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Capital Markets Modernization Taskforce

September 7, 2020

**Re: Consultation — Modernizing Ontario’s Capital Markets**

Thank you for the opportunity to comment on the issues raised and proposals advanced in your Consultation Report. This submission is from the current and incoming Independent Directors on the IIROC Board.

We appreciate the creativity and imagination with which the Taskforce has approached its mandate. We agree with the Ontario government and the Taskforce that a vibrant economy needs vibrant capital markets, driven by innovation, competition and diversity, and with the need for modernized capital markets in a post-pandemic economy that will assist businesses to raise capital, incubate innovative companies, invigorate large and small intermediaries, and protect investors.

Our submission focuses on issues relating to the governance and structure of self-regulatory organizations (**SROs**), and specifically on the proposals for SRO governance as they apply to IIROC. As Independent Directors of IIROC, we feel that we are in a unique position to provide information about IIROC’s governance practices and how we believe these proposals would affect IIROC.

In addition to preparing this submission, we retained Hansell LLP to provide an opinion on the governance proposals set out in Section 2.1.3 of the Report as they relate to SROs generally and IIROC specifically. The Hansell opinion is attached and we refer to it throughout our submission.

We understand that IIROC management is preparing a separate submission that addresses other issues raised in the Report.

IIROC receives its authority under a legislative framework that each provincial and territorial government has adopted, and it is to those governments that we owe our ultimate policy accountability. Overall, we believe that IIROC’s governance, including its direct oversight by the Ontario Securities Commission (**OSC**) and the other members of the Canadian Securities Administrators (**CSA**), helps ensure that IIROC acts in the public interest and fulfills its mandate to set high-quality regulatory and investment industry standards, protect investors and strengthen market integrity while maintaining efficient and competitive capital markets.

We support many of the proposals, although we believe that some are not required given current practice and that others could adversely affect IIROC’s effectiveness as an SRO.

Our detailed submissions on the proposals are as follows:

1. *SROs to submit an annual business plan covering all activities conducted in Ontario to the OSC for approval.*

We believe that this formal change is not required given current practice.

IIROC currently submits a substantial amount of information to the OSC/CSA on an annual, quarterly and *ad hoc* basis that provides significant transparency into IIROC's plans prior to publication.

In particular, IIROC prepares an annual statement of priorities under its strategic plan that management provides to the OSC and other CSA members in advance, and publishes it on its website, although without the formal approval of the OSC/CSA.

We agree with the Hansell opinion that business planning is an iterative process that requires significant ongoing alignment between the Board and management. Requiring OSC – and potentially CSA<sup>1</sup> – approval of an annual business plan would interfere with this process and with the Board and management's ability to adjust the plan as circumstances dictate in the face of a rapidly changing environment.

2. *OSC veto on significant publications*

We believe that this formal change is not required given current practice.

While not formally part of the Joint Rule Review Protocol for IIROC, the current practice is that IIROC pre-clears major public comment proposals with the CSA Oversight Committee and the appropriate CSA staff. After publication for comment, the OSC currently has a veto over any IIROC rule changes.

We agree with the Hansell opinion that an OSC veto on significant publications that are not rule-related would risk undermining IIROC's role and could compromise IIROC's ability to consult with stakeholders by delaying or preventing the publication of discussion papers concerning new policy concepts or issues that may be controversial in the industry.

3. *OSC veto on key appointments, including the Chair and the President and CEO*

We do not support this proposal.

We agree with the Hansell opinion that an OSC/CSA veto on the appointment of the Chair and CEO would take critical authority from the Board and create the risk that the individuals

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<sup>1</sup> We note in our concluding remarks that any amendments to the Recognition Order made by the OSC may be mirrored by the other CSA members.

in those positions will feel an accountability to the OSC that will compromise the role of the Board.

4. *Term limits for key appointments*

This proposal reflects IIROC's current practice as it relates to Director terms. We do not support this proposal as it relates to the Chair and the CEO.

We note that IIROC has always had term limits for its Directors (a maximum of four two-year terms<sup>2</sup>), and we believe that this approach strikes an appropriate balance between continuity and renewal on the IIROC Board.

We also note, as detailed in the Hansell opinion, that the Board establishes contractual terms for the IIROC CEO that ensure that the Board engages in a periodic review of the CEO's appointment (over and above the annual performance assessment).

We do not believe that it is appropriate for the OSC/CSA to constrain either the duration of a specific CEO's appointment or the number of times that contract may be renewed. We believe that term limits for the position of Board Chair and CEO create the risk that an individual will reach their term limit at a time when continuity is critical for the organization.

Finally, we do not believe that it would be appropriate to have term limits for other IIROC executives, as this is a matter that ought to be principally the CEO's responsibility and accountability.

5. *SROs should be required in their recognition orders to have directors with investor protection experience.*

This proposal is consistent with the approach that IIROC's Corporate Governance Committee currently takes to Director recruitment.

IIROC announced in February 2020 that the Corporate Governance Committee had formally amended the criteria used to identify candidates for Independent Directors to include direct experience with consumer and retail investor issues. IIROC's close attention to retail investors' interests is a driving force behind the Board's desire to bring direct experience in this area to the Board's composition. Moreover, we agree with the Hansell opinion that such a criterion is effective and meaningful as a recruitment objective, but if elevated to a regulatory requirement may be too vague to be of much practical value. Some categories of investor protection experience are unlikely to be controversial, however, and the Board will

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<sup>2</sup> A Director may serve more than eight years in total only if their first term was less than two years – see section 5.3(2) of IIROC's General By-law.

continue to build on its progress to recruit Independent Directors with hands-on consumer or seniors' experience, and looks forward to enhancing this expertise.<sup>3</sup>

IIROC has had, and will have, Directors with direct experience in retail investor protection issues, including:

- Lucie Tedesco (2018 to 2019): Ms. Tedesco was the Commissioner of the Financial Consumer Agency of Canada (FCAC) when she joined the IIROC Board. In her role at FCAC, Ms. Tedesco ensured that federally regulated entities complied with consumer protection measures and helped advance the financial literacy of Canadians. Ms. Tedesco resigned from the IIROC Board when she took her current position at McCarthy Tétrault.
- Malcolm Heins (nominated for election as an Independent Director in September 2020): Mr. Heins is a lawyer and a former insurance industry executive and CEO of the Law Society of Ontario. In 2015, Mr. Heins was appointed to Chair the Ontario Expert Committee to Consider Policy Alternatives for the Regulation of Financial Advisory and Financial Planning Services. He is a former member of the OSC's Investor Advisory Panel (IAP) and sits on various boards, including Legal Aid Ontario. Over his career and in particular in his capacity as a regulator, Chair of the Expert Committee and a member of the IAP, Mr. Heins has been an advocate for the public interest and consumer protection.
- Laura Tamblyn Watts (nominated for election as an Independent Director in September 2020): Ms. Tamblyn Watts is a lawyer, public speaker and advocate sought for her commentary on elder law issues. She is among Canada's most resounding voices for seniors and vulnerable investors, in her role as President and CEO of seniors' advocacy and policy group CanAge, and is a member of the OSC's Taskforce on Seniors. Ms. Tamblyn Watts is CARP's former Chief Public Policy Officer and a former board member of the Ombudsman for Banking Services and Investments.

Over and above these specific nominations, our experience of the dynamics of IIROC Board meetings is that *all* Directors – whether Independent or from the industry – take very seriously IIROC's central investor protection mandate and mission. It would be a negative outcome if stakeholders believed that only those Directors with specific investor protection experience had this focus on the Board.

6. *The compensation and incentive structure applicable to SRO executives should be linked to the delivery of the public interest and policy mandate delegated to these bodies.*

This proposal reflects IIROC's current practice.

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<sup>3</sup> IIROC confirms experience with investor issues a critical skill for Board succession, February 24, 2020.

The IIROC Board, through its Human Resources & Pension Committee, is responsible for determining the annual performance objectives for the CEO, as well as his or her compensation. The Board is also responsible for approving the overall compensation structure for IIROC staff. The CEO is, in turn, responsible for determining the annual performance objectives and compensation for the most senior IIROC executives.

We confirm that IIROC's delivery of its public interest and policy mandate has always been a principal annual performance objective for the current CEO, and a significant component of his annual compensation. We also confirm that the CEO takes the same approach for senior IIROC executives.

Finally, we agree with the Hansell opinion that giving the authority to determine the compensation and incentive structure for the CEO and other senior executives to a body other than the Board will greatly diminish the Board's ability to oversee management effectively.<sup>4</sup>

7. *Up to half of the directors should be appointed jointly by all CSA regulators and a mechanism should be put in place to resolve CSA disagreements on the choice of appointees in a timely manner.*

We do not support this proposal.

We agree with the Hansell opinion that Board planning is a challenging and important process in which multiple requirements and criteria need to be considered and balanced, and that this role for the CSA does not reflect the importance of and challenges associated with a well-constructed board and with effective succession planning.

The IIROC Board engages in a self-assessment and peer assessment every two years. If the CSA appointees were not subject to peer assessment, it would adversely affect Board dynamics and the ability of the Chair to address individual Board members' performance to ensure the optimal functioning of the Board.

8. *Continue ensuring the independence of independent directors by having requirements similar to those applicable to an independent director of a public company, including a cooling-off period between working for a member firm and becoming an independent director.*

This proposal reflects IIROC's current practice.

IIROC's General By-law defines in detail the qualifications for Independent Directors to ensure that Independent Directors have no connection to IIROC-regulated firms or IIROC itself.

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<sup>4</sup> We note that the Taskforce Report recommends against binding shareholder "say on pay" votes "because of the importance of preserving the board of directors' decision-making processes".

The Corporate Governance Committee Charter provides that the Committee has the following responsibilities for director recruitment:

Broadly consult to identify through its own efforts or by retaining an independent search firm and recommend to the Board, in accordance with IIROC's By-law, qualified candidates to be elected to the Board and as are necessary to fill vacancies and newly created directorships and determine the eligibility of any proposed nominees based on the By-law criteria and a desire to ensure that the Board, as a whole, reflects the skills, experience, expertise and judgement necessary to effectively oversee the regulatory and other operations of IIROC.

The Committee will consider all relevant factors in nominating directors to ensure that the composition of the Board: (a) complies with the requirements of IIROC's by-laws, (b) otherwise reflects, in the judgement of the Committee, the appropriate balance of interests and perspectives of IIROC's Members and stakeholders, and (c) addresses, in the judgement of the Committee, all potential conflicts of interest.

Without limiting the generality of the foregoing, the Committee will consider, for each potential director:

- (i) the business interests of the candidate or entities with which the candidate is associated;
- (ii) ownership interests in Members held by entities with which the candidate is associated;
- (iii) the extent of overlap and/or integration of the boards and/or management between Members and entities with which the candidate is associated (for example, consideration of the extent to which there are common managers and/or directors as between the candidate's firms and an ATS);
- (iv) contractual relationships between Members or IIROC and the candidate or entities with which the candidate is associated; and
- (v) in the case of Independent Directors, whether the candidate would have met the test to be an Independent Director (as defined in the By-law) for a period of at least one year prior to commencement of the candidate's term of office.

The final element incorporates the cooling-off period proposed in the Report. IIROC has observed this cooling-off period for Independent Director nominations with just one exception.<sup>5</sup>

9. *The number of independent directors should be higher than the number of directors from member firms. The actual number would have to be determined by function of how many directors would be appointed by the CSA.*

Under IIROC's Recognition Order, a majority of directors are already independent from industry: the CEO plus seven non-industry directors, as compared to seven directors from member firms.

To ensure that a majority of directors are independent from both IIROC management and member firms, the Recognition Order and IIROC's constating documents could be revised to require nine non-industry, non-IIROC directors, for a total of 17 Directors. We would not object to such a revision.

10. *The SRO Chair would be required to be an independent director.*

We support this proposal, modified by the recommendation in the Hansell opinion that the requirement should be subject to the public company practice that exceptions may be made in extraordinary circumstances.<sup>6</sup>

We intend to implement this requirement when IIROC's current Chair, who is a Dealer Director, reaches his term limit in 2022. We believe it is important for Board continuity that the current Chair remain in the role until then, and that he have the opportunity until then to work over that period with the Independent Director who will succeed him as Chair.

11. *Creation of an ombudsperson service to address any complaints that SRO member firms may have about services received from their respective SRO.*

We do not support this proposal.

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<sup>5</sup> Marianne Harris, who was then the Chair of the Board and a Dealer Director, retired from the industry in 2013. The Board, on the recommendation of the Corporate Governance Committee, appointed Ms. Harris as an Independent Director. The Corporate Governance Committee and the Board determined that it was appropriate to waive the cooling-off period for Ms. Harris in these specific circumstances, given the importance of continuity in the Board Chair position at the time.

<sup>6</sup> We also observe that there are trade-offs with respect to the independence of the Chair from industry. While such independence may minimize the risk of an appearance of bias on the one hand, on the other, a Chair from industry will have the knowledge, experience, and concern for the industry's reputation for fair dealing that motivate self-regulation in the first place.

We agree with the Hansell opinion that it is not apparent what problem the proposed ombudsperson is intended to address, and that layering an ombudsperson on to the existing OSC (and CSA) review power will create unnecessary jurisdictional ambiguity.

*12. Move to a single SRO that covers all advisory firms, including investment dealers, mutual fund dealers, portfolio managers, exempt market dealers and scholarship plan dealers.*

We agree with the Report that “[g]iven the evolution of the industry, having two separate SROs to regulate investment dealers and mutual fund dealers is outdated and is confusing to investors.”

We therefore support IIROC management’s proposal to bring together IIROC and the Mutual Fund Dealers Association (**MFDA**) as divisions of a consolidated SRO as an important first step.<sup>7</sup> We agree that the management proposal can be achieved without disrupting the existing rule framework, business models or regulatory fee structures. It would immediately offer firms flexibility in how to structure their operations, reduce regulatory burden for a broad range of market participants and enhance the regulatory and economic ecosystem. At the same time, consolidation would offer an improved investor experience and enhanced investor protection.

From that combined platform<sup>8</sup>, the new SRO could continue to support the OSC and the CSA in a comprehensive policy review of the other registration categories set out in the Report.

Finally, we agree with the Hansell opinion that if the proposed changes are adopted in the OSC Recognition Order, other CSA members may mirror the proposed changes in their own recognition orders so that the various recognition orders remain harmonized. Notwithstanding the successful efforts on the part of the CSA to work cooperatively and coordinate the exercise of their authority, not every such effort is successful and delays in decisions that affect the operation of IIROC’s business could compromise IIROC’s ability to meet its public interest mandate.

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<sup>7</sup> *Improving Self-Regulation for Canadians - Consolidating the Investment Industry Regulatory Organization of Canada (IIROC) and the Mutual Fund Dealers Association of Canada (MFDA)*, June 2020.

<sup>8</sup> We also support the Taskforce Report’s recommendation that the new SRO would continue to conduct national market surveillance.



In closing, we thank you again for the opportunity to comment on the issues and proposals in the Report, and look forward to the next phase of the Taskforce's work.

Yours truly,



Edward Iacobucci  
Chair, Corporate Governance Committee  
On behalf of:

Incumbent Independent Directors:

Michele Colpron  
James Donegan  
Victoria Harnish  
Shenaz Jeraj  
Gerry O'Mahoney  
Catherine Smith

Nominated Independent Directors:

Malcolm Heins  
Jennifer Newman  
Laura Tamblyn Watts