CIRO Rule Consolidation Project: Phase 4

February 3, 2025

Submission to the Canadian Investment Regulatory Organization (**CIRO**)

ASSOCIATION DES BANQUIERS CANADIENS
CANADIAN BANKERS ASSOCIATION

The Canadian Bankers Association (**CBA**)[1] appreciates the opportunity to provide input on the consultation with respect to Phase 4 of CIRO's Rule Consolidation Project (**Phase 4**). Below we provide our responses to the specific questions set out in the consultation, followed by some additional feedback.

CIRO Consultation Questions

1. **Definition and application of "investment product". Will the revised definition, and application of the term "investment product" provide additional clarity to the scope of Dealer Member obligations to clients? What additional investment products should we consider obtaining Board approval to include in this definition? Are there different products that should be added for different regulatory purposes?**

In our view, the proposed definition does not provide regulatory clarity but rather introduces potential ambiguity and unpredictability to the scope of Dealer Member obligations to clients. This is by virtue of the "catch all" provision that would grant CIRO jurisdiction over any business/product that has been "approved by the Board as an investment product," This is problematic as the criteria by which such Board approval would be granted, including consideration of limitation to CIRO's jurisdiction, is not specified. Moreover, there would be no opportunity for public comment prior to an expansion of CIRO jurisdiction under this provision.

To provide additional clarity to Dealer Members, any proposed expansion of CIRO's jurisdiction over type of business/product should be specific and follow the existing rule making/rule amendment process, as the definition of an investment product is material and central to the requirements under the rules. This includes review and approval by the Canadian Securities Administrators (**CSA**) and a public comment period. A public comment period is necessary, as it allows sufficient time for stakeholders to evaluate a proposal and if a rule amendment is approved, time for Dealer Members to consider the impact on and implement any required

[1] The Canadian Bankers Association is the voice of more than 60 domestic and foreign banks that help drive Canada's economic growth and prosperity. The CBA advocates for public policies that contribute to a sound, thriving banking system to ensure Canadians can succeed in their financial goals.

changes to policies, procedures, client disclosures/agreements and systems, as well as time to understand if notice to CIRO concerning new business is required.[2]

Further, there is a concern that a broad "catch all" could be used to expand the definition to, for example, products that are generally not captured or exempt under the provincial securities acts This concern of an overly broad application and potential uncertainty is compounded by the fact that other IDPC Rules refer to “types of business” or “products” (e.g., Rules 2553. 2803, 3211 and 3216) rather than investment products.

In addition to creating uncertainty and operationalizing the making of material rule changes without public consultation, the proposed definition could necessitate gratuitous rewriting of definitions or use of terms in Dealer Member client contracts and associated documents. This would be unduly disruptive and costly to Dealer Members and may lead to client confusion, without commensurate regulatory value.

Investment dealers were recently required, in an abbreviated timeframe, to implement documentation updates to reflect the derivatives modernization changes to definitions to add a new defined term of derivatives and include a precious metals bullion asset class throughout client agreements and elsewhere. These changes are now completed. The current proposed additional change to defined terms impacting products ought to have been proposed as part of the derivatives modernization changes if it was indeed necessary for regulatory purposes.

2. **Applying CFO requirements to mutual fund dealers. We recognize that requiring mutual fund dealers to appoint a CFO may be a significant material change to the governance and resourcing requirements of many such dealers.**

   We are seeking feedback on several points regarding this proposal:

   - **For mutual fund dealers who do not support the implementation of this**

[2] For example, a Dealer Member is required to notify CIRO prior to its Approved Persons dealing and advising in a type of business not listed in Investment Dealer and Partially Consolidated (I**DPC**) Rule 2553(3)(iv).

requirement (and in particular, any mutual fund dealer who do not currently have a CFO), we inquire as to who, at an individual level, fulfills their existing financial obligations under MFD Rule section 3 (which broadly assigns the obligations to the 'Member' instead of an individual), including a description of who oversees financial risk to clients and the organization on a regular (i.e. daily) basis.

- **To what extent, and on what basis, should the proposed CFO requirement reflect the Rule Consolidation Project objective of scalability? For instance, should the requirement for a Dealer Member to designate a CFO only apply to mutual fund dealers in certain scenarios, such as:**
- **Based on a certain minimum AUM (and what should that threshold AUM be),**
- **If a mutual fund dealer has a corporate governance and/or Executive structure beyond a single UDP/CCO, and/or**
- **Based on the complexity of products or services offered (and if so, which products and/or services require the financial expertise of a CFO)?**
- **Whether there are significant concerns regarding the potential scarcity of CFO candidates in the mutual fund industry and/or the anticipated time horizon to hire a CFO candidate at a mutual fund dealer**

In general, mutual fund dealers have demonstrated that a registered CFO is not necessarily required to conduct current business. Thus, a grandfathering should be granted to those existing mutual fund dealers who are maintaining their current business models. However, if a mutual fund dealer intends to change or expand its current business model to include margin accounts, or other products (e.g., ETFs) and services, then in our view, it would be appropriate for the proposed CFO requirements to apply due to the increased business risk and complexity. Requiring a registered CFO in the absence of evidence of a need will likely unnecessarily increase the cost of delivering investment advice to the public.

Given the new proficiency and experience requirements, we would recommend providing an adequate transition period to enable existing CFOs to meet these requirements. We are supportive of a provision whereby exemptions from the proficiency requirements can be requested similar to DC Rule 2504. See also our comments below in our response to Question 3 noting the need to defer implementation of any new proficiency requirements,

3. **Proficiency requirements and the Approved Person regime for UDP of mutual fund dealers.**

- **Given that the UDP has the highest level of liability and oversight in a Dealer Member, is it reasonable to impose the CIRO approval process as is currently set out in the IDPC Rules (including the successful completion of courses, examinations, and minimum experience) in addition to the registration required by securities legislation?**
- **If the answer to the above is 'yes,' this may be disruptive to mutual fund dealers whose UDP does not currently meet the proficiency requirements set out in the IDPC Rules. To what extent is it appropriate to exempt these existing UDPs from these requirements, or alternatively, to provide a longer time horizon (beyond the general implementation date) for them to complete their proficiency requirements?**

CIRO published proposed amendments to the IDPC rules to reflect a proposed new proficiency model in July 2024[3]. It was stated in the consultation notice issued in connection with those proposed amendments that consideration of any future changes to the proficiency regime relating to mutual fund dealers will be carried out in collaboration with the CSA. As the proficiency model for mutual fund Dealer Members of CIRO is still under consideration, the implementation of any new proficiency requirements for mutual fund dealers should be deferred until the new proficiency model is finalized.

If CIRO does move forward with this proposed change at this time, an adequate time horizon should be provided for existing UDPs to meet the proficiency requirements. A phased implementation of 2-3 years could ensure compliance while providing sufficient time for UDPs to complete necessary courses and examinations. Similar to our response to Question 2 above, if the mutual fund dealer's business model remains status quo, then existing UDPs should be

[3] Rule amendments - Request for comments - Proposed Proficiency Model - Approved Persons under the Investment Dealer and Partially Consolidated Rules | Canadian Investment Regulatory Organization

grandfathered with respect to proficiency requirements. However, if the business model changes in the future to include margin, managed accounts, or other products, then the proposed UDP proficiency requirements would apply at that time to address the risks and complexity associated with the new expanded business model.

4. **Implementation for existing (unregistered) Approved Persons of Mutual Fund Dealer Members. With respect to the categories of Approved Persons of mutual fund dealers that are not subject to a registration requirement under securities legislation, we have generally proposed these Approved Persons conform to CIRO's Approved Person regime and corresponding proficiency requirements. Our view is that these roles have significant oversight responsibilities that justify this potential additional regulatory burden on mutual fund dealers.**

   However, the same rationale may not apply for Directors. We expect that directors of mutual fund dealers who were not previously subject to proficiency requirements may not be 'actively engaged' in the activities of the business of the mutual fund dealer and do not play an operational, oversight nor managerial role in the dealer's business. Under the current proposals in Phase 4, these mutual fund dealer Directors would be subject to a CIRO approval process and net-new proficiency requirements.

   To what extent would it be appropriate to grandfather the existing Directors of mutual fund dealers into the Approved Person regime? Please advise if there are significant concerns regarding this approach, particularly regarding the lack of minimum proficiency requirements of existing mutual fund dealer Directors and whether this could undermine investor confidence in mutual fund dealer as compared to investment dealers.

As stated in our response to Question 3 above, we feel that the implementation of any new proficiency requirements for mutual fund dealers needs to be deferred until the new proficiency model for such dealers is finalized in collaboration with the CSA.

That being said, we believe that existing mutual fund dealer Directors should be grandfathered

into the CIRO Approved Person regime. The principles of CIRO's Rule Consolidation project include efficient development and non-disruptive implementation. To require Directors to undertake completion of the new proficiency requirements will be burdensome and unduly disruptive to the operations of mutual fund dealers. Investor confidence will not be undermined by grandfathering in existing Directors because these Directors will have been operating successfully within mutual fund dealers prior to the implementation of the consolidated rules and new Directors going forward will be subject to the harmonized proficiency requirements.

5. **Transition period for Approved Person categories where new requirements are introduced or existing requirements have been materially changed. We recognize that we have proposed significant changes, including net-new Approved Person categories and corresponding proficiency obligations, to the Approved Person regime for mutual fund dealers. As a result, existing Approved Persons sponsored by mutual fund dealers, as well as individuals who are not currently considered Approved Persons but will be caught by the proposed DC Rules, may be required to attain additional proficiencies. This may be a time-consuming process and might result in individuals incurring additional professional expenses.**

   Given the above considerations, should the proposed proficiency requirements for mutual fund dealers' Approved Persons be subject to an extended transition period beyond the general effective date for the DC Rules, and if so, what is an appropriate extended transition period?

As stated in our responses to Question 3 and 4 above, we feel that the implementation of any new proficiency requirements for mutual fund dealers needs to be deferred.

Should CIRO proceed with the proposed changes contemplated by Question 5, we support an extended period of 2 to 3 years beyond the general effective date to provide sufficient time for mutual fund dealers' Approved Persons to obtain new proficiencies where required. The new requirements will be time-consuming and costly for individuals to obtain and without additional time to obtain proficiencies, mutual fund dealer firms may be left with a large number of individuals who cannot qualify on the general effective date. This would cause delays, business

disruptions and a negative impact on the client experience. Providing additional time to allow affected Approved Persons to obtain the proficiency requirements supports the effective and non-disruptive objectives of the Rule Consolidation project.

6. **Prohibition on accepting certain positions of control or authority over client affairs. Does the addition of the prohibition on an Approved Person or employee accepting a position of power of attorney, trustee, executor or otherwise having full or partial control of the affairs of a client have implications in respect of the relationship between the client and the Approved Person or employee?**

   Should there be exceptions to this prohibition, and if so, under what circumstances?

In general, we are concerned with broad application of this prohibition to all employees, which would include individuals who are not client facing or in positions of influence. The general prohibition under the proposed Rule should apply to Approved Persons only. With respect to remaining employees, CIRO dealers should have the discretion to consider, in accordance with existing obligations under CIRO Rules, to identify and address conflicts of interests in the best interest of the client, whether through its own prohibitions in specific circumstances or other measures depending on the nature and role of the employee.

Moreover, including employees in scope sets this new proposed “conflict of interest” prohibition apart as more restrictive than the others that are applicable to Approved Persons only, such as undertaking certain fiduciary positions or lending to clients. The CIRO consultation document does not offer a rationale for this higher standard nor indicate if there are issues with cases of acceptance of such positions by Approved Persons.

7. **Is it appropriate to prohibit an employee or Approved Person from accepting the status of a beneficiary of a client’s estate or receiving a bequest from a client’s estate upon learning of such status unless they are a member of the client’s immediate family?**

While an Approved Person accepting the status of a beneficiary of a client’s estate can create a

material conflict of interest where that Approved Person is involved in managing that client's investments (unless they fall within the CIRO definition of "immediate family member" appropriately targeted to familial relationships that are commonplace in estate related circumstances), imposing an outright prohibition is overly prescriptive. It would extend to employees not involved in the management of the relevant client's assets. It is possible for an employee of a Dealer Member, who does not fall under the definition of a client's immediate family member and is not involved in managing that client's investments, to have a personal bona-fide relationship with that client. For example, a client of a Dealer Member leaves a bequest to a neighbour or close friend who happens to be an employee of the Dealer Member working in the Dealer Member's Information Technology department.

We would also note that applying a blanket prohibition to all employees would be especially restrictive and unfair in the case of larger Dealer Member firms, where designations and bequests of this kind are likely to exist.

In our view, it would be sufficient to address this issue with guidance respecting Approved Persons applicable to Dealer Members, rather than a broad prohibition in a rule that applies to all employees. The necessary flexibility would be preserved by addressing in guidance considerations for evaluating whether to approve, place conditions or disapprove beneficiary designations or bequests from non-relative clients of Approved Persons by the Dealer Member, including those existing prior to the issuance of the guidance, particularly in instances with unintended negative impact where the client may not have capacity or wish to change their beneficiaries or bequests.

Such a flexible approach would further be aligned with the recently adopted FINRA rule on this topic, which does not apply to employees generally, nor impose an outright prohibition on registered persons.[4] Rather, it allows the firm to evaluate and approve, place conditions or disapprove of the registered person being named a beneficiary or receiving a bequest. This flexible approach allows the firm to determine if there is evidence in any case that such

[4] 3241. Registered Person Being Named a Customer's Beneficiary or Holding a Position of Trust for a Customer | FINRA.org

proscription is warranted. It should also remain the determination of a Dealer Member as to whether it wishes to have a more stringent policy in place to restrict such acceptance completely from non-relative clients.

Additional Feedback

CIRO Guidance

Regarding the impacts of Phase 4, CIRO notes that it will continue to provide guidance that will contain more detailed suggestions for Dealer Members to achieve compliance. To fully understand and assess the impact of the amendments resulting from Phase 4, and the changes that will need to be made to Dealer Member systems, policies and procedures, any such guidance should be published for comment before the rules are finalized.

Other changes that will have significant impact on mutual fund dealers and/or investment dealers

There are net new requirements proposed under Phase 4 other than those referenced in CIRO's specific questions above that will impact mutual fund dealers and/or investment dealers. These changes will require a sufficient transition period to provide adequate time for changes to policies and procedures, systems, and training. Below we provide some examples of such requirements and note some issues that would benefit from clarification regarding these requirements:

a) **Rule 3110 – Personal Financial Dealings.** Similar to our comments above in response to Questions 6 and 7, extending this prohibition to all employees is too broad and should instead be limited to Approved Persons. We also note that in National Instrument 31-103, the restriction on lending to clients (s. 13.12) applies only to "registrants".

b) **Rule 3209 - Primary responsibility, delegation and obligation to keep current.**

The Mutual Fund Dealer (**MFD**) Rules reference "material change" and define what a material change is. Rule 3209 references "significant change", which is consistent with the definition of "material change" under current MFD rules. However, this term is not defined within the proposed Consolidated Rules but in IIROC *Guidance Notice - GN-3400-21-004 – Know-your-client and Suitability Determination for Retail Clients*.[5] We recommend that the term 'significant change" be defined in the Consolidated Rules for clarity.

c) **Rule 3216 – Relationship Disclosure.** The current requirement under IDPC Rule 3216 (5)(ii)(k) to include "a listing of the account documents required to be provided to the client with respect to the account" will be new for mutual fund dealers. Many mutual fund dealers use a static relationship disclosure document (**RDD**), and different account types have different documents associated with them. Dealers have procedures to ensure that clients are provided with the required documents on account opening. We are therefore uncertain as to the regulatory value of this requirement.

d) **Rule 3947 - Supervision of new Registered Representatives and Investment Representatives.** In the *Registered Representative / Investment Representative Monthly Supervision Report (**Report**)*[6] the requirement is to review "all client accounts of the approved person." Clarity is required with respect to the application of this requirement in cases where client accounts are not anchored with a specific Approved Person but serviced by a team of mutual fund dealing representatives. We would also seek clarification regarding the expectation in item 3 of this Report: "3. A review of trading activity on a daily basis has been conducted relative to the approved person's personal and related accounts" in relation to mutual fund dealing representatives whose clients only hold mutual funds and/or GICs. In this scenario, there would be no risk of front running or breach of client priority and very low risk of access to inside information.

[5] Guidance on Know-your-client and Suitability Determination | Canadian Investment Regulatory Organization
[6] Registered Representative / Investment Representative Monthly Supervision Report

e) Rule 1103 Delegation and automation and 3907(7) Delegation of supervisory tasks.

i) *Scope of Automation*

It would be helpful to provide guidance (including criteria and examples) on the scope of "automation" that would be captured under these rules. For example, would an excel macro that performs a simple operation, such as grouping entities for further analysis, be considered to be "automation"? If that macro was part of an end-to-end process that was otherwise entirely manual in nature, would the process be deemed "automation"?

ii) *Imposition of Additional Requirements*

DC Rule 1103(3)(i) requires the individual executing the automation "to understand how the automated tasks and activities work" and DC Rule 3907(ii) imposes a similar requirement on the Supervisor. Such requirement is not possible to comply with since "understanding" automation is subjective and internal to the individual. It may be more useful to have a proficiency/qualification or training standard that can be objectively applied for the purposes of executing automation, which should be within the purview of Dealer Members as is relevant to the automation at issue. Guidance on how these requirements will be interpreted would be helpful. Is the expectation that the individual and Supervisor understand how to execute/verify the successful completion of the "automation", or do these rules impose a new requirement to understand the technical details associated with that "automation"? If so, what level of detailed understanding would be required?

Guidance would also be helpful regarding DC Rule 1103(3) (ii), where the individual executing the automation is to "ensure proper performance of the related function" and DC Rule 3907(7) (iii), which imposes a similar requirement on the Supervisor. It is similarly not possible to "ensure" proper performance as automation often gives rise to technical issues which arise notwithstanding best efforts. It not possible to "ensure"

these issues never arise but they can be mitigated and dealt with through policies and procedures. In the circumstances, does this refer to business as usual Information Technology processes/procedures designed to support technology performance as expected, or is something more required on the part of the individual/Supervisor? It would be more appropriate to consider that the obligation is to have appropriate policies and procedures to support automated functionality as is already implemented by firms.

iii) *Automation Task Force*

We would encourage CIRO to provide early guidance on the extent to which Dealer Members will have new opportunities to automate particular functions. The time needed to implement new automation will be extensive and require significant changes to policies and procedures and training to Approved Persons. In this regard, the creation of an Automation Task Force would be a useful endeavour to provide guidance to the industry.

f) Rules 3402(6) and (7) regarding client leverage strategies. In our view, these provisions are too broad and place Dealer Members in an untenable position. It is not possible to know whether funds invested are borrowed from third parties if the client does not disclose this despite the Dealer Member's best effort to understand a client's financial circumstances. To assess, detect and prevent leverage strategies that are not recommended or known to the Dealer Member cannot be the firm's responsibility since that is dependent on client disclosure concerning activities with third parties and such disclosure cannot be compelled. In addition, the term "leverage strategy" should be defined to help clarify the scope of Dealer Member responsibilities.

g) Rule 3961(2) Responsibility of Supervisors for derivatives accounts. Similar to the point above, this provision presumes that Dealer Members would know, at account opening, whether funds invested are borrowed from third parties. In addition, it is not clear whether this provision means that a leverage strategy or other strategy implemented after account opening needs to be approved and supervised.

h) Rule 3602 Advertising. The proposed amendment prohibiting use of an image "which

conveys a misleading impression" creates a vague and subjective standard that similarly would put Dealer Members in an untenable position. In our view, the standard must be whether communications, including images, are false, which is an objective standard that can be proven one way or the other.

i) **Rule 2216 to 2219 Shared office premises.** As stated in our comments with respect to Phase 3 of the Rule Consolidation Project, in our view, certain aspects of the requirements with respect to shared premises do not adequately accommodate arrangements whereby bank owned Mutual Fund Dealers operate out of bank branches, where mutual fund dealing representatives are dually employed by the bank and sell both GICs and mutual funds. In addition, the carry-over from the Investment Dealer rules of a more stringent method of obtaining consent to disclosure of information between members of the financial institution's businesses than required under privacy law, for shared premises specifically, is unnecessarily burdensome and operationally unwieldly for all Dealer Members without any regulatory necessity.

j) **Rule 3114 Referral Arrangements**. We note that the definition of "referral arrangement" refers to providing or receiving a referral fee to or from another "person", whereas NI 31-103, section 13.7 refers to "person *or company*" when defining this term.[7]

Mutual Fund Dealer Branch Manager Proficiency Requirements

We note that CIRO plans to assess the appropriate proficiency requirements for Supervisors and whether those requirements can be harmonized across Dealer Members. In the event that harmonized proficiency requirements are ultimately adopted for both investment and mutual fund dealer Supervisors, we recommend that existing Supervisors should be grandfathered.

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[7] National Instrument 31-103 - Registration Requirements, Exemptions and Ongoing Registrant Obligations, s. 13.7

We thank you for taking the time to consider our views regarding Phase 4 and trust that you will find these comments helpful. We would be pleased to discuss our comments further at your convenience.