposes to re-introduce, in PLR subsection 2552(2), PMs and APMs as formal categories of approval for individuals providing discretionary management for managed accounts in order to more closely align these categories with the CSA’s AR and AAR categories as well as to provide a seamless transition from the CSA platform to IIROC. With these changes, PMs and APMs seeking registration for non-managed accounts will be required to meet the proficiencies of a RR. The proposed amendments include introducing new PM and APM definitions, new requirements relating to the supervision of APMs, as well new proficiency and experience requirement for each category that are aligned with the CSA’s AR and AAR categories. Furthermore, amendments have been made throughout the proposed PLR Rule Book to reference the new PM and APM categories where applicable.

(6) **UDP/CCO Exemptions**

- (a) ***PLR sections 2506 and 2507 - Appointing More Than One CCO/UDP:*** Sections 11.2 and 11.3 of NI 31-103 require a registered firm, including an investment dealer, to designate “an individual” who is registered under securities legislation in the category of CCO and UDP, respectively, to perform certain enumerated responsibilities. While the same individual may serve as CCO and UDP for an investment dealer pursuant to PLR sections 2506 and 2507, respectively, formal relief by applicable securities regulators

is required if a registered firm wished to appoint more than one person to serve as CCO or more than one individual to serve as UDP (this typically arises in situations where there are separate operating divisions of the registered firm as noted in Companion Policy 31-103 section 5.2). IIROC retains the discretion to approve more than one CCO to be responsible for separate business units of the Dealer Member pursuant to PLR subsection 2506(2). We have amended PLR subsection 2507(2) to similarly provide IIROC with specific discretion to approve more than one UDP to be responsible for separate business units of the Dealer Member.

(7) **Proficiency Requirements**

In addition to harmonizing, where appropriate, IIROC requirements with NI 31-103, the following amendments are directed at updating and improving the clarity of IIROC proficiency rules. There are also some transitional provisions that have been removed as they are no longer required given the passage of time since the rules were written.

(a) ***PLR section 2601– Introduction***

New language has been introduced in PLR section 2601 to align expectations on proficiency with the requirements of section 3.4 of NI 31-103. As Dealer Members are subject to the proficiency principle contained under section 3.4 of NI 31-103, IIROC has included an equivalent proficiency requirement within PLR subsections 2602(1) and 2602(2) to emphasize that Dealer Members have an obligation to take reasonable steps to ensure that an individual does not perform an activity that requires approval unless the individual has the education, training and experience that a reasonable person would consider necessary to perform their job functions competently, including understanding the structure, features and risks of each security the individual recommends.

CCOs and Supervisors must also not perform an activity that requires IIROC approval unless they have the education, training and experience that a reasonable person would consider necessary to perform the activity competently.

As individual applicants must meet the proficiency principle, it is recognized that courses may be updated, modified or changed to continually keep pace with the securities industry. PLR subsection 2601(2) was added to identify where a successor course, the scope and content of which is not significantly reduced, shall supersede the course specified in this Rule.

(b) ***PLR section 2602 – Proficiency requirements for Approved Persons***

We have proposed a number of amendments to the course requirements to address gaps identified in our requirements following introduction of registration reform amendments in 2009. We have discussed the more significant amendments below. All amendments are set out in the chart contained in PLR section 2602.

(i) ***Supervisors – Retail***

*Supervisors of RRs/IRs dealing with retail clients:* In order to reflect current practices, the proposed amendments will provide retail supervisors with alternatives in meeting the two-year relevant experience requirements with an IROC Dealer Member. The amendments will include acceptance of two years' of supervisory/compliance experience with a Mutual Fund Dealer, Portfolio Manager, or another entity governed by a recognized foreign self-regulatory organization as alternatives for meeting the two years' experience requirements. We currently allow such alternative experiences on a case by case basis given that with the implementation of NI 31-103, applicants are subject to the harmonized supervisory principles applicable to all registered firms. This change will streamline the review of Supervisor applications. Also, where the applicant does not meet the requirements as amended, a submission to the applicable District Council will be required.

(ii) ***Supervisors – Institutional***

To address gaps in the existing Dealer Member Rules, the proposed amendments include amendments to the proficiency and experience requirements for RRs and IRs dealing with institutional clients and those supervising such RRs and IRs. The amendments are intended to add similar proficiency and experience requirements on the institutional side as currently exists on the retail side. As such, the Supervisors of RRs/IRs dealing with institutional clients will be subject to a two year relevant experience requirement and will be required to complete the Effective Management Seminar within 18 months from the date of approval as Supervisor of RRs or IRs dealing with institutional clients.

(iii) ***Designated Supervisors***

In order to address gaps in the existing Dealer Member Rules following the introduction of registration reform amendments in 2009, which did not allocate specific proficiency requirements for certain designated Supervisors, we propose specific proficiency

requirements for Supervisors designated to be responsible for the following: (a) new accounts and supervision of account activity; (b) discretionary accounts; (c) managed accounts; (d) retail options accounts; (e) institutional options accounts; (f) futures contracts accounts; (g) pre-approval of advertising materials, sales literature and correspondence; and (h) research reports.

(iv) **Chief Compliance Officer**

While IIROC recognizes that each Dealer Member's business model and types of securities related activities may differ, we have amended the relevant rules to include the following experience requirements for the CCO of a Dealer Member: (a) five years working for an investment dealer, with at least three years in a compliance or supervisory capacity within the past three years before registration approval; or (b) at least three years of providing professional services in the securities industry, with at least 12 months experience working at a registered investment dealer in a compliance or supervisory capacity within the past three years before registration approval. These new experience requirements are intended to harmonize the IIROC requirements with the requirements set out in NI 31-103 for CCOs, RRs and IRs. The requirements also codify IIROC's existing practice and expectations for CCOs (as enforced, since the inception of this approval category).

(v) **RRs and IRs dealing in options**

An amendment has been made to clarify that an Approved Person trading in options must have the baseline proficiency requirements of an RR or IR, respectively.

(vi) **Portfolio Managers and Associate Portfolio Managers**

The proposed proficiency and experience requirements for APMs and PMs are intended to harmonize IIROC requirements with the CSA proficiency requirements for ARs and AARs, where practical, as embodied in NI 31-103 and Companion Policy 31-103.

(c) **New Transition Periods**

Two new transition provisions have been added. The provision under PLR subsection 2603(3) is intended to clarify that individuals approved as of the date of the effective change to the PLR Rule, will not be subject to the new proficiency or experience requirements, where applicable, provided they continue in the same role.

PLR subsection 2603(4) is intended to provide guidance to those Dealer Members who conduct portfolio management activities. Action is required to align each RR currently with the “business type” of portfolio management to the “approval category” of APM or PM, as applicable, by filing a Form 33-109F2 with IIROC. This applies to both managed and non-managed account activities. Dealer Members will have a 3-month time period in which to review and align their records for such Approved Persons.

(d) ***Extension of Recognition of CFA Level 1***

The CSA recognizes the CFA Charter and Level 1 of the CFA Program as an acceptable proficiency for certain licensing categories. IIROC recognizes the CFA Program as an acceptable proficiency for PMs. IIROC recently conducted an in-depth review and consultation with respect to the IIROC proficiency assurance model. We are proposing recognition of the CFA Level 1 as an alternative to the Canadian Securities Course (**CSC**) component of the proficiency requirements for IIROC representatives. This proposed amendment expands the options available to prospective registrants within the single course provider model and recognizes the varying educational interests and professional backgrounds and career goals of licensing applicants seeking representative level approval. We compared content of the CFA Program to the CSC, CPH and 90 Day Training program. We concluded that Level 1 of the CFA Program, together with the Canadian content in the CPH and the 90 Day Training Program, achieves substantial coverage of the CSC content. CFA Level 1 also includes a great deal of training that goes well beyond the CSC curriculum.

(e) ***Exemptions and Continuing Education***

(i) ***PLR section 2606 - Exemptions from rewriting courses***

The proposed amendments to the proficiency exemptions align with the timelines in NI 31-103. The amendments mirror the requirement for an individual to have 12 months of experience in the previous 36 months in order to keep a course valid for registration purposes. Further, all courses are now valid for three years. The validity period does not apply to the Canadian Investment Manager Designation, the Chartered Investment Manager Designation and the CFA Charter provided the holders of the designations continue to have the right to use the designation and the designation has not been revoked or otherwise restricted

The Partners, Directors and Officers Course (**PDO**) was included in the proficiency exemption section to address a change in 2009 with

the introduction of registration reform that officers were no longer required to be approved at Dealer Members. Only the Executives (mind and management) of a Dealer Member are required to be approved. The addition of the PDO exemption provision considers the course validity in relation to the surrender of approval of an officer (i.e. the time at which the officer was no longer required to be approved). The course validity can be maintained by considering the experience of the individual upon IIROC's review and approval.

(ii) ***PLR section 2650 – Continuing Education Requirements for Approved Persons***

Following the registration reform amendments in 2009, the Education and Proficiency Committee reviewed and proposed changes to the Continuing Education (CE) related rules within the existing Dealer Member rules. The purpose of the review was to compare the IIROC CE requirements to other professional organizations (such as Chartered Life Underwriter) with the goal of aligning our timelines and requirements with other professional organizations' standards.

The amendments include changes to: (a) the length of the cycle from three to two years; (b) reducing the amount of credits required for Compliance and Professional Development continuing education; (c) removing the three year grace period; and (d) allowing registrants to utilize the Wealth Management Essentials course for CE credits as well as meeting their Post-Licensing Requirement. The penalties for non-compliance have been amended to a single penalty amount of \$2500 and the individual is automatically suspended. The rules have been amended such that any penalty would be assessed at the beginning of the next cycle.

(f) ***National Registration Database***

Amendments to PLR Rule 2700 – The National Registration Database – are intended to harmonize, where appropriate, IIROC requirements with NI 31-103. The amendments include a requirement for Dealer Members to provide a Notice of Termination upon the request of a former Approved Person.

(g) ***Business conduct and client accounts***

- (i) ***PLR section 3103 – Know-your-client:*** This section reflects the requirements in existing Dealer Member Rule 2500, but is amended to ensure that the new registration reform categories of RR, PM and APM are assigned primary responsibility for the relevant know-your-client requirements.

- (ii) **PLR section 3220 – Record keeping; 3229 – Updating client accounts:** Dealer Members are required to keep a record of any persons with a trading authority over a client’s account and maintain updated client account information. Amendments to reflect the PM or APM responsibility for such accounts have been incorporated as part of the registration reform amendments.
- (iii) **PLR section 3252 – Opening an options account; 3257 – Additional requirements when opening a futures contract or futures contract option account:** Amendments to reflect the PM or APM responsibilities have been incorporated as part of the registration reform amendments.
- (iv) **PLR section 3274 – Persons authorized to effect discretionary trades; 3275 – Conflict of interest:** Amendments to reflect the RR responsibilities have been incorporated as part of the registration reform amendments.
- (v) **PLR section 3283 – Persons authorized to deal with managed accounts:** Amendments to reflect the APM responsibilities which have been incorporated as part of the registration reform amendments.
- (vi) **PLR section 3402 – Retail client suitability requirements; 3403 – Institutional client suitability requirements; 3404 – Exemptions from and exceptions to suitability requirements:** New provisions which conform to section 13.3(2) of NI 31-103 are included, as well as a separation of suitability requirements according to whether the client is retail or institutional, followed by the exemptions and exceptions.
- (vii) **PLR sections 3905 – Supervisory personnel and resources; 3909 – Responsibilities of the executive:** The amendments to the rules create consistency between the Dealer Member’s responsibilities in terms of appointing as many Supervisors as necessary and appointing as many Executives as necessary to ensure compliance with the Corporation requirements. The amendments also codify the existing expectation of the role of Executives within an IIROC Dealer Member, as noted in IIROC Notice 12-0379 *The Role of Compliance and Supervision*.
- (viii) **PLR section 3910 – Responsibilities of the UDP:** The amendments codify and clarify the responsibilities of the UDP.

- (ix) **PLR sections 3913 and 3915 –Responsibilities of the CFO:** The amendments codify and clarify the responsibilities of the CFO in such a manner that is parallel to the responsibilities allocated to the CCO.
  - (x) **PLR sections 3914 and 3915 – Responsibilities of the Chief Operating Officer:** The amendments codify who within the IIROC Dealer Member Rules is responsible for the operational rules of the Dealer Member.
  - (xi) **PLR section 3970 – Supervision of managed accounts:** Amendments to reflect the addition of registration reform supervisory obligations relating to managed accounts have been incorporated.
- (h) **PLR 4000**
- (i) As mentioned above, the proposed registration reform related amendments reflected in PLR Rule 1500 set out a key regulatory framework for managing significant areas of risk. This Rule sets out IIROC’s expectation that, for every significant area of risk within a Dealer Member, an appropriate Executive(s) be responsible for managing the area of risk. There are certain significant areas of risk (e.g. a Dealer Member’s risk adjusted capital and early warning levels) that IIROC believes should be the responsibility of a specific Executive (e.g. CFO and UDP). In addition, IIROC believes that certain roles within a Dealer Member need to be specifically assigned to ensure there is appropriate segregation of duties.

The amendments in PLR Rules 4100 through 4900 (i.e. the sections dealing with financial and operational matters) reflect IIROC’s expectations for managing significant areas of risk as discussed above while still allowing sufficient flexibility to accommodate various business models and not impose undue regulatory burden. For example, where the term “management”, “senior management” or “senior officer” is used in the existing Dealer Member Rules we have replaced that with the term “Chief Financial Officer”, “Ultimate Designated Person”, “Executive” or “appropriate Executive” depending on the matter. And, where the term “personnel”, “individuals”, “designated individuals” or “a single person” is used in the existing Dealer Member Rules we have replaced that with the term “employee(s)” depending on the matter.

### **3. Alternatives considered**

With respect to the proposed PLR Rule Book, we considered

- (i) the comments received from the public and the CSA on the previously published tranches;
- (ii) the need to proceed with the registration reform related amendments to ensure that IIROC rules are consistent with CSA requirements; and
- (iii) the independent policy matters that arose in the period of time between the previously published tranches and today,

and balanced these considerations and the objective of ensuring that the proposed PLR Rule Book was as complete as possible with the need to bring closure to the plain language rewrite project and implement the rules. In light of this, we were not able to deal with issues which were raised that we considered to be out of scope of the PLR Project – i.e. issues that were not related to the plain language rewrite process or the registration reform related process. We intend to address the out-of-scope issues that were raised in a manner consistent with our policy priorities.

### **4. Impact of the proposed PLR Rule Book**

IIROC, Dealer Members, and individuals acting on their behalf, will benefit from the enhanced clarity and certainty that the proposed PLR Rule Book offers. We recognize that the operationalization of the proposed PLR Rule Book by Dealer Members and individuals acting on their behalf, particularly on the institutional side, will require both a significant amount of time and resources on their part, and we will take that into account in the implementation phase.

### **5. Policy development process**

#### **5.1 *Regulatory purpose***

In addition to the discussion, throughout this Notice, of the purpose of the proposed PLR Rule Book, the purpose of the proposed PLR Rule Book is also to:

- (i) establish and maintain rules that are necessary or appropriate to govern and regulate all aspects of IIROC's functions and responsibilities as a self-regulatory entity;
- (ii) ensure compliance with securities laws;
- (iii) prevent fraudulent and manipulative acts and practices;
- (iv) promote just and equitable principles of trade and the duty to act fairly, honestly and in good faith;
- (v) foster cooperation and coordination with entities engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in, securities;
- (vi) foster fair, equitable and ethical business standards and practices; and
- (vii) promote the protection of investors.

Due to the extent and substantive nature of the proposed PLR Rule Book, it is classified as a public comment rule proposal.

## **5.2 Regulatory process**

The Board of Directors of IIROC (**Board**) has determined the proposed PLR Rule Books to be in the public interest and on November 19, 2015 approved it for republication for public comment.

IIROC consulted Dealer Members extensively throughout the rule development process both in respect of the previously published tranches<sup>8</sup>, and in respect of the proposed PLR Rule Book, including consultation with the Executive and various sub-committees of each of the Compliance and Legal Section and the Financial Administrators Section, and the National Advisory Committee.

After considering the comments on the proposed PLR Rule Book received in response to this Notice together with any comments of the Recognizing Regulators, IIROC may recommend that revisions be made to the proposed PLR Rule Book. If the revisions and comments received are not of a material nature, the Board has authorized the President to approve the revisions on behalf of IIROC and the proposed PLR Rule Book as revised will be subject to approval by the Recognizing Regulators. If the revisions or comments are material, the proposed amendments including any revisions will be submitted to the Board for approval for republication or implementation as applicable.

## **6. Attachments**

[Appendix 1](#) – Publication details of the previously published tranches that make up the proposed PLR Rule Book

[Appendix 2](#) – Proposed PLR Rule Book (blacklined to previously published tranches)

[Appendix 3](#) – Proposed PLR Rule Book (clean)

[Appendix 4](#) – Table of Concordance

[Appendix 5](#) – Responses to public comments on previously published tranches

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<sup>8</sup> Details of the consultation that was done in respect of the previously published tranches are set out in each Notice issued in respect of a tranche. See Appendix 1.