CONFLICTS OF INTEREST EXAMPLES: SELF-ASSESSMENT TOOL TO HELP MEMBERS OF INVESTMENT INDUSTRY ASSOCIATION OF CANADA (IIAC)

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INVESTMENT INDUSTRY ASSOCIATION OF CANADA

ASSOCIATION CANADIENNE DU COMMERCE DES VALEURS MOBILIÈRES

Disclaimer
The information and examples contained in this document are to help IIAC members meet the requirements under Rule 42 of the IIROC Client Relationship Model dealing with conflicts of interest. The conflict of interest examples included in this document are not intended to be all-encompassing, as the types of conflicts that can arise may be unique in each situation. Determining all conflicts of interest that may exist is ultimately the responsibility of each Investment Industry Regulatory Organization of Canada (IIROC) member firm. Members must be in full compliance with regulatory requirements and ensure that written policies and procedures are developed to identify and address material conflict of interest situations and that these policies and procedures are maintained and followed.

The table below lists a series of examples of conflicts of interest collected by PWC Canada, which has kindly agreed to their use in this tool prepared by the Investment Industry Association of Canada (IIAC) for IIAC member conflicts of interest identification and self-assessment purposes.

The table can be used:

i. simply as a list to test the conflicts of interest a firm already identified or
ii. as a simple worksheet to help record which conflicts are material and which are not, as well as why, or how the decision was reached **(Columns 2, 3 and 5)** or
iii. as a way to weight certain aspects of the material risks to help prioritize ones that may warrant most attention for purposes of building compliance controls **(Columns 2, 3, 6 and 7)** or identifying where training and communication /reminders may be most needed (for example, where investment advisors may come up against such conflicts rarely **(Columns 2, 3, 6 and 7)**.

For each possible conflict of interest, and for those not captured here that may be identified by an IIAC member firm and recorded in the space provided, a member firm may change the weighting assigned to best suit their purposes **(Columns 4, 6 and 7)**. For example, some firms may feel that ongoing conflicts that can be managed by systems or supervision may be less challenging than ones where disclosure is required in the case of a rarely arising conflict. As with any model, members are encouraged to use caution and to test findings under various scenarios.

Column 1	*Column 2*	*Column 3*	*Column 4*	*Column 5*	*Column 6*	*Column 7*	*Column 8*
Conflict	**Description**	**Risk?** *1=Yes* *0=No*	**Material?** *Yes* *2* *No* *1*	**Why *Not* Material?**	**Conflict …** **Ongoing** *1* **May Exist** *2*	**Conflict … Avoid** **0** **Manage** *1* **Disclose** *2*	**Weighting** *Column 3x4x6x7*
Bundling	1. Retail clients pressured to buy additional services on unfavourable terms to obtain access to particular product (e.g., consumer lending product linked to purchase of the firm's insurance product).	1	2		1	2	**4**
	2. Broker, in return for trading commission, supplies a package of services to a fund manager, such as research, computers, premises, etc. on the basis of an understanding of the level of business.	0					0
Cherry-picking	3. Firm provides new recommendation to a selected group of customers in anticipation of planned revisions to long-standing recommendations.	1	2		2	1	**4**

Note: Firms must obtain their own advice on conflicts of interest matters based on the facts of their business model client base and any other relevant factors.

CONFLICT OF INTEREST EXAMPLES AND WORKSHEET

Column 1	*Column 2*	*Column 3*	*Column 4*	*Column 5*	*Column 6*	*Column 7*	*Column 8*
		Risk?	Material?		Conflict …	Conflict … Avoid 0	Weighting
Conflict	Description	*Yes* 1	*Yes* *2*	Why *Not* Material?	Ongoing *1*	Manage *1*	*Column 3x4x6x7*
		No *0*	*No* *1*		May exist *2*	Disclose *2*	
Bundling	1. Retail clients pressured to buy additional services on unfavourable terms to obtain access to particular product (e.g., consumer lending product linked to purchase of the firm’s insurance product).						
	2. Broker, in return for trading commission, supplies a package of services to a fund manager, such as research, computers, premises on the basis of an understanding of the level of business.						
Cherry-picking	3. Firm provides new recommendation to a selected group of customers in anticipation of planned revisions to long-standing recommendations.						
	4. Firm chooses to finance its best customers by means of bank loans while underwriting securities for weaker clients.						
Churning	5. Sales agent undertakes multiple (unnecessary/unauthorised) transactions in client’s discretionary account to generate commission revenue.						
Competitive syndicate	6. Roles and responsibilities of syndicate members are not defined until later in the process creating pressure points around pre-deal research and marketing activities.						
Conflicting roles	7. Firm represents bond holders of a distressed company while also representing a prospective acquirer of that same company.						
	8. Firm represents both a buyer and a seller in an M&A deal.						
	9. Research department issues positive report after firm appointed lead manager in an IPO.						
	10. Sell-side analyst helps to attract and retain clients of the investment banking department.						

Column 1	Column 2	Column 3		Column 4		Column 5	Column 6		Column 7		Column 8
		Risk?		Material?			Conflict …		Conflict … Avoid	0	Weighting
Conflict	Description	*Yes*	1	*Yes*	*2*	Why *Not* Material?	Ongoing	*1*	Manage	*1*	*Column 3x4x6x7*
		No	*0*	*No*	*1*		May exist	*2*	Disclose	*2*	
Fees and commi-ssions	11. Broker pays more to ensure volume of client referrals (soft commissions).										
	12. Management fees charged to funds are disproportionate.										
	13. Inappropriate or inconsistent allocation of costs to funds.										
	14. Financial advisor network remunerated solely through commissions (i.e. does not charge for services).										
	15. Brokers direct customers to selected firms which make special payments (above normal) for volume (contingent commissions).										
	16. Firm offers financial advisor a fee to switch existing clients from a competitor's product to its own.										
	17. Firm pays a fee to financial advisor over and above normal commissions to ensure the inclusion of its products on the advisor's approved products list.										
Fiduciary duty	18. Retail sales agent does not (or is not perceived to) provide best advice to the client based on information available (or believed to be available) within the firm.										
	19. Financial advisor recommends that client replace existing products (e.g., wrap accounts) with similar products of its parent company (or other group company) in order either to reduce administration effort or to generate additional commission.										
	20. Firm adopts inconsistent approach to the selection and monitoring of brokers (potentially showing favour to certain brokers, or incurring additional, unnecessary costs for clients).										
	21. Parent company provides asset management services to a fund. The fund is not in a position to appoint different asset manager if the asset management services are not satisfactory.										

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		Risk?		Material?			Conflict …		Conflict … Avoid	0	Weighting
Conflict	Description	*Yes*	1	*Yes*	*2*	Why *Not* Material?	Ongoing	*1*	Manage	*1*	*Column 3x4x6x7*
		No	*0*	*No*	*1*		May exist	*2*	Disclose	*2*	
	22. Fund manager simultaneously manages hedge funds and registered funds.										
Front-running	23. Client issues a large buy order for Company Y: firm buys shares in Company Y ahead of client to take advantage of price increase.										
	24. Firm trades ahead of client to take advantage of pending favourable report prepared by the firm's research department/analysts.										
	25. Proprietary trading desk buys shares in Client X based on information from Corporate Finance that Client X will be bought by Company Y.										
	26. Salesperson informs colleague in fund management about large client order in Company Y. Fund manager purchases shares in Company Y for placement in the fund.										
Induce-ments	27. Employee accepts a gift from a customer which could compromise or give the impression of compromising his/her independence.										
Laddering	28. Firm offers shares in an IPO that it underwrites to 'preferred clients' with the understanding that they will purchase more shares at a specified price after the company begins trading publicly.										
Manage-ment/ director interlocks	29. Firm's officers and/or directors have seats on boards/committees of client companies.										
	30. Cross directorships of subsidiaries.										
Market manipula-tion	31. Intra-company dealing to boost book or to create demand perceptions.										
	32. Creating fake bids to give the perception of a competitive market (bid rigging).										
Market timing/late trading	33. Practices which enable firm to shift wealth from other investors to preferred clients (e.g., hedge funds).										

Column 1	Column 2	Column 3		Column 4		Column 5	Column 6		Column 7		Column 8
		Risk?		**Material?**			**Conflict …**		**Conflict … Avoid**	**0**	**Weighting**
Conflict	**Description**	*Yes*	1	*Yes*	*2*	**Why *Not* Material?**	**Ongoing**	*1*	**Manage**	*1*	*Column 3x4x6x7*
		No	*0*	*No*	*1*		**May exist**	*2*	**Disclose**	*2*	
Material interests	34. Firms fails to act in the customer's best interests when firm holds a material interest in a given transaction.										
	35. Firm fails to disclose a material interest in another firm which influences a buying decision (e.g., research firm) or which executes transactions (broker).										
	36. Separate customers with material interests which conflict.										
	37. Firm agrees to buy business of financial advisor on a 'last resort' basis, with the purchase price based on a multiple of annual commission.										
Misuse of confidential information	38. Firm acts, or appears to act, based on non-published confidential information not known by, or regarding, the customer.										
	39. Underwriting department sells shares aggressively to customers of the bank in order to benefit issuers.										
	40. Bank with loans to customer whose credit risk deteriorates, sells corporate bonds to the public, thus paying off the loan and earning a fee.										
	41. Firm pushes affiliates products to the detriment of customers.										
	42. Corporate finance uses confidential information on Client X to provide advice to Firm Y, a competitor of X in which the firm has made a venture capital investment.										
	43. Loan and/or credit derivatives trader obtains information that borrower/credit position is deteriorating and uses information to sell position.										
	44. Credit officer uses information from workouts group to request that debt trader reduce his position in distressed client's debt.										

Column 1	*Column 2*	*Column 3*		*Column 4*		*Column 5*	*Column 6*		*Column 7*		*Column 8*
	Description	Risk?		Material?		Why *Not* Material?	Conflict …		Conflict … Avoid	0	Weighting
Conflict		*Yes*	1	*Yes*	*2*		Ongoing	*1*	Manage	*1*	*Column 3x4x6x7*
		No	*0*	*No*	*1*		May exist	*2*	Disclose	*2*	
	45. Firm acts or appears to act based on relevant/confidential information not known to other parties in a merger or acquisition.										
	46. Trader has access to confidential information on Client X and uses it to sell short the company’s stock in advance of notice of poor performance.										
	47. Trader buys shares in Client X based on information gleaned from Corporate Finance that Client X will be bought by Company Y.										
	48. Sell-side analyst includes confidential information obtained from Corporate Finance within research report.										
	49. Cross-selling opportunities compromise client privacy through misuse of personal information.										
Non-disclosure and poor disclosure	50. Asset manager does not report, or incorrectly/incompletely reports, investment performance to clients or potential clients.										
	51. Tied agents do not adequately and clearly disclose their relationship with investment firm to clients and the impact that this relationship has on the advice/product offerings to the client.										
	52. Disclosures made to clients are obfuscated by being too legalistic, long-winded or presented in such a way as to discourage the client from fully understanding them.										
Personal account dealing	53. Firm’s employee acquires or sells shares on personal account based on non-public information held by the firm.										
	54. Employee uses personal account to deal ahead of large customer order.										
	55. Employee uses personal account to deal in advance of research publication.										

Column 1	Column 2	Column 3		Column 4		Column 5	Column 6		Column 7		Column 8
		Risk?		Material?			Conflict …		Conflict … Avoid	0	Weighting
Conflict	Description	*Yes*	1	*Yes*	*2*	Why *Not* Material?	Ongoing	*1*	Manage	*1*	*Column 3x4x6x7*
		No	*0*	*No*	*1*		May exist	*2*	Disclose	*2*	
	56. Research analyst undertakes a personal account transaction which is contrary to research recommendation or advice given to clients.										
Preferential treatment	57. Firm's officers/directors receive company loans at preferential rates.										
	58. Certain customers' orders are given priority over other customers' orders.										
	59. Account executives favour one type of customer over another (e.g., discretionary and advisory client) in allocating an over-subscribed stock.										
	60. Research department issues (or is perceived to issue) 'buy' recommendations only for listed entities with which the firm has a commercial relationship.										
Private interests	61. Directors and executives invest in company-managed private funds.										
	62. Individual managers take part, in parallel with their firms, in syndicates through private partnerships/companies.										
Remuner-ation/ rewards	63. Managers focus on revenues of own business to the detriment of other businesses within the organisation.										
	64. Managers focus more on short-term revenues to detriment of longer-term investment objectives of shareholders/policyholders.										
	65. Staff given incentives to sell complex 3rd party or in-house products which may not be appropriate for their clients.										
	66. Sales staff generating commission revenue to boost bonus.										
	67. Individual traders over-expose the firm due to excessive risk appetite.										
	68. Uncontrolled dispensation is given to 'star trader' in terms of internal controls/trading restrictions.										

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Conflict		*Yes*	1	*Yes*	*2*		Ongoing	*1*	Manage	*1*	*Column 3x4x6x7*
		No	*0*	*No*	*1*		May exist	*2*	Disclose	*2*	
	69. Traders book fictitious trades to an affiliate to boost bonus pool.										
	70. Sell-side analyst compensation linked to providing favourable client research.										
	71. Sell-side analyst compensation is linked to success of corporate finance deal (e.g., loan, underwriting).										
	72. Investment bank provides credit facilities to client without due regard to credit risk profile for organisation as a whole.										
Side arrange-ments	73. Deals contingent on buying debt or equity in customers or third parties.										
Spinning	74. Firm involved in IPO allocates shares to officers and directors of client firms on understanding of obtaining future business.										
Stuffing	75. Allocating securities from an undersubscribed IPO to the firm's discretionary retail accounts.										
Suitability	76. Firm sells complex structured derivative to client's treasurer without explaining the risks or understanding the client's needs/ sophistication.										
	77. Firm recommends that a customer frequently buy/sell riskier securities (even when not in the customer's best interest) as such securities generate higher commissions.										
	78. Investor advisor (in-house/agent) has interest in persuading client to invest in a product which is unsuitable in terms of the client's investor objectives.										
	79. Firm raises money for one client through securitisation and sells residual tranche ('toxic waste') to retail clients.										
Trade aggrega-tion/	80. Firm aggregation/allocation favours one customer over another.										

Column 1	*Column 2*	*Column 3*	*Column 4*	*Column 5*	*Column 6*	*Column 7*	*Column 8*
Conflict	**Description**	**Risk?** *Yes* 1 *No* *0*	**Material?** *Yes* *2* *No* *1*	**Why *Not* Material?**	**Conflict …** **Ongoing** *1* **May exist** *2*	**Conflict … Avoid** 0 **Manage** *1* **Disclose** *2*	**Weighting** *Column 3x4x6x7*
allocation	81. Firm aggregates client trade to the disadvantage of the customer.						
	82. Firm allocates trade to itself, or a member of its group, ahead of clients.						
Trade execution	83. Non-sequential execution of customer trades (allowing one 'preferred' customer to trade first).						
	84. Firm executes trade with own affiliate prior to that of customer.						
	85. Firm fails to identify/correct trade errors and does not pay/reimburse customer appropriately.						
	86. Firm fails to follow client instructions on a market transaction or delays in making payment in order to increase float.						
Tying	87. Firm uses its power to influence a client to also use other services (e.g., firm denies credit to customers who refuse to use securities, advisory, insurance services).						
	88. Firm makes below market loans to third-party investors on condition that proceeds are used to acquire securities underwritten by its corporate finance unit.						
Undue influence	89. Allowing a relationship with a 3rd party (with a material interest) to compromise actions on behalf of a customer in a transaction.						
	90. Underwriters exert undue influence on (in-house) analysts to provide favourable research.						
	91. Corporate Finance (or similar) has ability to influence outcome of draft research prior to publication.						
	92. Undue pressure exerted by senior editorial body (or other) to change research message in order to support the client's specific interests (for example, in order to protect a client facing a hostile takeover).						

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		No	*0*	*No*	*1*		May exist	*2*	Disclose	*2*	
	93. Preference for 'buy' recommendations (note: all clients can buy, on existing shareholders can sell).										
	94. Sell-side analyst is encouraged to make recommendations which support proprietary trading.										
	95. Analysts face pressure from institutional investor clients to create profitable investments.										
	96. Client pressurises the firm into not issuing a negative recommendation based on difficulties the client is currently facing.										
	97. Issuer's management retaliate against a bad report by cutting off analyst's access to management: issuer carries ill-will against the analyst and in turn against the broker-dealer for whom the analyst works.										
	98. Market 'herd' mentality leads to overly optimistic or pessimistic research expectations/requirements from management.										
	99. Asset management unit pressured by corporate banking client with shares in that company into voting for management's position in a contested corporate action (e.g., proxy battle).										
Unfair pricing	100. Under-pricing new issue to generate additional sales revenues.										
	101. Over-pricing new issue to generate additional corporate finance fees.										
Additional	102. Sharing accounts with a client										
	103. Refusing all first client complaints on the basis many may not take the matter further										
	104.										
	105.										

**WORKSHEET FOR FIRMS WITH
MORE COMPLEX ORGANIZATIONAL STRUCTURES,
E.G., SUBSIDIARIES AND AFFILIATES**

Note: Use examples above, inserting

[Please tick as appropriate]

##	Conflict		Potential risks	Potential causes	Risk within my organisation	Potential risk within my organisation	Not a risk in my organization	Laws/regulations prohibit this

Which business(es) does this impact?

[Please tick (✓) as appropriate]

Retail bank	Commercial banking/ corporate finance	Investment bank/Dealer	Broker/sales agent	Asset manager/ investment fund	Investment analyst	Insurance company	Insurance intermediary	Other

	Structural Arrangements				Policies and Procedures									
What arrangements do you have in place to manage this risk?	*Separate subsidia-ries*	*Separate department*	*Physical separation of potentially conflicted activities*	*Reporting lines*	*Information flow restrictions (Chinese walls)*	*'Crossing the wall' policies*	*Temporary Chinese walls for specific transactions*	*Non-sequential and non-simultaneous involvement of conflicted individuals*	*Personal account dealing*	*Invest-ment*	*Ethics and confident-iality*	*Remun-eration/ reward*	*Escala-tion*	*Conflicts disclo-sures*
[Please tick as appropriate]														

Additional Arrangements								
Transaction monitoring/ restricted lists and watchlists	*Compliance monitoring*	*Independent price verification*	*Exception reporting/ reporting triggers/ complaints monitoring*	*New business approval mechanisms (including legal & compliance sign-off)*	*Legal contracts*	*Conflicts management/monitoring system(s) [Technology]*	*Employment contracts/staff confirmations*	*Training programmes*

Other (please specify)