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Capital Markets Modernization Taskforce

September 4, 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 IIROC management. We agree with all the comments made by the Independent Directors of the Board of IIROC in their separate submission.

We fully support the Ontario Government's goal in creating the Taskforce to provide recommendations to reduce unnecessary regulatory burden and ensure a level playing field for all market participants, while improving investor experience, confidence and protection.

IIROC receives its authority under a legislative framework that each provincial and territorial government has adopted, and it is to those governments and their constituents that we owe our ultimate accountability. Overall, we believe that the existing IIROC governance structure, including its direct oversight by the Ontario Securities Commission (**OSC**) and the other members of the Canadian Securities Administrators (**CSA**), ensures 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 supporting efficient and competitive capital markets.

Our submission focuses first on the proposals that we believe will have an impact on IIROC's operations and our ability to meet our public interest mandate. We also comment on certain proposals that may impact market integrity given our position as the pan-Canadian self-regulatory organization (SRO) that oversees all investment dealers and trading activity on debt and equity marketplaces in Canada. Finally, we address some of the proposals relating to the Ombudsman for Banking Services and Investments (**OBSI**).

We have reviewed the separate submission of IIROC's Independent Directors (**Independent Directors' Submission**) focusing on issues relating to the governance of SROs, and specifically on the proposals for SRO governance as they apply to IIROC, along with the opinion from Hansell LLP.

We provide our response to the following proposals:

Section 2.1.3 – Strengthen the SRO accountability framework through increased OSC oversight

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

We agree with the Independent Directors' Submission 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 in support of our three-year Strategic Plan that we provide to the OSC and all CSA members in advance of any publication. Members of IIROC's executive management also meet formally and at regular intervals during the year with the executive leadership of the OSC (as well as other CSA members) to discuss strategic issues, align policy priorities and coordinate efforts.

2. OSC veto on significant publications

We agree with the Independent Directors' Submission that this formal change is not required given current practice.

For example, while not formally part of the Joint Rule Review Protocol for IIROC, IIROC pre-clears all major public comment proposals with the CSA Oversight Committee made up of representatives from all jurisdictions and the appropriate CSA staff.

The OSC/CSA already reviews and approves IIROC rule proposals and amendments. With respect to IIROC guidance, we recently issued "Guidance on Guidance"¹ which clearly outlines the role of guidance and how we will use it. We believe that the approach we describe in that Notice should address concerns that the Taskforce may have heard.

Our Guidance does not impose or imply specific requirements, but rather helps our Dealers comply with our rules in a manner that is appropriate for their individual business models. We also note that IIROC's OSC Recognition Order already contains a requirement for IIROC to "provide the Commission with reasonable prior notice of any document that it intends to publish or issue to the public or to any class of members which, in the opinion of IIROC, could have a significant impact on: (i) its members and others subject to its jurisdiction; or (ii) the capital markets generally".

¹ [IIROC Notice 19-0217, *Helping IIROC Dealer Members with Compliance – Role of Guidance* \(December 17, 2019\)](#)

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

We agree with the Independent Directors' Submission that the IIROC Board has always considered investor protection and retail investor issues.

IIROC has had, and will continue to 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 (previously known as the Canadian Association for Retired Persons) former Chief Public Policy Officer and a former board member of the Ombudsman for Banking Services and Investments (**OBSI**).

IIROC regularly engages with retail investors through qualitative and quantitative research with the assistance of an independent national research firm. IIROC's Investor Research Panel of 10,000 Canadian investors provides opportunities for direct input on a range of issues impacting investors and their confidence in the capital markets. This input also

informs management's and the Board's review of proposed rules and other requirements as they relate to retail investors, including²:

- 1,507 current and 501 aspiring investors' views on access to investment advice³
- 1,000 retail investors' awareness of and familiarity with policies and procedures to protect vulnerable investors, such as "safe harbour" and choosing a Trusted Contact Person⁴
- 1,011 retail investors' views on how breaches of IIROC rules and/or wrongdoing could be dealt with through alternative measures.⁵

We are currently conducting research to identify opportunities to improve our complaint-handling process and will use this opportunity to seek direct input from complainants about the potential return of disgorged funds collected from individuals or firms disciplined by IIROC.⁶

We also complement our quantitative research with qualitative focus groups on issues such as Know Your Client.

Early this year we announced plans to establish a pan-Canadian Expert Investor Issues Panel that will enable individuals with a wide variety of experience and expertise related to investors to provide direct input into or on all relevant investor issues, especially those that impact access to advice and services and investor outcomes and confidence.⁷ We are reviewing panels from other regulators and jurisdictions, such as the OSC's IAP, the Autorité des marchés financiers' Financial Products and Services Consumer Advisory Committee, and FINRA's Investor Issues Committee. Critical to this panel will be individuals with backgrounds in investor education, consumer outreach, seniors and/or vulnerable investor issues, professional regulation, financial services, government, public policy, and/or academics.

² In addition to the specific studies listed, we have also surveyed retail investors concerning their awareness of regulation (2020 and 2017), the Client Relationship Model (2018), IIROC's range of disciplinary sanctions (2018), market regulation (2017), and strengthening IIROC enforcement through legislative changes (2016).

³ [Access to Advice, January 2020.](#)

⁴ [Awareness and Attitudes Related to Provisions to Protect Vulnerable Investors and Investment Firms/Advisors, May 2019.](#)

⁵ [A Survey of Canadian Investors' Views on Alternative Disciplinary Proposals, July 2018.](#)

⁶ [IIROC Notice 20-0137, IIROC Priorities for 2021, June 29, 2020.](#)

⁷ [IIROC to form expert investor issues panel for valuable input on consumer issues, March 10, 2020.](#)

4. *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.

As outlined in the Independent Directors' Submission, 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 annual compensation. I confirm that as CEO I hold all my executives to the same high public interest standard.

5. *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 believe this proposal is necessary in light of the breadth of existing channels for Members to raise concerns with the service they receive from IIROC.

IIROC staff at all levels, including me, are readily and appropriately accessible to deal with issues that Members may have.

We use the feedback we receive from the National Advisory Committee and District Councils of Members who meet regularly with IIROC staff and the Board to understand and address regulatory challenges Members may be facing. Members also can raise any potential issues on a confidential basis through the Investment Industry Association of Canada (IIAC) and the Investment Funds Institute of Canada (IFIC). Furthermore, Members may also raise issues directly with the OSC and the CSA.

We also conduct a triennial Member Survey, which enables all IIROC-regulated firms to rate our performance in a confidential and anonymous manner. With the assistance of an independent research firm, we will be conducting this comprehensive survey later this month. In 2017, 71% of firms we regulate participated and the results were positive, with there being strong alignment and industry support for our Strategic Plan objectives. This includes being a trusted, respected and valued partner, making the delivery of securities regulation in Canada significantly more efficient, and inspiring confidence and deterring wrongdoing by having and using robust and appropriate tools. Almost all (92%) of respondents stated they believe IIROC is effective at delivering on its mandate.

6. *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 (Proposal 4)*

We agree with the Taskforce that having two separate SROs to regulate investment dealers and mutual fund dealers is outdated and confusing to investors.

IIROC's proposal to bring together IIROC and the Mutual Fund Dealers Association (**MFDA**) as divisions of a consolidated SRO as an important first step⁸ can be achieved without disrupting the existing rule framework, business models or regulatory fee structures.

This would immediately offer firms flexibility in how they 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 improve investor confidence and protection.

From that combined platform⁹, the new SRO will continue to support the OSC and the CSA in that review of the other registration categories set out in the Report.

Section 2.2 – Regulation as a Competitive Advantage

IIROC supports the Taskforce objective to foster innovation in capital markets. As the pan-Canadian SRO responsible for oversight of investment dealers and trading activity on debt and equity marketplaces in Canada, we can offer unique insights into some of the proposals found in Section 2.2. As some elements of each proposal are related, we address them in an order which we believe would be most helpful.

- 7. Introduce greater flexibility to permit reporting issuers, and their registered advisors, to gauge interest from institutional investors for participation in a potential prospectus offering prior to filing a preliminary prospectus (Proposal 8)*

We recognize the value of increasing the flexibility and efficiency of the capital-raising process that underlies this proposal and agree with the Taskforce that such a change would require increased monitoring and compliance examinations. In this context it is critical that such efforts be directed at preventing tipping, insider trading or other harms to market integrity.

IIROC is implementing mandatory client identifiers¹⁰ which will accompany trading information in debt and equity securities. With this additional information, our surveillance team will be able to attribute orders and trades to individual institutional investors in real-time to assist in detecting unusual trading behaviours.

⁸ [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.](#)

⁹ We also support the Taskforce Report's recommendation that the new SRO would continue to conduct national market surveillance.

¹⁰ [Mandatory client identifiers for reportable debt transactions came into effect on October 18, 2019. Mandatory client identifiers for all other transactions will come into effect on July 26, 2021.](#)

In addition, we suggest that the Taskforce consider the following:

- restricting the period to gauge interest to no more than five days prior to the filing of a preliminary prospectus and requiring disclosure to the market regulator that such a period has begun
- mandatory tracking by the issuer, and/or their registered advisors, of the identity of all institutional investors who are contacted.

8. *Prohibit short selling in connection with prospectus offerings and private placements (Proposal 13)*

IIROC supports this proposal.

Like the Taskforce, we have heard concerns about this activity and its potential impact on issuers, investors, and confidence in our capital markets. Implementing this proposal will mitigate some of our concerns with Proposal 8, discussed above.

This prohibition should improve the pricing and execution of prospectus offerings. We recommend that the period of restricted short selling should:

- begin when pre-marketing starts and end when the selling period is complete, should Proposal 8 be implemented, or
- begin at least five days prior to pricing and end when the selling period is complete.

With the implementation of mandatory client identifiers, IIROC's real-time surveillance will be able to monitor these offerings for activity that does not comply.

To maintain market efficiency, certain exemptions may be necessary, including an exemption for market makers to allow them to fulfill their obligations to marketplaces, and to assist with market stabilization activities.

9. *Mandate that securities issued by a reporting issuer using the accredited investor prospectus exemption should be subject to only a seasoning period (Proposal 5)*

Given the issues identified raised by the Taskforce in Proposal 13, we have concerns about the repeal of the four-month hold period.

We acknowledge the stakeholder views that many accredited investors are sophisticated and knowledgeable. However, we suggest that the four-month restricted period is not in place just for the benefit of these investors individually but rather for the market as a whole.

While removing the restriction may address some stakeholder concerns regarding the negative impact of the current hold period on liquidity, there may be significant unintended consequences. With no restriction on the ability to trade these securities, some accredited

investors may immediately liquidate their position. Should this become the norm, it could affect equity prices and harm both issuers and long-term investors. We also have concerns about the industry and regulatory resources needed to monitor and enforce the suggestion to include a representation and warranty in subscription agreements that the securities are being purchased with investment intent and not with a view to distribution.

In addition, this proposed change has consequences for retail investors. Sophisticated investors already have structural and economic advantages that make it more difficult for the small investor to compete on a level playing field. If adopted, the proposal could further exclude retail investor from financings, while more sophisticated investors get access to “hot” deals.

10. *Allow exempt market dealers (EMDs) to participate as selling group members in prospectus offerings and be sponsors of reverse-takeover transactions (Proposal 11)*

We support the public policy objective of enhancing capital raising opportunities for issuers, particularly venture issuers, as a means of stimulating economic growth in Ontario. However, without additional changes to accompany the proposal, we are concerned that doing so might undermine the underlying public policy goal.

EMDs are not able to trade directly on equity markets and, as a result, may not be able to support secondary trading in venture issuers. Due to their limited market capitalization, the securities of these issuers often struggle with illiquidity. We need to consider situations in which an EMD replaces an investment dealer in the selling group may result in the unintended consequence of removing the incentive for an investment dealer to support secondary market trading in the aftermarket. Therefore, the proposal may further negatively impact the secondary trading of such issuer’s securities and harm their economic prospects over the long term.

Section 2.6 – Modernizing Enforcement and Enhancing Investor Protection

11. *Give the power to designated dispute resolution services organizations, such as the Ombudsman for Banking Services and Investments (OBSI), to issue binding decisions ordering a registered firm to pay compensation to harmed investors, and increase the limit on OBSI’s compensation recommendations (Proposal 47)*

IIROC is a member of the Joint Regulators Committee (JRC) that oversees OBSI. The CSA members of the JRC announced in 2017 that they were actively engaged in considering options for strengthening OBSI’s abilities to secure redress for investors, including considering developing recommendations for implementing binding authority.

In 2018, the CSA members of the JRC advised that they had considered a regulatory framework that would empower OBSI to make awards that are binding on firms, but would also require legislative amendments, changes to OBSI processes, enhanced regulatory oversight of OBSI, and consideration of the need for a review mechanism for OBSI decisions.

They announced that they had decided to continue to monitor refusals and settlements for less than recommended amounts before further considering whether to move forward with the work necessary for binding decisions.

IIROC believes that binding authority for OBSI should be accompanied by appropriate process safeguards as noted above (changes to OBSI processes, enhanced regulatory oversight of OBSI, and consideration of the need for a review mechanism for OBSI decisions). We look forward to supporting the CSA's continued analysis of this proposal.

In closing, we applaud the Taskforce for undertaking this consultation to foster healthy capital markets and enhance investor confidence. The pandemic has certainly underscored the need to focus on appropriate and proportionate regulation and continue to be nimble and responsive to investors, issuers and the marketplace as a whole.

Thank you again for the opportunity to comment on the proposals in the Report. We would be pleased to address any questions you may have.

Yours truly,

A handwritten signature in blue ink, appearing to read "Andrew J. Kriegler". The signature is stylized with a large initial "A" and a long, sweeping underline.

Andrew J. Kriegler
President and Chief Executive Officer