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Dear Sirs:

**Re: IIROC Concept Paper – Lower Minimum Capital Requirements**

The Investment Industry Association of Canada (the “IIAC” or “Association”) appreciates the opportunity to comment on the Concept Paper.

The Association supports initiatives that appropriately target regulation and the scope and frequency of member reviews, based on criteria that clearly links the requirements to the risk presented by the registrant’s business model or conduct.

While the proposal to reduce capital requirements for Type 1 and 2 Introducing Firms attempts to apply such a risk-based approach for certain firms, there are a number of factors at play that render this approach ineffective and potentially at odds with the regulatory intent.

Although the classification of introducing brokers based on their access to, or ability to handle cash or securities does have some bearing on their risk profile, it is not the only, or even the most important factor to consider when assessing a firm's risk profile. A firm's inherent risk has more to do with the type of business it conducts, rather than its introducing category.

For instance, if a firm's business is based on a pure wealth management model, the risk will be lower than those firms that engage in proprietary trading, international trading, corporate finance, or other international business, or those that permit direct access to clients (including High Frequency Traders) or trade through their own Participating Organization number.

In respect of the minimum capital requirements, our members note that the stated minimums do not represent the actual capital requirements imposed by IIROC and by carrying firms. In practice, existing member firms and IIROC firm applicants are subject to IIROC's discretion, which generally results in a capital requirement that exceeds the regulatory minimum, in order to be approved for IIROC membership or carry on business as an IIROC member.

In addition to the IIROC capital requirements, carrying firms demand additional deposits for certain lines of business that they deem to carry a higher risk profile. In the process of assessing this "collateral cap", carriers will consider the capital requirements imposed by IIROC. As such, any reduction in the minimum capital requirement is likely to be counterbalanced by an increased collateral cap, negating any potential benefit.

It would be helpful to understand if there are particular issues or circumstances that this initiative is intended to address. If the initiative is intended to reduce the number of firms in early warning, we believe that this will only address this in the short term, as firms that consistently operate in this realm will likely draw down their capital and be left with a smaller capital cushion. This unintended consequence would erode investor protection and is potentially harmful to the market integrity of the industry and investor confidence.

For the reasons expressed above and in response to the questions posed below, the IIAC does not support a reduction of the minimum capital requirements, as it is likely to introduce more risk to the IIROC brand without commensurate benefit.

### **IIROC Consultation Questions**

- (i) Do the existing minimum capital requirements for Dealer Members that handle client assets on a limited basis, if at all, represent an undue regulatory burden for such Dealer Members? If so, what minimum capital requirement amount would be more appropriate? Would a lower minimum capital requirement**

**amount materially reduce that burden, or are there other issues that are more critical?**

The minimum capital requirements for Type 1 and 2 Dealer members does not represent an undue regulatory burden. The existence of higher standards in this regard for IIROC dealers versus other registrants is appropriate, and is consistent with the higher degree of investor protection provided by an IIROC dealer. Given that there is no beneficial counterbalance to the potential erosion of investor protection, a reduction in the minimum capital requirement is not in the best interest of the industry or the public.

The significant and arguably excessive regulatory burden on IIROC dealers is a result of initiatives and obligations such as multiple market regulation which effectively requires members to connect to all marketplaces regardless of their value, unregulated data costs, the CRM (particularly the elements of risk profiling and performance disclosure) as well as the constant onslaught of regulation that requires significant technical investment without clear investor benefits. As an example, UMIR 7.13 DEA rules have required a significant effort to create different legal agreements for the various types of market access arrangements and will continue to generate ongoing costs in order to tag every order with a unique ID that is specific to DEA clients. This has been particularly burdensome on carriers and institutional dealers for what appears to be of little benefit.

The problem is compounded by the near continual audits conducted by IIROC's Business Conduct, Financial Operations and Trade Desk departments and other regulatory bodies including FINTRAC, provincial regulators, as well as the redundant section 5970 audit. Preparation and response to the audits requires significant resources and it is not clear that the frequency and scope of these audits are in any way linked to risk.

**(ii) Is it appropriate that IIROC Dealer Members, whose business activities and risk profiles are comparable to those of registrants on other platforms (e.g., MFDA and CSA), are subject to significantly higher minimum capital requirements?**

As noted above, the minimum capital requirements do not represent a significant burden, and are appropriate for the investment dealer business. If capital requirements are to be differentiated based on risk, it should reflect the risk of the business model, not merely the ability of the firm to handle cash and securities. The capital requirements ideally should be raised for the other registrants, rather than lowered for IIROC dealers.

**(iii) Do the existing minimum capital requirements for Dealer Members that handle client assets on a limited basis, if at all, represent an inappropriate barrier to entry for potential new IIROC Dealer Members?**

The minimum capital requirements for Dealer Members is not, and should not be a barrier to entry for potential new IIROC dealer members. The existing standards are not overly burdensome, and differentiate IIROC firms from registrants that have lower standards. In addition, as discussed above, potential entrants are generally subject to higher requirements by both IIROC and carrying firms.

Further, given the significant and ever increasing regulatory costs of being an IIROC member, the capital requirements are not a material factor in respect of the initial or ongoing costs of IIROC registration. As noted above, the issues relating to a non-level regulatory environment, and the current erosion of the small dealer base and expansion of EMDs is not related to minimum capital requirements, but the substantial and increasing expenses for regulatory compliance relating to firms' ongoing business. As such, lowering the minimum capital requirement will not have a material effect on keeping existing IIROC members or attracting other registrants to the IIROC platform.

**(iv) Would a lower minimum capital requirement amount for Type 1 and Type 2 introducing brokers result in a greater alignment with risks associated with this category of Dealer Members?**

See our response above.

Thank you for considering our comments. If you have any questions, please do not hesitate to contact me.

Yours sincerely,



Susan Copland

