CIRO Rule Consolidation Project: Phase 3

July 17, 2024

Submission to the Canadian Investment Regulatory Organization (**CIRO**)

ASSOCIATION DES BANQUIERS CANADIENS
CANADIAN BANKERS ASSOCIATION

The Canadian Bankers Association (**CBA**)[1] appreciates the opportunity to provide input on the consultation with respect to Phase 3 of CIRO's Rule Consolidation Project (**Phase 3**). Below we provide our responses to the specific questions set out in the consultation, followed by our comments on shared premises requirements.

CIRO Consultation Questions

1. **Many of the comments received as part of the first phase of our Rule Consolidation Project indicated that once the initial publication of the five phases is complete, any subsequent republication of the proposed rules should be as an entire rulebook (i.e. not as separate phases). Should we republish the entire set of proposed Dealer and Consolidated Rules prior to their approval?**

We are supportive of the republication of the entire set of proposed Dealer and Consolidated Rules prior to their approval. This is necessary given the amount of time that will have elapsed from publication of the first phase of the project to the final phase.

Stakeholders would benefit from an opportunity to assess and provide final feedback to CIRO on the proposed rules as a whole to help identify any concerns that may have arisen over the course of the project or that may only become apparent when reviewing all the proposed rules together.

2. **Many of the comments received as part of the first phase of our Rule Consolidation Project indicated the Dealer and Consolidated Rules should be implemented all at once (and not in phases). Should we implement the entire set of proposed Dealer and Consolidated Rules at the same time? How long a period should we allow for the implementation of the proposed Dealer and Consolidated Rules?**

As this is Phase 3 of a five-phase project, stakeholders have not had the opportunity to review

[1] The Canadian Bankers Association is the voice of more than 60 domestic and foreign banks that help drive Canada's economic growth and prosperity. The CBA advocates for public policies that contribute to a sound, thriving banking system to ensure Canadians can succeed in their financial goals.

the proposals to come in phases 4 and 5, which may be more impactful to Dealer Members relative to previous phases. Therefore, it is premature to assess whether the new consolidated rules should be implemented all at once or in phases. We would ask that CIRO solicit feedback on this specific question in each of the remaining phases as well as when the proposed rules are published in their entirety after considering comments from stakeholders.

From a Dealer Member perspective, there are pros and cons to the “all at once approach”. The optimal implementation method will depend on the degree of procedural and other changes required by a Dealer Member to be implemented in response to the final consolidated rules. For example, if the overall impact to a Dealer Member is minimal and there are sufficient resources available at the time of implementation, the “all at once” approach may be more practical. Conversely, if certain changes result in heavy lifting required by a Dealer Member and there are resource challenges, an “all at once” approach may not result in the best outcome for the firm, its clients, or the industry.

Regarding the required implementation period, we note that there are several ongoing/ concurrent large CSA/CIRO regulatory initiatives underway (e.g., Total Cost Reporting, CSA Derivatives Business Conduct, CIRO Derivatives Modernization) and it is necessary that CIRO take this into account as well in implementation timelines on this initiative.

The appropriate length of the implementation period would necessarily depend on the nature and magnitude of the specific changes required – the greater the changes, the greater the time required to implement.

A minimum of 24 months should be provided for implementation by Dealer Members to enable sufficient time to take the necessary steps to comply, including updating systems, client disclosures, policies, procedures, training, and other supporting change management processes. Implementation periods of greater than 24 months should be provided as necessary for those changes deemed to have the most operational impact on Dealer Members.

3. **To ensure a level playing field for investment dealers and mutual fund dealers, we have proposed to require cross-guarantees between Dealer Members and their**

related companies. The term "related company" is exclusively used to explain the relationship between Dealer Members (through at least 20% common ownership of both Dealer Members (directly or indirectly)).

The result of adopting this amended IDPC and MFD rule requirement is that commonly owned investment dealers and mutual fund dealers will have to cross-guarantee each other.

Does requiring cross-guarantees between investment dealers and mutual fund dealers cause undue burden? If yes, please explain.

With CIRO's recently proposed Integrated Fee Model adding new fees for regulatory reviews of business initiatives that require CIRO approval, the increased regulatory and financial burden associated with obtaining such ownership approval would exceed its value. In addition, since each registered firm is regulated from a prudential standpoint, we fail to see the justification for requiring one regulated entity to back the financial obligations of the other. The outcomes from this proposed rule "harmonization" do have a material impact on stakeholders although not assessed as such in the consultation materials.

Ownership change rules could be amended to instead require notice to CIRO rather than approval, with certain ownership guideline requirements incorporated in the rule from which an exemption may be applied for. This would align with the Mutual Fund Dealer Rules which do not have an equivalent approval requirement. Adding additional administrative and financial burden on Dealer Members in the absence of any evidence of a need for more than notice above a transactional threshold has not been explained in the consultation materials to substantiate such requirement.

Moreover, if ownership is common between Investment Dealers and Mutual Fund Dealers, the legal utility of such cross-guarantees is unclear, as they are normally implemented to gain third-party or related party security for indebtedness as added protection to a lender. Such structure imposed in the context of prudentially regulated related entities with different registration categories, capital requirements and business models would impose undue burden with the

potential unintended consequence of Dealer Member liability for business the firm is not approved to conduct, blurring registration category distinctions.

It is also unclear why the Dealer Member would be obligated in Rule 2206(3)(i) to guarantee an amount equal to 100% of the Dealer Member's financial statement capital, but not the reverse by the related company in subparagraph (3)(ii) if the Dealer Member has less than 20% ownership. The rationale for the degree of obligation is unclear.

4. **The current membership disclosure requirements applicable to investment dealers and mutual fund dealers have the following key differences:**

    - **the mutual fund dealer policy requires that both the CIRO logo and a link to the CIRO website be included on account statements, whereas the investment dealer policy only requires the CIRO logo (the proposed Membership Disclosure Policy found in Appendix 5 extends the mutual fund dealer requirement to all Dealer Members)**
    - **the investment dealer policy requires that the CIRO decal be displayed at all public-facing business locations, whereas the mutual fund dealer policy does not have a similar requirement (the proposed Membership Disclosure Policy found in Appendix 5 removes this requirement for all Dealer Members)**
    - **the investment dealer policy requires that the CIRO official brochure be provided to clients at account opening or upon request, whereas the mutual fund dealer policy does not have a similar requirement (the proposed Membership Disclosure Policy found in Appendix 5 extends the investment dealer requirement to all Dealer Members)**

    Do you agree with the changes highlighted above and the proposed Membership Disclosure Policy found in Appendix 5? If not, please explain.

    A guiding principle for the Disclosure Policy should be to balance regulatory burden against the anticipated client benefits of any contemplated additional disclosure requirements.

In our members' experience, any changes to existing account statements will incur significant costs and operational resources to implement. The contemplated changes to statements highlighted in the question above do not provide any substantive benefit to clients to warrant the increase in costs and operational burden. Moreover, many clients have elected to receive statements electronically. Presumably, such clients and most other clients generally would be readily able to locate the CIRO website without a link in their account statements.

Since Investment Dealer's statements already contain the CIRO logo, the fact that CIRO is the regulator is already communicated to clients. Adding a link to CIRO's website does not add anything valuable as it is not likely that clients are going to the CIRO website using the link embedded in the statement. We also note that many Dealer Members likely include their own corporate website URL on account statements, with the corporate website including an active link to the CIRO website.

The anticipated costs and resources required to implement the contemplated change to account statements would be in addition to those already recently incurred by Dealer Members to accommodate the CIRO rebranding exercise.

For the reasons set out above, the requirement to include a link to CIRO's website on account statements should be removed for all Dealer Members. CIRO could, however, consider creating a logo version that contains the website link. Similar to the current selection of English/French/Bilingual/B&W/Colour logo varieties, the use of the logo with website links should be made optional to Dealer Members. If a CIRO website link was intended to be a requirement however, that ought to have been addressed as part of the CIRO rebranding which has already been undertaken.

Regarding the CIRO brochure, while it is already part of Investment Dealer processes and documentation provided on account opening, the rule should simply require providing the brochure to clients upon request (i.e. by providing a link to a downloadable and printable copy). This would allow Dealer Members who already provide the brochure on account opening to determine if they wish to change their disclosure processes.

Uniform rules with respect to CIRO membership disclosure is ideal, however the result should not impose additional costs and resource burdens to Dealer Members as it is clear there is no meaningful policy benefit in requiring such expenditures. In this vein we also agree with removal of the CIRO decal display requirement as proposed.

5. **Our assessment of the proposed harmonization of the transfer requirements suggests minimal impact to dealer members. Do you agree with this assessment? If not, what potential challenges do you anticipate?**

   As noted in CIRO's consultation materials, most Mutual Fund Dealer transfers occur outside of CDS ATON via transfer form or via FundSERV and we note the current Mutual Fund Dealer Transfers Rule 2.12 is brief, requiring authorizing instructions and dealers to simply act promptly to facilitate the transfer of the account. Recognition of this existing operational process appears to be through proposed Rule 4860 and it is indicated in the consultation materials that Mutual Fund Dealers that are not a participant of CDS ATON can continue to complete securities transfers via transfer form or FundSERV. However, proposed Rules 4852 to 4865, which appear to generally be suited for Investment Dealer account transfers through CDS ATON, should expressly indicate they are only applicable for Mutual Fund Dealers if they are participants of CDS ATON, to avoid appearing to require all Mutual Fund Dealers to become participants of CDS ATON and causing confusion.

6. **We believe that harmonizing trading and delivery standards for securities will be of minimal impact to Dealer Members' current practices. Do you agree? Why or why not?**

   We agree with CIRO's assessment that the impact to Dealer Members will be minimal.

7. **To deter Regulated Persons from misconduct, we propose increasing the maximum fine a CIRO hearing panel can impose to $10 million per offence, from $5 million. Do you agree with our proposal to increase the maximum fine a CIRO hearing panel can impose? Why or why not?**

In our view, the proposed doubling of the maximum fine is well outside the scope of the following stated objectives of the CIRO Rule Consolidation Project:

> The intended objectives to be realized through this project are as follows:
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> - Greater rule harmonization to:
>   - ensure like dealer activities will be regulated in a like manner
>   - minimize regulatory arbitrage between investment dealers and mutual fund dealers
> - Where practical and appropriate, adopt less prescriptive, more principles-based rule requirements to facilitate rules that are scalable and proportionate to the different types and sizes of dealers and their respective business models
> - Improve access to and clarity of the rules applicable to all CIRO Dealer Members, which will be known as the CIRO Dealer and Consolidated (DC) Rules.[2]

The increase in the maximum fine is also not in line with the spirit of the CIRO Sanctions Guidelines[3] (**Guidelines**). The Guidelines underline the principle of ensuring sanctions are proportionate and consider the impact on the respondent, including with respect to the size of the Dealer Member, the firm's financial resources, the nature of the firm's business and the number of individuals associated with the firm and an individual respondent's *bona fide* inability to pay. Ensuring proportionate sanctions includes ensuring proportionate maximum fines.

A review of recent CIRO enforcement reports indicates that the proposed doubling of the maximum fine would not be proportionate, as there have not been a significant number of fines issued that approach the current $5 million maximum. We also note that a $10 million maximum far exceeds fine limits set in provincial and territorial Securities Acts for offences

[2] Rule Consolidation Project Update | Canadian Investment Regulatory Organization (ciro.ca)
[3] Sanction Guidelines | Canadian Investment Regulatory Organization (ciro.ca)

and administrative penalties, with maximums typically set at $5 million per offence and $1 million for administrative penalties per contravention. No jurisdiction in Canada has legislated a maximum set fine of greater than $5 million for securities law violations. [4]

The proposed increase in the maximum fine should also be considered in the context of the proposed fee increases under the Integrated Fee Model despite the cost savings and efficiency gains that were expected benefits of SRO amalgamation. SRO amalgamation should, to the greatest extent possible, produce those cost savings and efficiency gains rather than increased regulatory revenue, even in the enforcement rule paradigm. In keeping with this objective, identifying efficiency and cost saving opportunities with respect to investigation and enforcement processes should be the focus.

Finally, leveraging the CIRO Rule Consolidation Project to double the maximum fine, without a well-founded policy rationale, invites the potential for unprincipled and arbitrary penalties in contested matters which will go beyond effective deterrence and evidence-based rulemaking. This risks the unintended consequence of reducing the availability of investment advice to the public due to a chill on professionals and firms engaging in business under such conditions.

8. **To help ensure that individuals do not engage in any activities that defeat the purpose of any CIRO sanction they might receive, we propose barring Regulated Persons from hiring or engaging in any capacity and remunerating any individuals who are subject to a bar or suspension during the period of the bar or suspension. Under this prohibition, Regulated Persons would still be able to pay remuneration to a sanctioned individual that is:**

    - **consistent with the scope of activities permitted under the sanction, or**
    - **pursuant to an insurance or medical plan, an indemnity agreement relating to**

[4] Statutory maximums in all provinces and territories other than QC and MB are: $5 million per offense or in some cases disgorgement; $1 million administrative penalty per contravention. MB: $5 million per offence, $500K administrative penalty. QC: $5 million per offence or disgorgement; $2 million administrative penalty.

legal fees or as required by arbitration awards or court judgment.

Under the IDPC Rules, Regulated Persons are prohibited from engaging an individual who is permanently barred from employment with an investment dealer. Under the MFD Rules, there is no specific prohibition, however, in practice Regulated Persons cannot engage any individuals to perform securities-related business where they have been barred or suspended from doing so.

Do you agree with our proposal to expand the activity restrictions on sanctioned individuals? Why or why not?

The proposed expanded activity restrictions will be casting the net too widely in terms of preventing individuals from working in *any* capacity for the Dealer Member, which may be problematic from an employment law perspective. We recommend CIRO provide clarification as to the employment law implications arising from the proposed expanded restrictions. Otherwise, the proposed expanded restrictions should be applied only to individuals who have been permanently barred from employment with a Dealer Member.

In addition, although “remuneration” is a defined term, given the proposed expanded restrictions, it would be beneficial if CIRO provided examples of the types of payments that would be considered “remuneration” and thus not permissible to be paid to individuals who are subject to a bar or suspension. It would also be helpful to clarify the timing of the remuneration restriction by specifying that any remuneration owing prior to the effective date of the bar or suspension would be permitted to be paid. For example, if the bar or suspension were to take effect on July 1, payment of any remuneration owing up to and including June 30 would be permitted.

Shared Premises

The outcomes from this proposed rule harmonization concerning shared premises do have a material impact on stakeholders although not assessed as such in the consultation materials. In our view, certain aspects of the requirements with respect to shared premises do not adequately accommodate arrangements whereby bank owned Mutual Fund Dealers operate out of bank branches, where Mutual Fund Dealing Representatives are dually employed by the bank and sell both GICs and mutual funds. In addition, the carry-over from the Investment Dealer rules of a more stringent method of obtaining consent to disclosure of information between members of the financial institution's businesses than required under privacy law, for shared premises specifically, is unnecessarily burdensome and operationally unwieldly for all Dealer Members without any regulatory necessity. Specifically:

- **Rules 2218(4)(ii) and 2218(5).** These requirements are impractical to operationalize simply for shared premises and have no regulatory value. The Mutual Fund Dealer Rules only refer to obtaining authorization as necessary under applicable privacy legislation, and do not require any more stringent consent method for any context. Rules 2218(4)(ii) and 2218(5) can thus be deleted as they are also not necessary in light of the requirement under Rule 2218(4)(i) to obtain client consent to the disclosure of confidential information. We believe the Rule 2218(4)(i) requirement addresses client confidentiality and privacy in the shared premises context sufficiently and in a consistent manner with applicable law in all circumstances.

- **Rule 2218(1).** The requirement that shared office premises be "laid out and operated" in a manner that ensures the control and confidentiality of client information could be taken to mean that firms are expected to reconfigure their premises. This would not be practical, especially in the case of Dealer Members that have Mutual Fund Dealer Representatives dually employed with banks.

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We thank you for taking the time to consider our views regarding Phase 3 and trust that you will find these comments helpful. We would be pleased to discuss our comments further at your convenience.