

# IIROC NOTICE

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Dealer Member Rules

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## **Guidance on Order Execution Only Services and Activities**

### **Summary**

This Guidance on order execution only (**OEO**) services offered by Dealer Members (**OEO firms**):

- sets out our expectations and the regulatory requirements applicable to all OEO firms
- discusses the scope of tools, services, activities and information (collectively, **tools**) that we consider to be consistent with the OEO regulatory framework.

OEO firms should evaluate their existing and future tools against this Guidance to determine whether they are consistent with the OEO regulatory framework. Whether or not a particular tool is appropriate under the OEO regulatory framework depends on the relevant facts and circumstances of the particular case. As such, this Guidance is not intended to be exhaustive. We encourage OEO firms to speak to us about any current or proposed tools if they have any questions.

**Appendix A** provides, as a reference, a summary of the key matters discussed in this Guidance.



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## 1. Background

The OEO business model was designed to provide investors who are comfortable making their own investment decisions with a lower-cost option to the traditional full-service dealer model. OEO firms provide their clients with access to an online trading platform that allows them to trade securities, on their own, without the benefit of receiving any recommendations or suitability assessment from the OEO firm.

As the OEO business model has evolved, OEO firms have made available a wide variety of new and innovative tools to help educate and inform clients. This Guidance covers:

- certain regulatory requirements applicable to the OEO business model
- the scope of tools that we consider consistent with the OEO regulatory framework.

OEO firms should evaluate their existing and future tools against this Guidance to determine whether they are consistent with the OEO regulatory framework.

## 2. Regulatory Framework

IIROC's regulatory requirements, which set out the basic framework for the OEO business model, are designed to ensure that an OEO firm's clients make their own investment decisions, without receiving any recommendations or suitability assessment from the OEO firm.<sup>1</sup> To this end, IIROC rules prohibit OEO firms from providing any recommendations (**Recommendation Prohibition**).<sup>2</sup> So long as an OEO firm does not provide any recommendations to clients, IIROC rules exempt the OEO firm from the suitability requirements<sup>3</sup> (**OEO Suitability Exemption**)<sup>4</sup>.

In this Part, we provide our views on certain regulatory requirements applicable to the OEO business model. Part 3 of this Guidance sets out our views on the meaning of the term "recommendation" for purposes of the Recommendation Prohibition.

### 2.1 OEO Suitability Exemption

The OEO Suitability Exemption exempts OEO firms from all suitability obligations (order and non-order related).<sup>5</sup> OEO firms are not responsible for suitability arising from non-order related events such as transfers out or changes in life circumstances of a client.

### 2.2 Appropriateness

IIROC expects Dealer Members to determine, prior to opening an account, whether:

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<sup>1</sup> To assist readers, we have included footnotes in this Guidance referencing applicable Plain Language Rule Book (PLR) provisions (see [Notice 18-0014 - Re-publication of Proposed IIROC Dealer Member Plain Language Rule Book](#)). Since PLR is not yet effective, we have shaded these footnotes in grey. Upon implementation of PLR, we will remove the grey shading from the footnotes and delete this footnote.

<sup>2</sup> See definition of "order execution only account" in subsection 1201(2) of the IIROC rules.

<sup>3</sup> The suitability requirements are in subsections 3402 and 3403 of the IIROC rules.

<sup>4</sup> The OEO Suitability Exemption is in subsection 3404(1) of the IIROC rules.

<sup>5</sup> See subsection 3404(1) of the IIROC rules.



- (a) it would be appropriate for an investor to become a client of an OEO firm (**Account Appropriateness**)<sup>6</sup>
- (b) the scope of products and account types that a *specific* potential client would have access to within their account would be appropriate for that potential client (**Product/Account Type Appropriateness**)<sup>7</sup>.

Below are our views on the application of Account Appropriateness and Product/Account Type Appropriateness in the context of the OEO model.

### 2.2.1 Account Appropriateness

We believe there may be circumstances where it would not be appropriate for an investor to become a client of the OEO firm. OEO firms should be mindful of certain “red flags” which indicate that it would be inappropriate for the investor to engage in self-directed investing. These include circumstances where it is obvious that:

- the person would be incapable of conducting online activities (e.g., clear and persistent difficulties in completing the OEO firm’s online new-account application form)
- the investor is looking for advice.

### 2.2.2 Product/Account Type Appropriateness

We are of the view that OEO firms need not conduct Product/Account Type Appropriateness for a potential client, as it is inconsistent with a suitability-exempt business model.<sup>8</sup> Nevertheless, the scope of products an OEO firm chooses to make available on its platform for *all clients* generally must be in accordance with IIROC requirements and other applicable securities laws. For example, under securities laws, OEO firms are prohibited from making available certain products to any of their clients (e.g., binary options<sup>9</sup>) or may only make available certain products to qualifying clients (e.g., through private placements<sup>10</sup>).

OEO firms are also required to meet IIROC requirements and other applicable securities laws (including terms and conditions) when offering certain specific products or account types to a client(s). For example, IIROC requirements include specific obligations when offering contracts for difference<sup>11</sup>, margin accounts and options, futures contract and futures contract options products<sup>12</sup>.

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<sup>6</sup> See clause 3211(1)(i) of the IIROC rules.

<sup>7</sup> See clause 3211(1)(ii) of the IIROC rules.

<sup>8</sup> See subsection 3211(2) of the IIROC rules.

<sup>9</sup> Pursuant to [Multilateral Instrument 91-102 Prohibition of Binary Options and Related Companion Policy](#), most provinces and territories in Canada have made it illegal to advertise, offer, sell or otherwise trade binary options shorter than 30 days with any individual.

<sup>10</sup> Private placements can only be made available to investors who qualify to purchase such products (e.g., accredited investors) under applicable securities laws.

<sup>11</sup> See [Regulatory Analysis of Contracts for Differences \(CFDs\)](#), as amended on September 12, 2007 for a discussion on CFDs.

<sup>12</sup> See Parts E and F of IIROC rule 3200.



OEO firms are reminded of their regulatory obligations when they consider which products to make available on their platforms for clients generally. For example:

- (a) *Product Due Diligence.*<sup>13</sup> As described in [Notice 09-0087](#), as gatekeepers to the securities industry, Dealer Members (including OEO firms) must take a proactive approach to reviewing and improving their procedures for introducing new products and monitoring those that are not new but that have unique and complex features that may require monitoring.
- (b) *Conflicts of Interest.*<sup>14</sup> Under IIROC rules, conflicts of interest must be addressed by a Dealer Member considering the best interests of the client or clients. For example, OEO firms should consider any compensation-related conflicts when deciding which series (or series equivalent in the case of a platform traded fund (**PTF**)) of a fund to make (or not make) available on their platforms.

### 2.3 Other IIROC Requirements

OEO firms must comply with all IIROC requirements other than those for which they are specifically exempted.<sup>15</sup> Notwithstanding, we note that there may be circumstances where an OEO firm satisfies an IIROC requirement differently than a full-service dealer due to the nature of the OEO regulatory framework.

For example, the know-your-client (**KYC**) obligation requires all Dealer Members to use due diligence to learn and remain informed of the essential facts concerning every client and for every order or account they accept.<sup>16</sup> We interpret this requirement, in the context of the OEO business model, to exclude OEO firms from having to collect KYC information that is relevant only to assist Dealer Members in meeting their suitability obligation.

In other words, since OEO firms are not required to assess suitability with respect to their clients, it is reasonable that OEO firms need not collect KYC information that is normally collected by Dealer Members solely for purposes of suitability. However, OEO firms are required to collect certain KYC information for purposes other than suitability (e.g., meeting their anti-money laundering obligations).

## 3. Recommendations

As discussed in Part 2, the Recommendation Prohibition prohibits an OEO firm from providing recommendations. So long as an OEO firm does not provide any recommendations, it:

- is exempt from the suitability requirements
- need not conduct a Product/Account Type Appropriateness analysis with respect to a potential client.

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<sup>13</sup> See [Notice 09-0087](#) - *Best practices for product due diligence* and also [Notice 09-0086](#) - *Response to comments received on draft guidance notice: "Best practices for product due diligence"*.

<sup>14</sup> See Part B of Rule 3100 in the IIROC rules.

<sup>15</sup> See subsection 2155(2) of the IIROC rules.

<sup>16</sup> See section 3103 of the IIROC rules.



In this Part 3, we provide our views on the meaning of the term “recommendation” for purposes of the Recommendation Prohibition. In addition, we have analyzed the more common tools currently offered by OEO firms and provided our views on the circumstances where such tools may constitute a recommendation.

### 3.1 Meaning of “Recommendation”

We are of the view that, for purposes of the Recommendation Prohibition, the term “recommendation” means:

*any communication or statement of opinion sent or made available to an investor (or class of investor) that could, based on the context or circumstances, reasonably be expected to influence that investor (or class of investor) to make an investment decision regarding a security (including any class of securities and the securities of a class of issuers) (collectively, **securities**).*<sup>17</sup>

We set out below our interpretation of certain wording used in the meaning of the term “recommendation”:

- (a) The phrase “any communication or statement of opinion” should be interpreted broadly to include:
- any tool offered or made available by an OEO firm
  - any form of communication (e.g., written or spoken).

How the communication or statement of opinion is generated or created is irrelevant. For example, it could be a simple mathematical calculation, computer generated, made by a live person or based on publicly available or confidential information (or a combination thereof).

- (b) The phrase “sent or made available” includes both direct and indirect communications. For example, it includes a message sent or directed to a particular client (or class of client) or merely posted on the OEO firm’s website that any investor may access.
- (c) The phrase “that could, based on the context or circumstances, reasonably be expected to” is intended to emphasize that whether or not a particular tool is considered to be a recommendation will depend on the relevant facts and circumstances of the particular case, and should be evaluated in that context.
- (d) The phrase “investor (or class of investor)” should be interpreted broadly to include:
- any investor (and not merely clients of the OEO firm)
  - any class of investor (e.g., conservative investors, investors within a certain demographic, etc.).

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<sup>17</sup> While the meaning of “recommendation” provided in this Guidance uses the specific term “security”, we believe it would be impractical, and potentially confusing to clients, for OEO firms to adopt a different meaning for investment products that may not be securities. Accordingly, we would expect OEO firms to apply this Guidance to all investment products offered, and not merely securities.



The primary focus of this Guidance is on tools an OEO firm makes available to its clients. However, we use the term “investor” in the meaning of recommendation to avoid the circumstance where an OEO firm posts a recommendation on its website that is accessible by any investor (client or non-client). OEO firms are prohibited from providing recommendations to clients and non-clients alike.

In this Guidance, the term “**investor**” means both an individual investor and any class of investor. Similarly, the term “**client**” or “**OEO client**” means both an individual client and any class of client of an OEO firm.

- (e) The term “investment decision” includes any of the following:
- the purchasing, selling, holding or exchanging of securities
  - the manner in which the purchase, sale or exchange of securities should be effected (e.g., the timing of a purchase).<sup>18</sup>

### 3.2 General Application of “Recommendation”

When assessing whether a particular tool may constitute a recommendation, OEO firms should consider the following:

(a) *Tailored Information vs. General Information*

Tailored Information is information that is customized or personalized to an investor using KYC-type information regarding the investor. Examples of tools providing tailored information include:

- informing a client that the OEO firm believes the client to be of a particular class of investor (e.g., based on asking the client questions or using any KYC-type information such as transaction history, etc.)
- providing information to clients based on their transaction history (e.g., informing the client “as you purchased Product X in the past, you may be interested in Product Y”).

Generally, we consider a tool that provides tailored information to be more likely to be a recommendation as it is more likely to be relied on by clients as relevant to them. However, there are circumstances where tailored information would not be considered a recommendation and would be appropriate under the OEO model.<sup>19</sup>

General Information is information that is not tailored or personalized to an investor.

Tools providing general information to clients are less likely to be a recommendation. However, general information may be a recommendation if it could reasonably be expected to influence an investor to make an investment decision; for example:

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<sup>18</sup> For example, see subsection 3.3.7 (*Trade Execution Assistant Tools*) of this Guidance.

<sup>19</sup> For example, see discussion in clause 3.3.12(c) (*Multiple Fund Series*) where OEO firms provide factual information (e.g., the availability of Series D of a fund) based on the tailored information that a client holds or is in the process of acquiring Series A of that fund.





- publishing a general communication advising investors to purchase a particular class of security
- pushing (see below) general information to a client.

(b) *“Push” vs. “Pull”*

Generally, a tool that is merely made available on an OEO firm’s website and can be “pulled” by a client is less likely to be a recommendation. In contrast, a tool (or information) that is “pushed”, or sent/directed, to a client is more likely to be considered a recommendation.

We believe that a tool that is pushed or pushes information to clients is more likely to be relied on by clients as relevant to them.

The relative importance of the “push vs. pull” consideration will depend on the tool and the facts and circumstances. In section 3.3 of this Guidance, we apply the “push vs. pull” consideration to various tools currently offered by OEO firms.<sup>20</sup> As discussed, we consider certain tools to be recommendations regardless of the fact that they are merely available on an OEO firm’s website to be “pulled” by clients.<sup>21</sup> Conversely, we consider other tools to not be recommendations so long as they are merely available on an OEO firm’s website and are not pushed to clients.<sup>22</sup>

(c) *Historical/Factual Information vs. Future/Predictive Information*

Generally, where a tool merely provides historical or factual information, it would likely not be considered to be a recommendation. This includes information on the past performance of an issuer, security or market segment.

In contrast, providing a prediction on how an issuer, security or market segment, will/may likely perform in the future would generally be considered a recommendation because it would reasonably be expected to influence clients’ investment decisions. Accordingly, other than as discussed in this Guidance<sup>23</sup>, OEO firms should ensure that their tools do not include any future and/or predictive information regarding an issuer, a security or market segment.

(d) *Use of Disclaimers*

While disclaimers are helpful to remind clients that OEO firms do not provide recommendations, OEO firms cannot circumvent the Recommendation Prohibition by

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<sup>20</sup> Specific examples of the application of the “push vs. pull” distinction in this Guidance are provided in subsections 3.3.7 (*Trade Execution Assistant Tools*), 3.3.10 (*Filtering Tools*) and 3.3.11 (*New Issues*) and clauses 3.3.12(b) (*Research Reports*) and 3.3.12(e) (*Model Portfolio Tools*).

<sup>21</sup> For example, see subsection 3.3.6 (*Trading Tools*).

<sup>22</sup> For example, see subsections 3.3.7 (*Trade Execution Assistant Tools*), 3.3.10 (*Filtering Tools*) and 3.3.11 (*New Issues*), clause 3.3.12(b) (*Research Reports*) and Permitted Model Portfolios discussed in clause 3.3.12(e) (*Model Portfolio Tools*).

<sup>23</sup> For example, see clause 3.3.12(b) (*Research Reports*).





providing disclosure to clients claiming that a tool, which is otherwise a recommendation, does not constitute a recommendation.

### 3.3 Specific Application of “Recommendation” to Tools

To help OEO firms evaluate their existing and future tools, we set out below how we apply the Recommendation Prohibition to the more common tools currently offered by OEO firms.

We note that this Guidance could not possibly contemplate all existing and future tools offered by OEO firms. *Whether a particular tool constitutes a recommendation will depend on an analysis of all the relevant facts and circumstances of the particular case and whether a reasonable person in similar circumstances would believe a recommendation has been made.*

#### 3.3.1 Pricing Incentives

OEO firms occasionally use (and post on their websites) pricing incentives (e.g., offering “commission free” or “low commission” exchange traded fund (**ETF**) trades). While such incentives may provide a financial incentive or encouragement for an OEO client to trade in a particular class of product, generally, and depending on the facts and circumstances, we do not view pricing incentives as being a recommendation.

While we generally do not consider pricing incentives as providing a recommendation, the particular facts and/or circumstances may lead to a different conclusion. For example, the following would more likely be considered to be a recommendation:

- a pricing incentive on a specific security (or small number of securities)
- a pricing incentive on a class of securities where the OEO firm only offers a single (or small number) of products within that class
- a pricing incentive that favours proprietary products.

We believe each of the above pricing incentives could reasonably be expected to influence persons to make an investment decision and is therefore more likely to be a recommendation.

#### 3.3.2 Fair Visibility, Availability and Accessibility

An OEO firm should ensure the fair visibility, availability and accessibility of all products and information it makes available.

It is inappropriate for an OEO firm to favour certain products (e.g., proprietary products) over other products (e.g., third-party products) by making it more difficult to execute trades or access information in the less favoured products. Examples of inappropriate practices include:

- requiring more “clicks” to execute a trade or access research
- making it difficult to obtain necessary documentation (e.g., FundFacts)
- obscuring or making information less prominent/visible (e.g., varying font sizes)

for the less favoured product.

Not only would we consider such practices as not dealing with clients fairly, honestly and in good faith, but we believe they could reasonably be expected to influence clients to make an investment decision.



### 3.3.3 Hyperlinks and Portals

Depending on the applicable facts and circumstances, we view hyperlinks and portals offered by an OEO firm to a third-party website (collectively, **Hyperlinks**) as generally acceptable.

However, where the content of the Hyperlink provides a recommendation, OEO clients may:

- (a) consider the content of the third-party website to be attributed to or endorsed by the OEO firm
- (b) not be aware that they have left the OEO firm's website.

These concerns are magnified where the Hyperlink is to the website of an affiliate/related company of the OEO firm with a similar business name.

Consistent with [Notice 11-0349](#) - *Guidelines for the review, supervision and retention of advertisements, sales literature and correspondence* (**Notice 11-0349**)<sup>24</sup>, whether or not a Hyperlink (or third-party communication) would reasonably be considered to be the OEO firm's communication will depend on the facts and circumstances of each case. As discussed in Notice 11-0349, OEO firms should consider:

- (a) the use of disclaimers
- (b) the nature of their involvement in the preparation of the third-party communication prior to posting
- (c) any evidence of explicit or implicit endorsement or approval of the communication by the OEO firm

to help determine whether or not the third-party post reflects the views of the OEO firm.

OEO firms should note that using disclaimers will not necessarily relieve them of their responsibility for Hyperlinks or third-party communications. Notice 11-0349 provides suggested best practices relating to third-party communications, including the development of policies and procedures to address the issues related to Hyperlinks.

### 3.3.4 Social Media

OEO firms should not engage in social media activities that could be considered recommendations. For example, re-tweeting or sharing of a third-party post or providing a "thumbs-up" or "liking" the post may be considered an endorsement and potentially a recommendation.

Some OEO firms make chat rooms available for their clients to discuss investment-related topics. We do not view chat rooms for "clients only" as inappropriate. However, a recommendation may occur if an OEO firm representative participates in chat room discussions with the intention (or effect) to influence a person(s) to make an investment decision (e.g., by discussing the merits of a security or class of securities).

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<sup>24</sup> See Part VI - *Third-Party Communications and Research* of [Notice 11-0349](#).



Please refer to subsection 3.3.3 on Hyperlinks and [Notice 11-0349](#) for guidance and suggested best practices on social media issues relating to third-party communications, including the development of applicable policies and procedures.

### 3.3.5 Integrated Tools

Some OEO firms offer tools that are integrated with third-party tools (**Integrated Tools**). For example, a third party may offer research reports<sup>25</sup> that provide a “trade now” functionality linked to an OEO firm’s platform. With a single click of the “trade now” button on the third party’s website, the client is automatically directed to the OEO firm for trade execution where the trade details (e.g. security name, etc.) are automatically populated.

Depending on the applicable facts and circumstances, we view Integrated Tools as generally acceptable. However, as discussed in connection with Hyperlinks, OEO clients may:

- (a) consider the content of the third-party website to be attributed to or endorsed by the OEO firm, or
- (b) not be aware that they have left the OEO firm’s website.

These concerns are magnified where the Integrated Tool is linked to the website of an affiliate/related company of the OEO firm with a similar business name. OEO firms should take steps to mitigate these risks.

Please refer to subsection 3.3.3 on Hyperlinks and [Notice 11-0349](#) for guidance and suggested best practices relating to third-party communications, including the development of applicable policies and procedures.

### 3.3.6 Trading Tools

We consider a “**Trading Tool**” to be a method or plan of trading in investment products that uses a predefined set of rules for making trading decisions. In other words, Trading Tools inform an investor of *what* trades to make.

The OEO firm may create the Trading Tool itself, or they may purchase or license it from a third party. Often, Trading Tools are delivered to, and used by, investors through computer programs (e.g., algorithmic trading programs) which either: (a) automatically trade on the investor’s behalf; or (b) provide the investor with suggested trades that they subsequently execute on their own.

As Trading Tools are intended to influence clients’ investment decisions, we view Trading Tools made available by OEO firms to their clients<sup>26</sup> as recommendations and therefore a violation of the Recommendation Prohibition. As such, Trading Tools should not be made available by OEO firms.

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<sup>25</sup> See clause 3.3.12(b) (*Research Reports*).

<sup>26</sup> This may also include the endorsement of third-party trading tools. Please refer to subsection 3.3.3 (*Hyperlinks and Portals*) for a discussion on third-party communications.



Further, except for Automatic Rebalancing Tools<sup>27</sup>, we note that making available a Trading Tool that automatically trades on a client's behalf may be considered to be providing managed account services requiring registration as a portfolio manager with IIROC or a Canadian securities regulatory authority.

### 3.3.7 Trade Execution Assistant Tools

As discussed above, while a "Trading Tool" informs an investor of *what* trades should be made, we consider a "trade execution assistant tool" to be a method or plan on *how* or *when* to most effectively execute a trade(s) (**Trade Execution Assistant Tool**). For example, assuming a client wanted to make a large purchase of a single security, a Trade Execution Assistant Tool would inform the investor on how or when to effect the purchase(s).

Trade Execution Assistant Tools may be a recommendation depending on how they are offered.<sup>28</sup> So long as the Trade Execution Assistant Tool is merely made available on an OEO firm's website to be "pulled" by the client, without prompting or influence by the OEO firm, we would not consider it to be a recommendation.

For example, OEO firms may offer their clients the option of how to execute trades (e.g., Volume Weighted Average Price, Percentage of Volume or Time). So long as the choice is made by the client, on their own initiative, without any recommendation provided by the OEO firm regarding which of these options, if any, a client should choose, we would consider such options acceptable.

Further, OEO firms remain subject to best execution obligations and other regulatory requirements in effecting trades on behalf of their clients.<sup>29</sup> An OEO firm using an automated "smart order router" to meet its best execution obligations for *all OEO client trades* can be distinguished from a Trade Execution Assistant Tool in that a Trade Execution Assistant Tool is tailored to a specific client, or class of clients.

### 3.3.8 Pre-entering of Orders

A common tool made available by many OEO firms permits clients to "pre-enter" an order (i.e., on the client's own initiative and without any recommendation from the OEO firm). For example, a client may wish to place an order for a security for a later date or when the security reaches a particular price (e.g., a limit order). This type of tool does not, in our view, constitute a recommendation.

### 3.3.9 Automatic Rebalancing Alerts & Tools

Some OEO firms offer clients the ability to rebalance their account holdings to pre-determined levels.

For example, a client who holds four different securities in their account may wish to maintain a balanced account such that each security represents 25% of the total account. To facilitate, an OEO firm could:

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<sup>27</sup> As discussed in subsection 3.3.9, an Automatic Rebalancing Tool automatically re-balances a client's account in accordance with a client's pre-determined instructions. In contrast, a Trading Tool does not use a client's predetermined instructions. Rather, the Trading Tool itself generates the trade instructions and either automatically trades on behalf of the investor or provides the investor with suggested trades which the client could then subsequently execute on their own.

<sup>28</sup> As discussed in clause 3.1(e), we consider the phrase "investment decision" to include not only influencing a person on which particular security to purchase or sell, but influencing the manner in which the purchase or sale should be made.

<sup>29</sup> OEO firms should refer to the applicable Canadian securities laws and IIROC rules, regulations and guidance notices relating to best execution and direct electronic access.



- (1) offer a service whereby an alert message is sent to the client if the client's account moves outside the client's desired pre-determined levels (**Rebalancing Alert**), or
- (2) automatically make the appropriate transactions to re-balance the account in accordance with the client's desired levels (**Automatic Rebalancing Tool** and, together with the Rebalancing Alert, **Rebalancing Tools**).

Assuming the OEO firm did not influence the client's determination of their desired pre-determined levels or rebalancing instructions (in other words, the OEO firm did not provide any recommendations) then, depending on the applicable facts and circumstances and subject to the discussion below, we do not view Rebalancing Tools as recommendations.

A Rebalancing Alert notifies the OEO client that his/her account has moved outside their chosen pre-determined levels (without any recommendations from the OEO firm). Upon receiving an alert, the OEO client may or may not choose to rebalance the account.

If an Automatic Rebalancing Tool was merely acting on an OEO client's instructions (provided when the client acted alone in selecting its pre-determined levels or rebalancing instructions) to execute rebalancing transactions, we would not consider this activity to influence a client's investment decisions.

Notwithstanding our view that Rebalancing Tools are generally not recommendations, these tools raise certain risks and concerns that OEO firms should consider and address.

- (a) *As discussed above, OEO firms should not provide any recommendations that could influence a client's selection of his/her desired pre-determined levels or rebalancing instructions.* Further, OEO firms should never retain any level or form of discretion to carry out investment decisions (e.g., purchases, sales, exchanges or holds of securities) on a client's behalf through a Rebalancing Tool.

If an OEO firm were to provide a recommendation in connection with the client's initial rebalancing instructions and then make available an Automatic Rebalancing Tool, this could be considered to be discretionary management and require registration as a portfolio manager with IIROC or a Canadian securities regulatory authority.

- (b) In dealing with clients honestly, fairly and in good faith, OEO firms should ensure that their clients understand details relating to the Automatic Rebalancing Tool, including:
  - the frequency of the Automatic Rebalancing Tool's review and rebalancing of the client's account for conformity with the client's instructions
  - cost/fee implications<sup>30</sup>

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<sup>30</sup> For example, an OEO firm normally charges a commission/fee per transaction. However, under an Automatic Rebalancing Tool, the client/OEO firm may not know the number of transactions that would be effected because of the Automatic Rebalancing Tool.



- details about which securities will be purchased and sold to rebalance the client's account and rebalancing parameters.<sup>31</sup>

(c) *Confirmation of Rebalancing Instructions*

Clients who create rebalancing instructions using an Automated Rebalancing Tool may forget that they created the instructions or experience a change in circumstance necessitating a change in their instructions.

Accordingly, OEO firms should obtain periodic confirmations (no less than quarterly) from clients that the automatic rebalancing instructions should continue.

(d) *Unintended Consequences*

There may be circumstances where an Automatic Rebalancing Tool creates an unintended consequence that could be potentially harmful to clients.

Recall the example of a client who holds four different securities in their account and wishes to maintain a balanced account where each security represents 25% of the account total. Assume that one of the securities is of an issuer that experiences a catastrophic event causing its security price to plummet. Under the pre-determined rebalancing instructions, as the value of the client's holdings in this particular security drops, the Automatic Rebalancing Tool would automatically sell some of the client's holdings in the remaining three securities to purchase more of the plummeting security. While the client selected their pre-determined levels and rebalancing instructions with the goal of maintaining a "balanced" account to minimize their risk of over-exposure to any one of the four securities, the unintended consequence of the Automatic Rebalancing Tool is that it could over-expose the client to a security rapidly declining in value.

OEO firms should implement safeguards to manage the risks to clients related to unintended consequences of Automatic Rebalancing Tools; for example, implementing appropriate alerts to clients should the value of any single security change significantly in a short period.

### 3.3.10 Filtering Tools

Many OEO firms allow clients to sort or filter the list of all securities the OEO firm has available for purchase and sale (**Filtering Tools**). These Filtering Tools allow clients to sort all available securities by criteria such as the name of the issuer, industry sector, trading volume or some other factual criteria relating to the security.

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<sup>31</sup> Consider the previously cited example of a client wishing to maintain each of his/her four securities at 25% of the account total. OEO clients should be provided with details of when will the Automatic Rebalancing Tool take effect (e.g., when any one security represents greater than 30% or less than 20% of the account total, or another amount?).



We do not consider Filtering Tools to be recommendations, so long as the client initiates (pulls) the sorting/filtering.

An OEO firm should not narrow the list of securities available to a client on its own initiative or suggest any product(s) based on client-related information (e.g., asking the client leading questions, data mining of previous purchases and/or sales<sup>32</sup> or using any KYC-type information gathered about the client).

For example, consider a scenario where an OEO firm offers 20 securities of technology sector issuers on its platform. Where a client searches for all securities of technology sector issuers offered by the OEO firm, the firm's Filtering Tool should list all 20 securities in response to the client's query. If the OEO firm narrows the list to provide the client with less than 20 securities, then it would be providing a recommendation.

In the above example, the client could choose to narrow the list of 20 securities based on some additional factual criteria (e.g., trading volume), but the resulting list produced by the Filtering Tool should be reflective of the entire list of available products meeting the client's query.

#### 3.3.11 New Issues

Some OEO firms make initial public offerings (**New Issues**) available to clients. New Issues that are merely made available on an OEO firm's website to be pulled by a client, without prompting or influence by the OEO firm, are not generally considered to be recommendations.

However, OEO firms should not push any New Issues to clients, for example by providing information about a particular New Issue to a client based on tailored information (e.g., KYC-type information or transaction history). Further, an OEO firm should be mindful of not providing any explicit or implicit endorsement of any New Issues made available on its website.

#### 3.3.12 Informative Tools

Many OEO firms make a variety of tools available to their clients that are designed to inform and/or educate clients (collectively, **Informative Tools**). Informative Tools are undoubtedly helpful to clients; however, they may, depending on the facts and circumstances, be considered to be recommendations if they could reasonably be expected to influence a person's investment decision.

In addition to the general considerations set out in section 3.2, below are our views on some of the more common Informative Tools currently made available by OEO firms.

##### (a) *Educational Tools*

Educational tools are often made available by OEO firms to educate clients on, among other things, a particular class of securities or trading in general (**Educational Tools**).

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<sup>32</sup> We consider an OEO firm that provides clients with suggested securities based on previous transactions (or data mining) to be providing a recommendation. However, data mining for purposes other than for providing a recommendation is generally acceptable. For example, see clause 3.3.12(c) (*Multiple Fund Series*), which contemplates data mining of security holder information for purposes of providing factual information regarding lower cost fund series.





Whether a particular Educational Tool constitutes a recommendation is contextual. The appropriate test is whether, on balance, the primary purpose of the Educational Tool is to educate clients or whether it is to influence the client's investment decisions.

For example, consider an Educational Tool on "*What are Options?*". Depending on the specific facts and circumstances, if the primary purpose of the tool is to educate clients on options and option trading, then we would not view this as a recommendation. However, if the tool reasonably appears to be a selling tool (e.g., recommending a specific option trading strategy/strategies or option product(s) or describing the ease of option trading and potential for profit), then it would likely be considered a recommendation.

(b) *Research Reports*

Normally, a research report contains an analyst's recommendation about the purchase, sale or holding of a security.<sup>33</sup> Notwithstanding, we do not generally consider these 'recommendations' as providing sufficient motivation to influence a client's investment decision, due in part to investors' increased familiarity with research reports.

However, research reports may be a recommendation depending on how the information is presented to clients. So long as they are merely made available on an OEO firm's website to be "pulled" by the client, without prompting or influence by the OEO firm, we would not consider them recommendations.

(c) *Multiple Fund Series*

OEO firms may offer various series of the same or equivalent funds (e.g., Series A or D of the same fund or the equivalent PTF).<sup>34</sup>

We do not consider it to be a recommendation when an OEO firm provides factual information to a client of the availability of a lower-cost series of a fund the client holds or is in the process of acquiring (e.g., the availability of Series D, or the equivalent PTF, where the client holds or is in the process of acquiring Series A of that fund).

(d) *Portfolio Analyzer Tools*

Portfolio Analyzer Tools (sometimes referred to as "Asset Allocation Tools") provide a breakdown, sorting, grouping or distribution (collectively, a **breakdown**) of a client's *existing* holdings by class of security, industry sector or another criteria.

For example, an OEO client may wish to learn the breakdown of his/her account by asset class (e.g., equity, debt and mutual funds). The Portfolio Analyzer Tool would merely reveal the breakdown of the client's account holdings to be: X% in equities, Y% in debt and Z% in mutual funds.

Portfolio Analyzer Tools do not provide clients with suggestions or indications of future trades a client should/could make to achieve a particular breakdown. They provide clients with information on what the breakdown of their account currently *is* (rather than what it *should be*).

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<sup>33</sup> See definition of "research report" in subsection 1201(2) of the IIROC rules.

<sup>34</sup> As discussed in subsection 2.2.2 of this Guidance, OEO firms are reminded of their conflicts of interest related obligations when they consider which series (or series equivalent in the case of a PTF) of a fund they make available on their platforms. *IIROC Notice 18-0076 – Rules Notice – Guidance Note – Dealer Member Rules – Guidance on Order Execution Only Services and Activities*



Our view is that Portfolio Analyzer Tools do not constitute a recommendation as they merely provide factual information regarding a client's existing holdings and are not meant to influence an OEO client's investment decision.

(e) *Model Portfolio Tools*

A Model Portfolio Tool provides clients with examples of portfolios or portfolio distributions that purport to be an appropriate guide for building a portfolio. For example, a model portfolio may show a suggested portfolio by security, class of asset or industry sector, or be based on a specific type of investor and/or time horizon.

In contrast to Portfolio Analyzer Tools, Model Portfolio Tools assist or influence clients in making *future* investment decisions (or, a breakdown of what the account *should be*) by suggesting model portfolios which the client may attempt to emulate. As such, we generally view them as a recommendation.

However, depending on the context in which they are made available, certain limited Model Portfolio Tools may be acceptable, provided they:

- (i) are limited to class of investor, asset class, industry sector and/or time horizon,
- (ii) do not reference specific securities (as defined below) or issuers, and
- (iii) are only made available on OEO firms' websites to be "pulled" by the client, without prompting or influence by the OEO firm, and are not "pushed" to clients.<sup>35</sup>

We refer to such limited Model Portfolios as "**Permitted Model Portfolios**".

We do not generally consider Permitted Model Portfolios as providing sufficient motivation to influence a client's investment decision, due in part to investors' increased familiarity with model portfolios.

We interpret "**specific securities**" broadly to include any security that may be purchased by an investor, including but not limited to any equity, debt or fixed-income product, mutual fund, ETF and/or PTF. Model Portfolio Tools should not refer to specific securities or issuers, as we consider any model portfolio that names specific securities or issuers to be significantly more likely to influence a client's investment decision than a model portfolio that is limited to broader asset classes and/or industry sectors.

Additional guidance is provided below regarding each of the four acceptable bases for Permitted Model Portfolios.

- (1) *Class of Investor.* Examples of "Classes of Investors" include "Conservative Investor", "Balanced Investor", "Aggressive Investor", or other such names as determined by an OEO firm.

Regardless of the name used to describe them, an OEO firm should provide a definition for each Class of Investor used in its Permitted Model Portfolio. Clients may then use these

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<sup>35</sup> Please refer to clause 3.2(b) for general guidance on the "push vs. pull" distinction.



definitions to determine, for themselves (without any assistance or suggestion provided by the OEO firm), which Class of Investor best suits them.

An OEO firm should not:

- (a) help a client determine what Class of Investor he/she is,<sup>36</sup> or
  - (b) inform a client that the OEO firm believes the client to be a particular Class of Investor (e.g., by asking the client questions, using KYC-type information or transaction history, or by any other method).
- (2) *Asset Class*. Examples of “Asset Classes” include “Equities”, “Debt”, “Mutual Funds” and other such name(s) as determined by the OEO firm. OEO firms should provide a definition for each Asset Class used in their Permitted Model Portfolios.
  - (3) *Industry Sector*. Examples of “Industry Sectors” include “Financial Services”, “Agriculture”, “Manufacturing”, etc. OEO firms should provide a definition for each Industry Sector used in their Permitted Model Portfolios.
  - (4) *Time Horizon*. “Time Horizons” help ensure that OEO clients appreciate whether the Permitted Model Portfolio is designed for “short-term”, “mid-term” or “long-term” investment. OEO firms should define each Time Horizon used in their Permitted Model Portfolios (e.g., “short term” means “less than 2 years”).

OEO firms may couple their Permitted Model Portfolios with their Filtering Tools (see subsection 3.3.10) to allow clients to identify those specific securities that are consistent with a Permitted Model Portfolio. For example, where a Permitted Model Portfolio identifies a particular Asset Class or Industry Sector (such as “Manufacturing Sector”), the OEO firm may provide a link to its Filtering Tool to identify *all* Manufacturing Sector securities it offers.

We set out examples of certain Permitted Model Portfolios in **Appendix B**. We also include examples of model portfolios that we consider inappropriate for OEO firms to make available to clients (referred to as **Non-Permitted Model Portfolios**).

#### 4. Conclusion

This Guidance is not intended to be exhaustive. OEO firms should evaluate their existing and future tools against this Guidance to determine whether they are consistent with the OEO regulatory framework. Whether or not a particular tool constitutes a recommendation will depend on an analysis of all the relevant facts and circumstances of the particular case.

We encourage OEO firms to speak to us about their current and proposed tools if they have any questions.

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<sup>36</sup> Other than by providing a definition for each Class of Investor as discussed in the preceding paragraph.  
*IIROC Notice 18-0076– Rules Notice – Guidance Note – Dealer Member Rules – Guidance on Order Execution Only Services and Activities*



## 5. **Attachments**

Appendix A – *Guidance Summary*

Appendix B – *Examples of Permitted & Non-Permitted Model Portfolios*



Summary of Guidance

Guidance Reference	Topic	Summary
Part 1	Background	Provides background on the OEO business model.
Part 2	Regulatory Framework	Describes IIROC's regulatory requirements applicable to the OEO business model.
Part 3	Recommendations	Describes what may or may not constitute a "recommendation" for purposes of the Recommendation Prohibition.
Section 3.1	Meaning of "Recommendation"	Provides that "recommendation" means: <i>any communication or statement of opinion sent or made available to an investor (or class of investor) that could, based on the context or circumstances, reasonably be expected to influence that investor (or class of investor) to make an investment decision regarding a security (including any class of securities and the securities of a class of issuers).</i>
Section 3.2	General Application of "Recommendation"	Provides general interpretive guidance for OEO firms to consider when assessing whether a particular tool may be a recommendation.
Section 3.3	Specific Application of "Recommendation"	Sets out our analysis of some of the more common tools currently being offered by OEO firms.  Whether a particular tool constitutes a recommendation will depend on an analysis of all the relevant facts and circumstances of the particular case and whether a reasonable person in similar circumstances would believe a recommendation has been made.
Subsection 3.3.1	Pricing Incentives	Pricing incentives are generally acceptable, depending on the facts and circumstances. A pricing incentive would more likely be considered a recommendation where it: <ul style="list-style-type: none"> <li>• is on a specific security (or small number of securities)</li> <li>• is on a class of securities, but the OEO firm only offers a single (or small number) of securities within that class, or</li> <li>• favours proprietary products.</li> </ul>
Subsection 3.3.2	Fair Visibility, Availability and Accessibility	OEO firms should ensure the fair visibility, availability and accessibility of all products and information they make available.
Subsection 3.3.3	Hyperlinks & Portals	Hyperlinks offered by an OEO firm to a third-party website are generally acceptable, depending on the facts and circumstances.  Consistent with Notice 11-0349, OEO firms should consider: <ul style="list-style-type: none"> <li>• the use of disclaimers</li> <li>• the nature of involvement in preparation of third-party communication</li> <li>• any evidence of explicit or implicit endorsement</li> </ul> to help determine whether or not the third-party post reflects the views of the OEO firm.



Guidance Reference	Topic	Summary
Subsection 3.3.4	Social Media	OEO firms may engage in social media activities, so long as they do not engage in activities that would be considered recommendations.
Subsection 3.3.5	Integrated Tools	<p>Integrated Tools are generally acceptable, depending on the facts and circumstances.</p> <p>Consistent with Notice 11-0349, OEO firms should take steps to mitigate the risks that OEO clients:</p> <ul style="list-style-type: none"> <li>• consider the content of a third-party website to be attributed to or endorsed by the OEO firm, or</li> <li>• are not aware that they have left the OEO firm’s website.</li> </ul>
Subsection 3.3.6	Trading Tools	Trading Tools constitute recommendations and accordingly violate the Recommendation Prohibition. Trading Tools should not be made available by OEO firms.
Subsection 3.3.7	Trade Execution Assistant Tools	<p>Trade Execution Assistant Tools may be a recommendation depending on how they are offered. So long as the Trade Execution Assistant Tool is merely made available on an OEO firm’s website to be “pulled” by the client, without prompting or influence by the OEO firm, we would not consider it to be a recommendation.</p> <p>For example, OEO firms may offer their clients the option of how to execute trades (e.g., Volume Weighted Average Price, Percentage of Volume or Time). So long as the choice is made by the client, on their own initiative, without any recommendation provided by the OEO firm regarding which of these options, if any, a client should choose, we would consider such options acceptable.</p>
Subsection 3.3.8	Pre-entering of Orders	Pre-entering of orders is acceptable, assuming that the order is pre-entered solely by the client, on their own initiative, without any recommendation being provided by the OEO firm.
Subsection 3.3.9	Automatic Rebalancing Alerts & Tools	<p>Rebalancing Tools are generally acceptable provided that the OEO firm did not influence the client’s selection of their desired pre-determined levels / rebalancing instructions.</p> <p>OEO firms should be mindful of the risks and concerns raised by Rebalancing Tools.</p>
Subsection 3.3.10	Filtering Tools	Filtering Tools that merely sort/filter all securities the OEO firm has available for purchase and sale are not considered to be recommendations, so long as the client initiates (pulls) the sorting/filtering.
Subsection 3.3.11	New Issues	New Issues that are merely made available on an OEO firm’s website to be pulled by a client, without prompting or influence by the OEO firm, are not generally considered to be recommendations.
Subsection 3.3.12	Informative Tools	Informative Tools are generally acceptable, depending on the facts and circumstances. However, they may be considered recommendations if they could reasonably be expected to influence a person’s investment decision.
Clause (a)	Educational Tools	Educational Tools are generally acceptable, so long as their primary purpose is to educate, and not influence, clients.



Guidance Reference	Topic	Summary
Clause (b)	Research Reports	Research Reports that are merely made available on an OEO firm's website to be "pulled" by the client, without prompting or influence by the OEO firm, are not considered to be recommendations
Clause (c)	Multiple Fund Series	We do not consider it to be a recommendation when an OEO firm provides factual information to a client of the availability of a lower-cost series of a fund the client holds or is in the process of acquiring (e.g., the availability of Series D, or the equivalent PTF, where the client holds or is in the process of acquiring Series A of that fund).
Clause (d)	Portfolio Analyzer Tools	Portfolio Analyzer Tools are generally acceptable so long as they merely provide a breakdown of a client's <i>existing</i> holdings.
Clause (e)	Model Portfolio Tools	<p>Permitted Model Portfolios that:</p> <ul style="list-style-type: none"> <li>• are limited to class of investor, asset class, industry sector and/or time horizon</li> <li>• do not reference specific securities or issuers, and</li> <li>• are only made available on OEO firms' websites to be pulled by the client and are not pushed to a client(s)</li> </ul> <p>are not generally considered to be recommendations.</p>



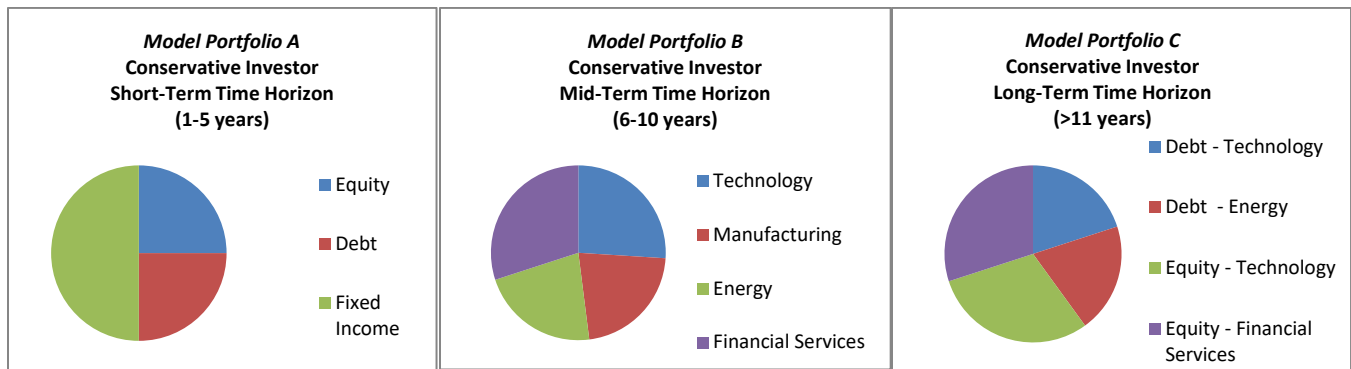


**Examples of Permitted Model Portfolios & Non-Permitted Model Portfolios**

In accordance with clause 3.3.12(e) of the Guidance, below are examples of Permitted Model Portfolios and Non-Permitted Model Portfolios.

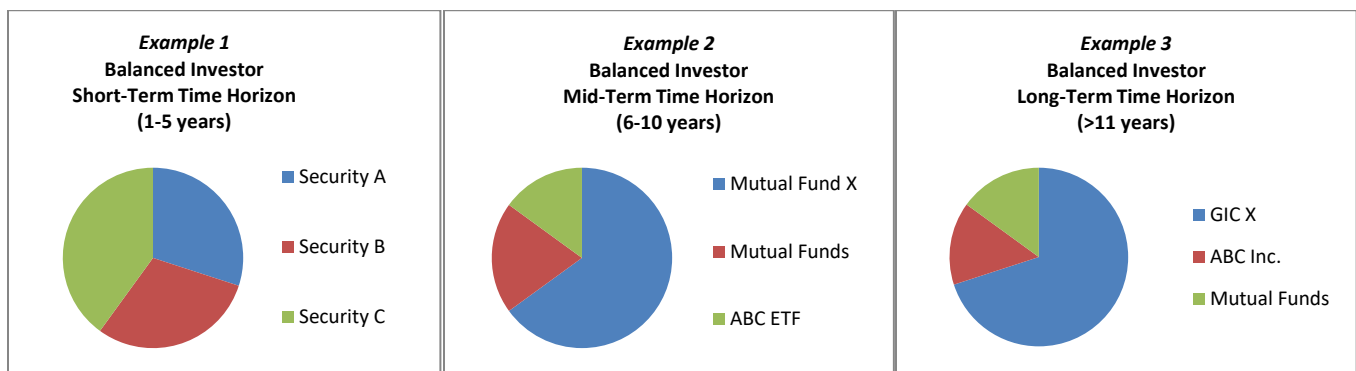
**A. Examples of Permitted Model Portfolios<sup>37</sup>**

Model Portfolio A<sup>38</sup> provides a suggested portfolio distribution based on Asset Class; Model Portfolio B provides a portfolio distribution by Industry Sector; and Model Portfolio C provides a combination of Asset Class and Industry Sector.



**B. Examples of Non-Permitted Model Portfolios**

We do not consider the model portfolios in Examples 1-3 to be acceptable because they each provide a distribution based on specific securities or issuers (i.e., Example 1 - Security A, B & C, Example 2 - Mutual Fund X and ABC ETF and Example 3 - GIC X & ABC Inc.).



<sup>37</sup> Links should be made available defining all applicable terms used in the Permitted Model Portfolios (e.g., “Conservative Investor”, “Equity”, “Debt”, “Fixed Income”, “Equity – Financial Services”, etc.).

<sup>38</sup> As discussed in clause 3.3.12(e), OEO firms may couple a Permitted Model Portfolio with a Filtering Tool. For example, in “Model Portfolio A”, the terms “Equity”, “Debt” and “Fixed Income” may be hyper-linked terms allowing clients to use the Filtering Tool to list all the specific securities offered by the OEO firm which it considers to be “Equity”, “Debt” and “Fixed Income”, respectively. In addition, the term “Model Portfolio A” itself could also be linked to identify the specific securities (such as ETFs, mutual funds or PTFs) offered by the OEO firm that are consistent with the distribution provided in Model Portfolio A.