

# IIROC NOTICE

## **Rules Notice Request for Comments**

Dealer Member Rules

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**12-0111**  
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## **Plain language rule re-write project: Clean up amendments**

### **Summary of the nature and purpose of the proposed Rule**

On June 29, 2011, the Board of Directors (“the Board”) of the Investment Industry Regulatory Organization of Canada (“IIROC”) approved the publication for comment of the proposed clean up amendments.

IIROC has undertaken a project to rewrite its rules in plain language. While the primary objective of this project is to develop a set of rules that is clear, concise and organized, without changing the rules themselves, we did identify a number of rules that also required substantive revisions.

To date, 7 of the 8 planned tranches of the proposed plain language rulebook have been published, namely:

- (1) 1000 series - "Interpretation and principles"
- (2) 2000 series - "Dealer Member organization and registration"
- (3) 3000 series; Part I - "Business conduct and client accounts"
- (4) 3000 series; Part II - "Dealing with clients"
- (5) 4000 series - "Financial and operational rules"
- (6) 5000 series - "Margin rules"
- (7) 7000 series - "Debt markets and Inter-dealer bond brokers"

The 6000 series (Market Integrity rules), the 8000 series (Consolidated Enforcement Rules), as well as parts of the 9000 series (procedural matters relating to the Consolidated Enforcement Rules), will be drafted separately and published at a later date.

The objective of the clean-up amendments is to account for all of the rule provisions which were not otherwise accounted for in one of the previously submitted series. IIROC staff conducted an overall review of the current rulebook to ensure that all existing rules are either:

- (a) included as part of the plain language rules; or
- (b) repealed.

In the course of that review IIROC staff determined that:

- o some definitions, that were originally to be included in the 1000 series, were better located in other rule series that had been previously submitted;
- o provisions from the 9000 series, which were not related to the consolidated enforcement rules had to be inserted; and
- o some provisions had been missed inadvertently.

Rule provisions that should have been included in one of the previously submitted tranches have been set out in Attachment A and B. The list of the repealed provisions has been included in Attachment A, as item number 44. ; the texts of all repealed provisions have been included in Attachment C.

In order to demonstrate that all current rule provisions have been accounted for, IIROC staff has prepared a black-lined consolidated table of concordance, attached as Attachment D. The table of concordance catalogues each existing rule provision along with its corresponding plain language rule number, if any. Where a current rule provision is proposed to be repealed, an explanation is provided. As part of the overall review of the current rulebook, IIROC staff noted that although some current provisions were redrafted and included in the plain language rules,

the reference to the section was missing or the provision was incorrectly referenced in the table of concordance submitted with each tranche. These changes have also been black-lined in the attached consolidated table of concordance.

Most of these clean up amendments are not substantive in nature, however, the following amendments have been marked as substantive:

- (a) the proposal to repeal Dealer Member Rule 5.12(a) dealing with the distribution of a Dealer Member's securities;
- (b) the proposal to repeal Dealer Member Rule 17.04 dealing with the requirement to report another Dealer Member who is unable to or refuses to fulfill its contracts; and
- (c) the proposal to repeal IIROC Dealer Member Rule 900.1, along with the proposal to amend IIROC Dealer Member Rule 900.2, dealing with commission fees on the exercise of rights.

These substantive proposals, along with a summary of the non-substantive amendments, are discussed below.

## **Issues and specific proposed amendments**

### ***Current rules***

Other than those proposed rules that have been noted as substantive, the proposed Rules do not create any new obligations for Dealer Members and have been drafted to clarify the existing Rules.

### ***Proposed rules***

In addition to the plain language rewrite of the existing requirements, the following three substantive amendments are proposed:

- *Rules relating to distribution of a Dealer Member's securities:* Current Dealer Member Rule 5.12(a) states that a Dealer Member may distribute its securities through a transaction such as a take-over bid or an amalgamation that will create a trading market in the securities if it publishes information equivalent to that in a prospectus under applicable securities legislation. IIROC staff proposes that this provision be repealed, as the requirements set out in this provision is more appropriately dealt with under securities legislation.
- *Rules relating to Dealer Member's contracts:* Current Dealer Member Rule 17.04(a) requires Dealer Members to fulfill their contractual obligations and report any other Dealer Members who refuse or are unable to fulfill their contractual obligations. IIROC staff proposes that this provision be repealed as matters relating to the performance of contractual obligations between Dealer Members is a business matter and it is not

necessary for IIROC to mandate that such contractual obligations must be fulfilled or that a failure to perform must be reported to IIROC.

- *Rule relating to service charge on rights:* Current Dealer Member Rule 900.1 sets out specific requirements with regard to the amount of commission that may be charged by a Dealer Member in connection with the exercise of rights to subscribe for shares. The provision states: (1) Dealer Members may only charge half of the amount that would be charged if the shares were acquired directly; (2) the amount charged by a Dealer member must be reduced by any amount paid by the issuing company to the Dealer Member; and (3) the conditions under which Dealer Members may waive the charges. IIROC staff proposes that Dealer Member Rule 900.1 be repealed as the provisions are no longer relevant.

Furthermore, current IIROC Dealer Member Rule 900.2 specifies that the commission paid in connection with the exercise of rights may only be paid by the Dealer Member to a Registered Representative or Investment Representative. This specific requirement is not provided for within the current IIROC Dealer Member rules with respect to commissions paid for other trades. However, the requirement set out in Dealer Member 900.2 is equally applicable to all trades. In light of the current interpretation of IIROC Dealer Member rules and securities legislation, IIROC staff therefore proposes that the provision be amended to generally apply to all trades. The proposed plain language Rule will state that a Dealer Member must not pay any commission fees, or other fees in connection with payments received from a client or issuer, to any person other than a Registered Representative or Investment Representative.

As previously noted, most of the clean-up amendments are non-substantive in nature. Many of the non-substantive amendments consist of simply adding definitions within the current rulebook that originally were to be included in the 1000 series; IIROC staff determined that it is more appropriate to include these definitions within a specific series of rules rather than the general definition section of the 1000 series. As a result, these definitions have been added to the text of the appropriate series, previously submitted.

The following are some of the key, non-substantive amendments made to each of the previously submitted series:

### ***1000 series - “Interpretation and principles”***

With respect to the 1000 series, IIROC staff has added the following definitions to proposed plain language rule 1201(2):

- *actively engaged in the business of a Dealer Member*
- *remuneration*
- *safekeeping or securities held for safekeeping*

### **2000 series - “Dealer Member organization and registration”**

With respect to the 2000 series, IIROC staff has:

- 1) added a new section, proposed plain language rule 2102, which consists of the following definitions:
  - *industry investor*
  - *public ownership*
  - *qualified independent underwriter;*
- 2) added the following definitions to proposed plain language rule 2652:
  - *continuing education course*
  - *continuing education participant*
  - *continuing education program;*
- 3) added a new condition within proposed plain language subsection 2655(2) dealing with compliance course continuing education program;
- 4) added the definition of national registration database administrator to proposed plain language rule 2702; and
- 5) re-numbered various provisions within the 2000 series as a result of the above noted changes.

### **3000 series – “Business Conduct”**

With respect to the 3000 series, IIROC staff has:

- 1) added the following two sections which were missing from the previously proposed Rule 3100:
  - Mutual fund sales practices, proposed plain language rule 3105, currently set out in Dealer Member Rule 29.12
  - Tied selling, proposed plain language rule 3106, currently set out in Dealer Member Rule 2400;
- 2) added a new section, proposed plain language rule 3502, which consists of the following definitions:
  - *distribution*
  - *distribution discussions*
  - *commencement of distribution;*
- 3) added a new paragraph within proposed plain language rule 3506 which relates to commission fees currently set out in Dealer Member Rule 900.2;

- 4) added a new section, proposed plain language rule 3602, which consists of the following definitions:
  - *advertisement or advertising*
  - *correspondence*
  - *sales literature*
  - *trading strategy*
- 5) added a new section, proposed plain language rule 3606, which consists of the following definitions:
  - *analyst*
  - *equity related security*
  - *investment banking services*
  - *research report;*
- 6) repealed the definition of supervisory analyst from current Rule 3400, as the term is no longer used; and
- 7) re-numbered various provisions within the 3000 series as a result of the above noted changes.

#### **4000 series - “Financial and operational rules”**

With respect to the 4000 series, IIROC staff have:

- 1) added provisions within proposed plain language rule 4136 to account for current Dealer Member Rule 20.28 and 20.29, not previously submitted with the 4000 series;
- 2) added the following new sections missing from the previously proposed 4000 series:
  - *Daily supervisory review of segregation reports*, proposed plain language rule 4332, currently set out in Dealer Member Rule 2600, statement 4, minimum required firm policies and procedures (5) and (7)
  - *Board of Directors review and designation*, proposed plain language rule 4466, currently set out in Dealer member Rule 2600, Statement 3, minimum required firm policies and procedures (1) and (2)
  - *Designated senior officer review*, proposed plain language rule 4467, currently set out in Dealer Member Rule 2600, statement 3, minimum required firm policies and procedures (3)-(5)
  - *Senior management prompt action*, proposed plain language rule 4468, currently set out in Dealer Member Rule 2600, statement 3, minimum required firm policies and procedures (6);

- 3) added new sections relating to formal valuation and fairness opinions to proposed plain language rule 4200
- 4) added the definition of “bulk segregation” to proposed plain language rule 4311;
- 5) added a new definition section, proposed plain language rule 4341, which consists of the following definitions:
  - *acceptable external securities location*
  - *acceptable internal securities location*
  - *set-off risk*
- 6) re-numbered various provisions within the 4000 series as a result of the above noted changes

### **5000 series - “Margin rules”**

Proposed plain language rule 5370, dealing with securities held in a registered trader’s account, was added to the 5000 series.

### **7000 series - “Debt markets and Inter-dealer bond brokers”**

With respect to the 7000 series, no new sections were added.

### **Other amendments**

As previously noted, the 6000 series (Market Integrity rules), the 8000 series (Consolidated Enforcement Rules), as well as parts of the 9000 series (procedural matters relating to the Consolidated Enforcement Rules), will be published at a later date. However, in the cleanup amendments IROC staff have added the following three proposed plain language rules relating to the 9000 series:

- 1) Proposed plain language rule 9500, alternate dispute resolution, currently set out in Dealer Member Rules 37.01-37.04;
- 2) Proposed plain language rule 9600, compliance fees, currently set out in Dealer Member Rule 16.07; and
- 3) Proposed plain language rule 9700, Canadian Investor Protection Fund, currently set out in Dealer Member Rule 41.

In addition to the above noted sections added to each of the series, previous incorrect references to certain sections within the various series were corrected. These changes are black-lined, for ease of reference, in the consolidated table of concordance.

Furthermore, some sections not previously accounted for, have been marked as repealed. Most of the provisions that were repealed are not substantive in nature; those that have been marked as “substantive” are discussed above.

IIROC staff has included a list of all repealed sections in Attachment A, as item number 44. This list includes those repealed sections discussed in one of the previously submitted tranches as well as those that are marked as “repealed” as part of the clean up amendments. The text of all repealed sections are set out in Attachment C.

The full text of the proposed clean up amendments are included in Attachments A and B.

### **Rule-making process**

The rules relating to the 1000 series, 2000 series, 3000 series, 4000 series, 5000 series and 7000 series have been published for public comments. Prior to publication these tranches, they were made available to all Dealer Members through a Dealer Members’ only website and their input was sought. A designated Compliance and Legal Section working group and/or the Financial Administrators Section also reviewed and provided comments on the proposed rules within the previously published tranches.

As a result of the above noted consultations, as well as independent review by IIROC staff, it was noted that a few provisions from the existing IIROC Dealer Member rules were not accounted for within the previously submitted series.

The clean up amendments will be implemented at the same time as the rest of the plain language rule rewrite project.

The proposed clean up amendments were approved for publication by the IIROC Board of Directors on June 29, 2011.

The text of proposed clean up amendments are set out in Attachment A and B. The text of the existing Dealer Member Rules to be repealed is set out in Attachment C. A consolidated table of concordance is included as Attachment D.

### **Issues and alternatives considered**

An alternative to the inclusion of the amendments being proposed was to leave the rules substantively as they were prior to the plain language rewrite. IIROC staff considered other pending projects and proposals as well as the extent of the potential, substantive changes identified in order to decide which of the substantive changes would be proposed as part of the plain language rule rewrite project. Those substantive changes which were originally identified as part of the plain language rule rewrite project, but which were ultimately excluded from the plain language rule rewrite project are being pursued as separate rulemaking projects.

The attached amendments are, for the most part, those that were omitted from one of the previously approved tranches. Other alternatives were not considered.

## **Proposed Rule classification**

Statements have been made elsewhere as to the nature and effects of the proposed Rules. The purposes of the proposed Rules are to:

- Ensure compliance with securities laws;
- Prevent fraudulent and manipulative acts and practices;
- Promote just and equitable principles of trade and emphasize the duty to act fairly, honestly and in good faith;
- Foster fair, equitable and ethical business standards and practices; and
- Promote the protection of investors.

IIROC staff propose that the proposed rules included as part of the clean up amendments should be rewritten to reflect actual IIROC expectations, to enhance the clarity of the rule and to ensure consistency with applicable securities legislation. The substantive amendments included are in addition to the plain language rewrite of the existing rule provisions. The Board has determined that the proposed substantive amendments are not contrary to the public interest.

Due to the extent and substantive nature of these proposed amendments, they have been classified as Public Comment Rule proposals.

## **Effects of proposed Rule on market structure, Dealer Members, non-members, competition and costs of compliance**

With proposed clean up amendments, Dealer Members will benefit from enhanced clarity and certainty in the proposed Rules.

The proposed clean up amendments will not have any significant effects on Dealer Members or non-Dealer Members, market structure or competition. Furthermore, it is not expected that there will be any significant, increased costs of compliance as a result of the proposed Rules.

The proposed clean up amendments do not impose any burden or constraint on competition or innovation that is not necessary or appropriate in the furtherance of IIROC's regulatory objectives. The proposed Rules do not impose costs or restrictions on the activities of market participants that are disproportionate to the goals of the regulatory objectives sought to be realized.

## **Technological implications and implementation plan**

There should not be significant technological implications for Dealer Members as a result of the proposed amendments. Proposed rules set out within the clean up amendments will be implemented at the same time as the rest of the plain language rules.

## **Request for public comment**

Comments are sought on the proposed amendments. Comments should be made in writing. Two copies of each comment letter should be delivered within 90 days of the publication of this notice. One copy should be addressed to the attention of:

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A second copy should be addressed to the attention of:

Manager of Market Regulation  
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19th Floor, Box 55  
Toronto, Ontario  
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[marketregulation@osc.gov.on.ca](mailto:marketregulation@osc.gov.on.ca)

Those submitting comment letters should be aware that a copy of their comment letter will be made publicly available on the IIROC website ([www.iiroc.ca](http://www.iiroc.ca) under the heading “IIROC Rulebook - Dealer Member Rules - Policy Proposals and Comment Letters Received”).

Questions may be referred to:

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## **Attachments**

- [Attachment A](#) - Text of proposed clean up amendments
- [Attachment B](#) - Black-lined text of the proposed clean up amendments
- [Attachment C](#) - Text of relevant provisions of existing IIROC Dealer Member Rules
- [Attachment D](#) - Consolidated table of concordance (black-lined)