INVESTMENT INDUSTRY ASSOCIATION OF CANADA
ASSOCIATION CANADIENNE DU COMMERCE DES VALEURS MOBILIÈRES

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Dear Mr. Hart and Ms. Tabesh-Ndreka:

RE: Request for Comments: Rules Notice 10-0266 "Plain language rule re-write project – Dealing with clients, Proposed Rules 3400 - 3900" (the "Notice")

The Investment Industry Association of Canada (IIAC) appreciates the opportunity to comment on the Notice, issued on October 8, 2010.

The IIAC organized a Working Group to identify and discuss issues with the proposal put forward in the Notice. We ask that IIROC consider the comments and request for clarification articulated by our members. The IIAC would be happy to meet with IIROC staff to further discuss the issues raised in this letter.

Proposed Plain Language Rule 3400 (Suitability)

Suitability of orders and recommendations (Proposed Rule 3402(2))

Proposed Rule 3402(2) will require Dealer Members to consider a number of new criteria when accepting an order from a client or making a recommendation to ensure that the suitability obligation is met. It is proposed that Dealer Members will consider "the suitability of the account type, the suitability of the trading strategy, the suitability of the order type and the method of financing the trade." The Working Group would appreciate further information as to why these criteria have been chosen, as well as clarification on what is required with respect to determining the "method of financing the trade."

Current Dealer Member Rule 29.26 (now Proposed Rule 3209) dealing with leverage disclosure, requires that a leverage risk disclosure statement be provided to clients at the time a new account is opened, when a recommendation is made to a client to purchase securities using borrowed money or when the Dealer Member becomes aware of a client's intent to purchase securities using borrowed money. Is the intention of the Proposed Rule to broaden what is currently required under the leverage requirement? Will Dealer Members now be required to ask the client, on every trade, whether they intend to use borrowed money?

The Working Group cautions that determining the method of financing the trade for each trade could result in delays in putting trades through. Furthermore, if it is the intention of the Proposed Rule that this information be determined on a trade-by-trade basis, we request clarification as to whether reasonable efforts would suffice in trying to obtain this information and what reasonable efforts would entail.

The Working Group suggests that if such language is retained in the rule, that this only be taken into account where margin is being used or, alternatively, that the wording be amended to state "method of financing the trade if aware of it."

The Working Group would also like further guidance on how an account type suitability review would be conducted. The IIAC had previously questioned how this would be done in our comment letter on the draft Guidance Note 09-0293, dealing with KYC and Suitability. For instance, if a client wishes to open a margin account, but never borrows money from the Dealer Member to purchase securities, would this account type be deemed suitable? Further guidance is appreciated.

With respect to suitability of the order type, the Working Group would appreciate clarification as to what this would entail, as the Working Group is unable to determine a situation to which this would apply.

The Working Group also has concerns with the change in language to now require a Dealer Member to refuse an unsuitable order which is a different standard than previously required and is inconsistent with National Instrument 31-103 (NI 31-103). The Working Group requests that the current rule be retained which only applies to

recommendations and which in practice requires a Dealer Member to warn a client if they think an unsolicited trade is unsuitable.

Suitability determination not required (Proposed Rule 3405(1)(iii))

The Working Group is pleased with the inclusion of regulated entities under Proposed Rule 3405. However, we note additional changes have been made from the current version of the rule which have not been discussed in the Notice. Current IIROC Rule 2700 provides an exception to the suitability requirements for permitted clients, as defined under National Instrument 31-103 (NI 31-103) where a waiver is obtained. The Proposed Rule does not appear to retain this exemption and the Working Group would appreciate clarification as to where in the Proposed Rules this provision has been moved or confirmation that the exemption for permitted clients under NI 31-103 is available to Dealer Members.

Proposed Plain Language Rule 3500 (Sales Practices)

Service fees (Proposed Rule 3506)

The Working Group is pleased that IIROC has clarified that the requirement to provide a service fee schedule does not apply to institutional clients. However, the Working Group would appreciate if IIROC would verify that the 60 days prior notice requirement does not apply to interest rate charges.

Commission fees and advisory fees (Proposed Rule 3505)

Proposed Rule 3505 requires Dealer Members who charge advisory fees, or a fixed dollar or percentage commission fee, to provide the fee schedule to retail clients upon opening the account or 60 days prior to the fee being charged. This proposal will have a major impact on current practice, as often fees are negotiated and renegotiated on a client basis, account basis and often on a trade-by-trade basis. Generally, each Dealer Member has guidelines which have been approved with respect to the minimum and maximum commission or advisory fee that can be charged. The client receives information about the fee that applies to that client, allowing the client to compare fees. It would therefore, appear that the entire firm's fee schedule that applies to all clients is irrelevant to any individual client. Instead of referring to a "fee schedule", a simple reference to the "fee" that is applicable to the client could provide clarity.

The Working Group would appreciate clarification as to what securities this provision applies to and specifically, whether it would apply to products with embedded compensation. As the term "advisory fee" may encompass a broad range of fees, the Working Group proposes that a definition be provided to clarify the types of fees that fall under the Proposed Rule. For instance does this only include fees known at the time of account opening and not all potential fees charged to any account of the firm?

Section 14.2 of National Instrument 31-103, requires disclose to a client of the fee that a client will pay to the Dealer Member for operating the client's account. Furthermore, the Canadian Securities Administrators (CSA) noted in its June 25, 2010 publication requesting comments on amendments to NI 31-103 that they are continuing to work on developing the requirements and guidance on cost disclosure to clients as part of their development of the client relationship model. In light of the existing requirement to disclose costs, and the impending CSA client relationship model proposal, the Working Group suggests IIROC should refrain from pursing this proposal until it can be considered in the larger regulatory context. However, if the Proposed Rule is retained, the Working Group proposes that the Proposed Rule contain a carve out where the commission has been agreed to between the parties. There does not appear to be any reason for a waiting period where a fee has been negotiated between the parties.

Inside information (Proposed Rule 3507)

The Working Group commends IIROC for replacing the terms: fiduciary obligation, privileged information and recipient of information with special relationship, material non-public information and in the necessary course of business respectively. Such changes bring these concepts further in line with securities legislation, provide less ambiguity and eliminate the need for competing rules with different terminology.

Distributions (Proposed Rule 3502)

Proposed Rule 3502(1) states that "a Dealer Member cannot participate in the distribution of securities to the public at a price higher than the stated initial price of the securities." The Working Group notes that this language has been changed from the current version where this is restricted only to those acting as a member of the distribution group. The current rule states that "a Dealer Member shall not offer for sale or accept any offer to buy all or any part of the securities acquired by such Dealer Member through participation in such distribution as an underwriter or as a member of a banking or selling group." The Working Group requests that the current limitation be included in the Proposed Rule.

Premarketing (Proposed Rule 3508)

The Working Group noted that the term Distribution Discussions is capitalized and as such, queried whether it is meant to be a defined term. For clarity and consistency with securities legislation and the Universal Market Integrity Rules (UMIR), we request that IIROC provide a definition for the term.

Proposed Plain Language Rule 3600 (Communication with the Public)

Scope of obligation (Proposed Rule 3602)

The current rules with respect to advertising only refer to Dealer Member and do not specifically reference the obligation of Approved Persons in communicating with clients.

The Proposed Rule will now specifically reference Approved Persons and the Working Group is in agreement with this amendment.

The Working Group is, however, concerned with the change in language in Proposed Rule 3602(1), which removes the qualifier "knowingly" with respect to the use of a Dealer Member's name. The Working Group has some concerns with the imposition of this strict liability on the use of a Dealer Member's name. Practically speaking, the Dealer Member cannot control all usages of its name before the fact and should not be liable for statements made under its name without its knowledge.

Record retention (Proposed Rules 3602(7) & 3802)

Proposed Rules 3602(7) and 3802 require that all copies of advertisements, sales literature and correspondence and all records of supervision be retained for a period of seven years from the date the record is created. The Working Group acknowledges that this time line is consistent with NI 31-103. However, from an operational perspective, there are some concerns with the requirement to store and retrieve the information given the sheer magnitude of these records. The Working Group would like clarification as to whether the information will be required to be kept on site and whether storage requirements can be satisfied by electronic methods.

Research Reports (Proposed Rules 3606 - 3623)

The Working Group notes that while IIROC has not indicated any changes having been made to the rules dealing with Research Reports, there appears to be a shift in the language and terminology used under this rule. For instance, the current rules use the phrase "beneficially own 1% or more of any class of the issuer's equity securities." The Proposed Rule uses the phrase "has a financial interest in the equity securities of the subject issuer." Another example of a change in phrasing is that, under the current rule, it states "hold or are short any of the issuer's securities directly or through derivatives," while under the Proposed Rules it states "has a financial interest in any equity securities of the subject issuer." It is unclear whether having a "financial interest" is the same as holding or being short directly or through derivatives. When calculating "financial interest" would short positions be offset against long positions so that if a person had no economic exposure to a security they would have no financial interest?

While we understand that IIROC has re-written the rules in plain language, the Working Group has some concerns that the change in phrasing may ultimately result in a change in the requirements. As such, the Working Group requests that IIROC review the amended language to ensure that the requirements have not changed.

The Working Group requests come clarification under Proposed Rule 3606(1)(iv), which states that "Dealer Members will be required to have written policies and procedures governing the making of recommendations." Currently, the research rules only apply to an analyst's recommendations and the change in wording is confusing, since there is currently a requirement that recommendations be suitable for a client under Rule 3400

and a supervisory requirement under Rule 3900. As such, the Working Group recommends for clarity that IIROC add the word "analyst" to Proposed Rule 3606(1)(iv) immediately before the word "recommendation."

The Working Group would also appreciate some information on an FAQ that existed with respect to Research Reports and was posted on the IIROC website. We have been unable to find this helpful FAQ on the website and would appreciate clarification as to where this information can be located.

In Proposed Rules 3610(2) and 3616(1) the qualification at the end of Subsections (ii) and (iv) respectively, should qualify all Subsections of these sections. As drafted, it could be read to only qualify those specific sections and, as such, we ask that it be amended.

Proposed Plain Language Rule 3700 (Reporting and Handling of Complaints, Internal Investigations and other Reportable Matters)

The Working Group does not have any issues with Proposed Rule 3711 relating to the prohibition of release restrictions being extended to institutional clients.

Settlement Agreements (Proposed Rule 3710(3))

Proposed Rule 3710(3) uses the term Approved Person. The Working Group suggests that this term be replaced with Partner, Director, Officer or Employee since an individual does not have to be registered to be authorized by the Dealer Member to approve settlements.

Handling Client Complaints (Proposed Rule 3722)

Proposed Rule 3722 and other rules use the term "sales Supervisors" and the Working Group would appreciate clarification as to who "sales Supervisors" applies to. To remain consistent with current definition, we suggest that the word "sales" be removed from the term "sales Supervisors" or the term "Supervisor" be changed to lower case to remain consistent with the current definition.

Guidance Note 3700-2

Guidance Note 3700-2 requires Dealer Members to report prescribed internal investigations related to the activities of duly employed representatives (a registrant employed by both the Dealer Member and the bank). Given privacy issues between the Dealer Member and the bank, Dealer Members may be able to report as required but may not be able to readily share information arising from the bank. The Working Group questions whether IIROC would still find this reporting useful and whether IIROC is fully aware of any limitations/restrictions in providing this type of information from a privacy perspective.

Proposed Plain Language Rule 3800 (Books and Records)

Reference to "Statistical or other Information (Proposed Rule 3805(4))

The Proposed Rules uses the phrase "statistical or other information" and the Working Group would appreciate clarification of the phrase "statistical or other information."

Opening and closing transactions requirement for blotter, record of order received and trade confirmation (Proposed Rule 3806(1)(xi))

The Proposed Rule requires Dealer Members to maintain blotters by itemizing daily "whether the transactions are opening or closing transactions." The Working Group would like clarification on the type of transactions this requirement applies to, such as equity, options or futures.

Client and non-client ledger accounts (Proposed Rule 3808(3))

The Proposed Rule provides that when a Dealer Member invests the funds segregated for the benefit of its clients, the ledger must contain specified information. Current Rule 200.1(c)(6) specifies the requirement with respect to any investments of such money proceeds or funds. We note that the term "funds" is not specific and would like to seek clarification on the meaning of the term.

Records of orders received (Proposed Rule 3812(3)(ii))

The Proposed Rule provides that a Dealer Member must record specified information if the order or instruction is placed by a person other than "a person authorized in writing to direct orders for the account." Current Rule 200.1(g)(5)(B) provides that the requirement applies when the order is placed by "an individual other than… an individual duly authorized to place orders or instructions on behalf of a customer that is a company."

We note that the proposed section is not specific and would like clarification as to whether this requirement applies to corporate accounts only or other types of accounts as well. If it does apply we would appreciate clarification on applicability of the rule to personal accounts.

The Working Group would also like clarification with respect to current Rule 200.1(g) dealing with memoranda. This provision does not appear to have been adopted in the Proposed Rules and should be included. The Working Group would appreciate clarification as to whether Proposed Rule 3812 requires Dealer Members to only keep records of instructions from clients or does it extend to instructions between Dealer Member employees?

Account transfers (Proposed Rule 3813(1))

The Proposed Rule requires Dealer Members to maintain an electronic record of all communications about account transfers. This reflects what is currently included under Guide to Interpretation Rule 200.1(n).

The Working Group would appreciate further explanation as to whether the Proposed Rule requires Dealer Members to tape and scan all relevant phone calls and paper documents, respectively.

Marketplace disclosure requirements (Proposed Rule 3831(1)(iii))

Proposed Rule 3831(1)(iii) states that "a confirmation of the transaction sent to a client must contain as a minimum the following information: the marketplace on which the transaction took place, or if applicable, a statement that the transaction took place on more than one marketplace or over more than one day." The Working Group would appreciate confirmation that where the transaction took place on more than one marketplace over more than one day, that the language on the confirmation would simply read "the transaction took place on more than one marketplace or over more than one day," as opposed to specifying each exchange and each date, with the specific information being available on request as it is under accumulation accounts.

Requirements for confirmations (Proposed Rule 3831(1)(vi))

The Proposed Rule provides that the trade confirmation sent to a client must include the phrase "the commission, sales charge, service charge and any other amount charged in respect of the transaction."

We note that in June 2010, IIROC published for comment a proposal which requires Dealer Members to disclose yield to maturity on trade confirmation for fixed-income securities, and notations for callable and variable rate securities and to include on trade confirmations sent to retail clients in respect of OTC transactions a statement indicating that they have earned remuneration on those transactions unless the amount of any mark-up or mark-down, commissions or other service charges is disclosed on the confirmation (see IIROC Notice 10-0163).

It appears that the Proposed Rule is related to the items that are currently under consideration and we assume that the rules will be made consistent. We would also like to seek clarification as to what "any other amount charged in respect of the transaction" refers to.

Requirements for client account statements (Proposed Rule 3841(1) and 3841(2))

The Notice states that the Proposed Rule takes into consideration the requirements as set out in Section 14.14 of NI 31-103. The Working Group would like to note that the CSA has proposed amendments to NI 31-103 to conform with the change to International

Financial Reporting Standards (IFRS). The current CSA proposal which is out for comment refers to "fair value" not "market value" as contemplated under Proposed Rule 3841. Additionally, IIROC published Notice 10-0230 on August 27, 2010 which contemplates changes to IIROC Form 1 to adopt IFRS for regulatory reporting purposes and contemplates using a fair value approach. The Working Group assumes that Proposed Rule 3841 will be updated once the changes to NI 31-103 and IIROC Form 1 have been finalized. The Working Group requests that Proposed Rule 3841 should require that a client statement use fair market value in accordance with the definition of fair value as described by IIROC it its Notice on Form 1.

Consolidated statements (Proposed Rule 3842)

The Proposed Rule sets out the requirements relating to consolidated statements. IDA MR Notice 0087 clarifies that the "consolidated monthly statements could include the customer's full trading and portfolios, including transactions done and/or positions held at the Member, non-member affiliates of the Member, and in customer name at non-related locations such as mutual fund companies" and could also be for showing "both the introduced business and the business handled in-house".

We would like clarification as to what type of transactions the proposed section applies to and whether "consolidated statements" should include accounts held at IIROC regulated entities only.

The Working Group would also appreciate guidance as to what is meant under Proposed Rule 3842(4) with respect to including a reference on the consolidated statement to the "Dealer Member's legal entity statement" and asking clients to ensure this statement is accurate and to report any discrepancies to the auditors.

Proposed Plain Language Rule 3900 (Supervision)

Proposed Rule 3925 states that "Dealer Members must appoint one or more alternate Supervisors to assume the responsibility of the designated Supervisor in his or her absence." The Working Group was under the assumption that IIROC was moving away from requiring alternates and that this issue would be decided by firms internally as to how they would structure their supervision. Clarification on this point would be appreciated.

The Working Group would also appreciate clarification as to why the anti-money laundering requirements currently under Rule 2700 IV. B(5) have not been included in the Proposed Rule.

Institutional Accounts (Proposed Rule 3960)

Proposed Rule 3960 states that the Dealer Member must have policies and procedures on the supervision of institutional accounts designed to detect improper account activity including "trading in securities that have restrictions on transfers." As there is no

prohibition under Canadian securities legislation for trading securities which have restrictions on transfers and institutional clients often trade in "144A" securities or "Reg S" securities which have restrictions on transfers, the Working Group would appreciate if IIROC would remove this Subsection.

The Proposed Rule does not specifically require that the policies and procedures on supervision of institutional accounts be designed to detect "transactions raising a suspicion of money laundering or terrorist financing activity", which is provided under current Rule 2700IV.B(5). We are seeking clarification as to why the anti-money laundering requirements are not expressed in the Proposed Rule.

Managed Accounts (Proposed Rule 3970)

Proposed Rule 3970 now requires Dealer Members to appoint one or more Directors or Executives to be responsible for the supervision of managed accounts. The Working Group questions why this requirement has been added and whether this would not be more appropriately dealt with by supervisors.

Execution only trades in advisory accounts (Proposed Rule 3981)

Proposed Rule 3981(2) requires a Dealer Member to review execution only trades in advisory accounts and the Working Group seeks clarification on the timeframe for the review to take place.

Conclusion

The IIAC and our Working Group hope that our comments will be considered in finalizing the Proposed Rules. We would be happy to meet with IIROC staff to discuss these matters further.

Yours sincerely,

"Deborah Wise"

Deborah Wise
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