

IIROC NOTICE

Rules Notice
Request for Comment
Dealer Member Rules and UMIR

Please distribute internally to:
Legal and Compliance
Operations
Senior Management

Comments Due By: May 23, 2018

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Request for Comment – Enforcement Alternative Forms of Disciplinary Action

Executive Summary

As part of IIROC's Three-Year Strategic Plan, IIROC adopted an objective to expand our portfolio of Enforcement Options to help us address wrongdoing in a fair and proportionate manner in order to inspire confidence and deter wrongdoing by having and using robust and appropriate tools. To further this objective, Enforcement Staff are considering two proposals to provide for alternative forms of disciplinary action. The proposals would allow for more tailored enforcement responses and ensure enforcement actions are fair and proportionate to the particular circumstances of cases under investigation. In addition, Staff believe these proposals will create operational and procedural efficiencies by promoting more timely resolution of certain cases while also freeing up resources needed for larger and more complex cases.

1. **A new Minor Contravention Program (MCP)** under which an Approved Person or Dealer Member would agree to the imposition of a sanction for rule contraventions that are deemed minor. The MCP would provide a more efficient means to resolve cases that cannot be adequately addressed by way of a Cautionary Letter but do not warrant formal disciplinary action.

2. **The use of Early Resolution Offers** to conclude settlement agreements at an earlier point in the enforcement process to promote the efficient resolution of cases, increase the application of the IIROC Staff Policy Statement on Credit for Cooperation,¹ and encourage firms to take remedial measures and address investor harm through voluntary acts of compensation.

In developing these proposals, Staff has reviewed its practices and comparable programs and approaches adopted by securities and other regulatory bodies. By providing the option for more tailored responses, Staff believes these proposals will assist in deterring wrongdoing in a fair and proportionate manner.

IIROC stakeholders are encouraged to review and comment on the proposals. To supplement and engage a broader representation of stakeholders, IIROC will consult directly with Canadian investors to get their views on the proposed alternative forms of disciplinary action. In our current Strategic Plan, IIROC committed to actively consulting with retail investors on key policy issues. To do so, we established an online pool of 10,000 Canadian investors, from which we would consult on key proposals to better understand their needs, experiences and perceptions. We will draw on a subset of this pool to solicit input on this proposal from retail investors coast to coast.

Following the close of the 90-day comment period, Staff intends to draft a consolidated response to the written comments received and, where appropriate, revise the proposals to address the comments received. We also intend to publish the results of the investor survey. Staff may also consider inviting those who submit comments to a meeting with Staff to discuss issues related to the adoption and implementation of the proposals.

Staff anticipates that implementation of the MCP will require amendments to the IIROC Consolidated Enforcement, Examination and Approval Rules (the Consolidated Rules). Any proposed amendments will be published for further public comment before implementation.

How to Submit Comments

Comments should be made in writing and delivered by May 23, 2018 to:

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Commentators should be aware that a copy of their comment letter will be made publicly available on the IIROC website at www.iiroc.ca.

¹IIROC Staff Policy Statements, Credit for Cooperation,
http://www.iiroc.ca/industry/enforcement/Documents/IIROCStaffPolicyStatements_en.pdf

Table of Contents

1. MINOR CONTRAVENTION PROGRAM	3
1.1 Background	3
1.2 Purpose	4
1.3 Process and Key Features.....	4
1.4 Principles and Factors for issuing a MCP Notice.....	4
1.5 Eligibility	5
1.6 Types of Contraventions	5
2. EARLY RESOLUTION OFFERS	6
2.1 Background	6
2.2 Purpose	6
2.3 Process and Key Features.....	6
2.4 Criteria for making an Early Resolution Offer	7
3. COMMENTS REQUESTED	7
3.1 Minor Contravention Program	7
3.2 Early Resolution Offers	7
3.3 Other Considerations	8
Schedule A – Comparable Regulatory Programs	1

1. MINOR CONTRAVENTION PROGRAM

1.1 Background

Currently, after an investigation is completed, Staff can close a matter with no action, issue a Cautionary Letter, or initiate formal disciplinary proceedings.

Where there is clear and convincing evidence to support an allegation of a contravention of IIROC requirements, Staff generally pursue formal disciplinary proceedings, which must be resolved through either a settlement agreement or a full disciplinary hearing before an IIROC hearing panel. Pursuing formal disciplinary proceedings requires a minimum expenditure of resources and costs regardless of the seriousness and scope of the contravention and the specific circumstances of the conduct.

A Cautionary Letter represents Staff’s opinion that an IIROC requirement may have been contravened and outlines Staff’s concerns about the conduct. A Cautionary Letter has limited value. It provides Staff with historical information about a particular Approved Person or Dealer Member and it may be a factor considered in commencing a future investigation or prosecution. However, a Cautionary Letter has no legal effect and does not constitute a finding that an IIROC requirement has been contravened. The deterrent effect of a Cautionary Letter is minimal and it does not materially enhance confidence in IIROC’s enforcement efforts.

In Staff’s view, there are cases that require a more serious regulatory response than a Cautionary Letter, but do not warrant the initiation of formal disciplinary proceedings, which are resource intensive. An option, other than a settlement or contested hearing, will highlight the importance of progressive discipline and ensure enforcement outcomes are proportionate yet meaningful.

Staff believes the MCP would provide the necessary flexibility to achieve a more efficient and effective Enforcement response. In developing the proposal, Staff have considered analogous programs adopted by other regulators including the United States (FINRA), Australia (ASX) and Quebec (the Bourse).²

1.2 Purpose

The purpose of the MCP is to provide for the imposition of a meaningful sanction for a minor contravention of IIROC requirements. The MCP would provide additional flexibility in handling cases, allowing for a regulatory response that is proportionate to a minor case, in terms of both resources and costs expended and the consequences to the Approved Person or Dealer Member. The program would address cases that warrant a more meaningful regulatory response than a Cautionary Letter, but do not warrant the increased expenditure of time, resources and costs associated with proceeding with formal disciplinary action.

1.3 Process and Key Features

In appropriate cases, based on the criteria set out below, Staff would issue a Minor Contravention Program Notice (the MCP Notice) to an Approved Person or Dealer Member in lieu of commencing a disciplinary proceeding by way of a Notice of Hearing and Statement of Allegations. The MCP Notice would specify the alleged IIROC requirement contravened, the facts relied on to support the allegation and the fine sought.

The sanction would be fixed at \$2,500 per contravention for an Approved Person and \$5,000 for a Dealer Member.

An Approved Person or Dealer Member receiving an MCP Notice would have a prescribed time within which to accept the terms of the MCP Notice and make payment of the fine.

By agreeing to the MCP Notice, the Approved Person or Dealer Member would admit to contravening the specified IIROC requirement. Staff would not be permitted to initiate a disciplinary proceeding based on the admitted contravention in the MCP Notice. The admission would not constitute a formal disciplinary record and therefore an Approved Person or Dealer Member would not be required to disclose it as disciplinary history, for instance on an individual's application for registration. However, Staff could rely on the admission at a future disciplinary proceeding against the Approved Person or Dealer Member.

On a quarterly basis, Staff would issue a public notice setting out all matters resolved by way of MCP Notice, specifying the contravention and a summary of the facts set out in the MCP Notice without identifying the Approved Person or Dealer Member. IIROC would promptly notify the Recognizing Regulators of all MCP Notices.

Staff would retain the ability to commence a disciplinary proceeding pursuant to Consolidated Rule 8200 if the Approved Person or Dealer Member chose not to agree with a MCP Notice.

1.4 Principles and Factors for issuing a MCP Notice

The cases resolved by way of MCP Notice would be at Staff's discretion based on principles consistent with those set out in the IIROC Sanction Guidelines. The objective of the MCP is to discourage future misconduct by the individual or firm in question by imposing a sanction that is

²See Schedule A, Comparable Regulatory Programs

proportionate to the conduct at issue and appropriate for the individual or firm who engaged in the misconduct.

1.5 Eligibility

The MCP would be available to both Approved Persons and Dealer Members. However, individuals with prior disciplinary records will likely be disqualified from being considered for a MCP Notice. Factors to consider will include the age and relevance of the prior disciplinary record.

Staff believes that the MCP would be more applicable and relevant to cases involving individual misconduct. It is also not anticipated that the MCP would be offered more than once to a particular individual.

1.6 Types of Contraventions

MCP Notices will be issued for contraventions of IIROC requirements that are isolated and result in limited or no harm to the public and the capital markets.

Staff will consider the following criteria in making a determination about whether a contravention of IIROC requirements may be resolved by way of a MCP Notice:

1. the contravention is technical;
2. the contravention is an isolated incident;
3. the contravention resulted in:
 - limited or no harm to clients or other market participants;
 - limited or no harm to market integrity or the reputation of the marketplace;
 - limited or no benefit to the firm or individual engaged in the conduct or any related parties; and
4. the conduct was unintentional or inadvertent.

If the above criteria are met, Staff will also consider additional factors such as whether:

1. the conduct is admitted;
2. the conduct is self-reported;
3. the conduct has been the subject of internal discipline by the Dealer Member;
4. corrective or remedial measures were taken in response to the contravention;
5. there have been voluntary acts of compensation, including voluntary disgorgement of commissions, profits or benefits.

The nature of the contravention, applying the criteria set out above, will determine whether a matter may be resolved by way of the MCP. Self-reporting, an admission of wrongdoing and remedial or compensation acts are additional factors to be considered. For example, the following factors would generally result in Staff pursuing formal disciplinary proceeding, regardless of the post-conduct steps taken by the Approved Person or Dealer Member:

1. the conduct is deliberate;
2. a prior disciplinary history;
3. significant harm to investors or the reputation of the capital markets;
4. the seriousness and complexity of the issues involved in the conduct; and
5. the conduct relates to whether a firm fully and properly supervised securities-related activity.

2. EARLY RESOLUTION OFFERS

2.1 Background

Currently, Enforcement cases may be resolved by entering into a settlement agreement that is subject to approval by an IROC hearing panel. A settlement agreement is typically reached after a full investigation is completed and extensive negotiations between Staff and the Respondent have taken place. Staff have always encouraged early settlement of cases and have adopted measures to facilitate timely resolution, including:

1. **the Staff Policy Statement on Credit for Cooperation**, which provides for the imposition of a reduced sanction if a respondent demonstrates proactive and exceptional cooperation; and
2. **the Enforcement Mediation Program**, which provides for the use of an independent third-party mediator to facilitate the settlement of proceedings or proposed proceedings.³

Despite the implementation of these measures, the settlement process has not been significantly impacted. While there are often valid reasons for delayed or protracted negotiation in certain circumstances, Staff believes there is an opportunity to achieve early resolution in more cases and that early resolution would benefit both parties involved, protect investors and deter wrongdoing. For example, early resolution would be desirable in cases involving discrete violations where there are no on-going related civil actions, the misconduct has been acknowledged and compensation or remedial measures taken.

2.2 Purpose

Early Resolution Offers will promote the timely resolution of cases, increase the application of the Staff Policy Statement on Credit for Cooperation and encourage firms to implement timely compensation and remedial measures. An Early Resolution Offer will constitute Staff's best offer by granting substantial credit in the determination of the fine and costs sought in exchange for entering into a settlement agreement.

2.3 Process and Key Features

In cases that meet the criteria set out below, Staff will make formal offers of settlement at an earlier point in time in the enforcement process. For example, in cases where the relevant facts can be established at, or shortly after, the commencement of the formal investigation. In those circumstances, conducting a further, more extensive investigation can result in a substantial use of regulatory resources without significantly advancing Staff's understanding of the relevant facts.

While an Early Resolution Offer may be subject to negotiation between Staff and the respondent, the time for acceptance of the offer would be strictly time-limited. If an Early Resolution Offer is rejected or the time for acceptance expires, the matter would proceed through the normal enforcement process. Any subsequent settlement negotiations would take into account the terms offered pursuant to the Early Resolution Offer.

³Enforcement Mediation Program, <http://www.iroc.ca/industry/enforcement/Pages/mediationprogram.aspx>

Staff intends to make transparent to the respondent, the public and other stakeholders why and how credit was granted pursuant to an Early Resolution Offer.

A settlement agreement reached through an Early Resolution Offer would still be subject to acceptance by an IIROC hearing panel pursuant to Consolidated Rules 8200 and 8400. The adoption of this proposal does not entail any change or amendments to the Consolidated Rules or the practices and procedures currently in place with respect to disciplinary proceedings.

2.4 Criteria for making an Early Resolution Offer

Staff will consider the application of the following criteria in determining whether to make an Early Resolution Offer:

1. Staff reasonably believe that the extent, scope and harm of the misconduct, non-compliance, or regulatory breach, has been determined;
2. the extent to which the subject has demonstrated proactive and exceptional cooperation in accordance with Staff's Policy Statement on Credit for Cooperation;
3. the extent to which the non-compliance which is the subject matter of the case has been remedied or will be remedied as part of the settlement;
4. whether the respondent has or agrees to disgorge the amounts obtained or loss avoided as a result of the contravention(s);
5. whether the respondent has compensated or agrees to compensate any client(s);
6. in the case of individuals, whether they have been internally disciplined; and
7. whether the respondent, through counsel, an agent or otherwise, has expressed a willingness to resolve the matter in a timely manner.

3. COMMENTS REQUESTED

IIROC Staff welcome any comments on the two proposed programs. Staff is particularly interested in comments in response to the following questions.

3.1 Minor Contravention Program

1. Do you believe that the proposed MCP would be useful?
2. Should a Dealer Member be eligible for the MCP?
3. What aspects of the proposed MCP, if any, should be public?
4. What legal or regulatory effect should acceptance of a MCP Notice have?
5. Do you agree that the sanction should be a fixed amount?
6. Do you agree with the quantum of the proposed sanctions?

3.2 Early Resolution Offers

1. Do you believe that the Early Resolution Offers initiative is necessary? Will it meet its objective?
2. How can Staff best demonstrate the credit given for accepting an Early Resolution Offer?

3. To what extent should Staff factor internal discipline into the decision to make an Early Resolution Offer?

3.3 Other Considerations

1. Are there other initiatives or programs that Staff should consider in order to provide more flexibility and options in addressing breaches of regulatory requirements in a fair and proportionate manner?

Schedule A – Comparable Regulatory Programs

REGULATOR	DESIGNATED RULES eligible for program	SANCTIONS	PROCESS	ADMISSION	PUBLIC REPORTING	RULE
IIROC Proposal <ul style="list-style-type: none"> ▪ Minor Contravention Program 	No. Staff discretion to proceed taking into account severity of contravention.	Monetary – fixed at \$2,500 for individuals and \$5,000 for Dealer Members.	Voluntary acceptance, otherwise routed through normal disciplinary process.	Yes	Yes, on anonymous basis Report to CSA No public disciplinary record	Yes
Financial Industry Regulatory Authority (FINRA) <ul style="list-style-type: none"> ▪ Minor Rules Violation Program (since 1993) 	Yes	Monetary – up to \$2,500 on member firm or associated person. Staff determines amount proposed up to maximum.	Staff provides letter describing contravention, rule, and sanction(s) to be imposed, and effective date. If letter accepted, it is submitted to Office of Disciplinary Affairs, which can also refer to National Adjudicatory Council. If accepted by one of those bodies, becomes final decision; if rejected, normal disciplinary process but cannot be used as evidence in that process.	Yes	No Reported to SEC No public disciplinary record	Yes
Australian Stock Exchange (ASX) <ul style="list-style-type: none"> ▪ Notification of Alleged Minor Infringements 	No, discretion to proceed by way of Alleged Minor Infringement Notice for any ASX rule.	Monetary penalty and/or non-monetary sanctions	Staff can decide to proceed by way of Minor Infringement Notice. Regulated person may comply with Notice by paying penalty or agreeing to comply with non-monetary sanctions in manner acceptable to ASX. If Notice is complied with not regarded as having admitted contravention or having contravened rule specified.	No	Yes, on anonymous basis (Quarterly publication of all enforcement activities, including Minor Infringement Notices)	Yes

Schedule A – Comparable Regulatory Programs

REGULATOR	DESIGNATED RULES eligible for program	SANCTIONS	PROCESS	ADMISSION	PUBLIC REPORTING	RULE
			If non-compliance with Notice within period set out for compliance, can issue Enforcement Notice and proceed before a Tribunal.			
Bourse de Montreal (MX) <ul style="list-style-type: none"> ▪ Fines for Minor Violations (since May 2017) 	Yes. 7 categories of eligible infractions deemed minor (e.g. position limits, inaccurate reporting of derivatives positions)	Predetermined fine grid for each of the 7 rules to a max of \$5,000 for some rules (escalating fines for each violation, then discipline complaint).	<p>VP of Regulatory Division serves a notice of minor violation, outlining specifics of violation and the amount of fine.</p> <p>Regulated person has 20 days to provide a response or ask to proceed before disciplinary committee. If no election or response within time limit, deemed to have agreed to pay fine and relinquished rights to a hearing.</p>	Yes However, provides a process to challenge the notice of minor violation and appeal.	Yes, on anonymous basis	Yes
ICE Futures Canada <ul style="list-style-type: none"> ▪ Administrative Penalty Provisions (since January 2017) 	Yes	Cease-and-desist instructions Fine of up to \$5,000 per violation	<p>Staff issues Administrative Penalty Letter as alternative to regular disciplinary route (Originating Notice), setting out particulars and sanctions. If no appeal is filed within 10 days, sanctions take effect and fine is due immediately.</p> <p>Regulated person may file appeal within 10 days and hearing is scheduled within 30 days. Within 10 days of appeal hearing, a decision is rendered either upholding,</p>	Yes, but process for challenging.	No	Yes

Schedule A – Comparable Regulatory Programs

REGULATOR	DESIGNATED RULES eligible for program	SANCTIONS	PROCESS	ADMISSION	PUBLIC REPORTING	RULE
			varying or dismissing penalty imposed. No further appeals permitted.			
Australian Securities and Investments Commission (ASIC) <ul style="list-style-type: none"> ▪ Infringement Notices* <p>*Least comparable as the ASIC can proceed by way of criminal proceedings, civil actions, and the Infringement Notice procedure is largely akin to a full administrative tribunal hearing process.</p>	Applicable to less serious breaches of the continuous disclosure obligations under Australian securities law	Various – more akin to remedies available under Consolidated Rule 8209 and provincial securities acts	<p>Recommendation to issue Infringement Notice made to an ASIC delegate (not involved in investigation and reviewing for first time).</p> <p>If delegate believes there is a breach, hearing held which takes into account submissions and evidence and decides whether to issue Infringement Notice.</p> <p>If Infringement Notice is issued, Regulated person may comply, seek extension of time, seek to have it withdrawn or choose not to comply.</p> <p>If the notice is not complied with, ASIC may start a civil action. If withdrawn, ASIC may proceed as it sees fit.</p>	Yes	Yes	Yes