



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

DOWN THE RABBIT HOLE

**RULES, REGULATIONS, AND
RESPONSE OF THE IIAC**

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DOWN THE RABBIT HOLE RULES, REGULATIONS, AND RESPONSE OF THE IIAC

Good morning. I'm delighted to be here at the NBCN'S
Empowering You Conference.

I want to begin by reminding you of the story of Alice in
Wonderland. Alice as you know fell into a rabbit hole, and found
herself in a world that was quite strange.

It was a world where authority figures abounded.

The lowly Mouse said: "Sit down, all of you, and listen to me."

The Dodo gave orders about the caucus race.

The Queen held a Croquet Tournament in which she shouted "Off
with their heads."

The King presided over an unruly courtroom and threatened to
behead those who got out of hand!

It was a world where there was a rule and a punishment for
everything. No wonder Alice laments: "I was never so ordered
about in all my life, never!"

Some of us may feel that way in the Canadian securities industry.
There does seem to be a rule for almost everything. And while
execution is not the order of the day in our industry, securities
companies do have to obey a heavy set of rules and devote huge
resources to doing so, when in fact their efforts would be better
spent on their business. No one knows that better than you, who

are the very administrative officers who have to deal with these heavy rule books.

So what's the IIAC doing about it? That's what I am here to talk to you about today. The Investment Industry Association of Canada, is now completely independent from IDA. We are the voice of the industry. We are dedicated to ensuring that the regulatory environment in which our members operate supports their business.

In fact, the message I bring you is this: we are doing everything we can to ensure that you are spending less time on regulatory rigmarole and more time on growing your business.

How are we doing it? I'd like to share five ways.

1. Streamlining Client Relations

The *first* way the IIAC is helping members get on with their business is by encouraging the Investment Dealers Association to streamline its client relations model.

Over a year ago, the IDA put forth a new Client Relationship Model (CRM) to provide more detailed rules around how brokers interact with clients. Of course there were already rules for this. But the regulator wanted to leave nothing to chance. Every aspect of the client-advisor relationship would be spelled out.

When the IDA produced the new rules they encouraged comments and open consultation with the industry. So we took the draft rules to our members. We asked them what they thought and what, if anything, needed to be changed about the rules governing client-broker interactions. We listened, and took note of specific concerns.

What we heard was that members found the proposed rules impractical. Take for instance the Relationship Disclosure Document. Our members didn't see a need for it. Advisors felt they were already very clear in explaining their relationships with their clients. For example, they were already explaining to clients how they as brokers were being compensated and whether there were any conflicts of interest. They didn't need more rules to govern those procedures. Rules on top of rules.

Besides, explaining this Relationship Disclosure Document to their clients would take more time...wasted time. . . And they felt that adding this measurement would be far too complex from an administrative standpoint. They also had concerns about cost, and assumed that new costs would ultimately be borne by clients. They felt that the implications of this new form of reporting hadn't actually been fully considered by the regulator. Finally, there would probably be a high cost in implementing this new process. The regulator did not conduct a cost-benefit analysis before drafting these new rules. The regulator had promised to do this

analysis *after* the rules were introduced. That sounds backwards doesn't it? We thought so.

In fact, the whole thing, as Alice might have put it, seemed *curiouser and curiouser!*

So this April we responded to the IDA's Client Relationship Model with a letter that highlighted these member concerns. We suggested the IDA adopt a more "principles-based" type of regulation. We believe that the current regulatory system in Canada contains too many detailed rules around the advisory relationship with clients and around how firms carry out their business. This heavy focus on rules limits the way firms can service their clients. And it forces everyone to focus on minute details instead of exercising judgment to achieve the best results for clients.

So rather than having every single little iota of conduct examined in detail by the regulator, a statement could be drawn up that states how a firm is supposed to behave and conduct its business with care, skill and integrity. That way, the regulator can use its discretion with firms that are playing by the rules, and get tough with the ones that are abusing the principles.

The good news is that because of the strength of our argument, the CSA staff has agreed to have the whole Client Relationship Model

reviewed by the chairs of the commissions. And it has agreed to consider other options before proceeding.

That's a victory for us and for members. We're proud of that win! But that's only one of the areas of regulation we've been addressing.

2. Simplifying Registration in Canada

The second way the IIAC is helping you, our members, is by working to simplify the rules governing registration of firms and brokers in Canada.

The present system doesn't make sense to us....and I don't think it makes sense to member companies. It requires that you register your firm....and its brokers...in every single Canadian province in which you conduct business. Let's say you have an advisor with clients in Ontario...and one of those clients moves to Alberta...If you want to keep servicing that client your firm and the broker have to register in Alberta just to maintain that relationship. Yet regulations in both provinces are virtually the same! Why force firms to register and spend the time and money required to do so when nothing changes?

Let me give you an example. One of our member firms is based in Winnipeg. It draws many of its clients from the local military and RCMP. Many of these armed forces and police services clients move around a lot. That means every time one of these clients is

transferred...this Winnipeg brokerage firm incurs significant registration costs to follow the client to the new province. And as a firm, they find those costs difficult to bear. Who pays the price? The firm itself... and ultimately its clients.

The IIAC feels that this is a poor use of resources. We wanted to let the regulator know that this is unacceptable. So last June we wrote a detailed letter to the Canadian Securities Administrator, or CSA, expressing our views. The CSA was taking a harder look at streamlining many of the rules that govern the industry, including the mobility of advisors between provinces, and they had requested our input. We sent this letter in the hopes of encouraging the regulator to work with us to find a good solution to this issue. We are awaiting the results, and hope that when they issue their updated proposal toward the end of this year, they will see a new and better approach.

In the meantime, do everything you can to keep your clients from crossing provincial borders!

3. Streamlining Canada-U.S. Business

A third and related issue we are working on is the regulatory policy governing securities firms engaged in U.S. business. The IIAC is working to minimize regulatory costs for Canadian firms doing business with U.S. institutional investors.

Let me explain.

Right now, Canadian-based independent firms that carry out institutional business in the U.S. are required by the regulator to have a U.S. subsidiary that's registered with the Securities and Exchange Commission in the United States. This subsidiary can operate in the same premises and with the same employees as the parent firm in Canada. So there is no infrastructure cost.

The problem lies in the fact that as a separate entity, the U.S. subsidiary must have a separate pool of capital for broker dealers. SEC regulation doesn't allow the subsidiary company to just draw on the funds of the Canadian parent. It has to have a separate pool of money for its U.S. business. How much? We have many institutional firms with \$10-50 million in capital focused in the U.S. institution marketplace. Requiring a separate capitalized affiliate to conduct the U.S. business limits the clients they can deal with and the business carried out.

And it is a double-edged sword: if a firm doesn't reserve substantial amounts of money for the U.S. sub, it loses its chance at U.S. business. But, if it allocates the money to the U.S. subsidiary, it has less money to run its business at home. This is a huge concern for our boutique firms as they don't have a huge amount of capital to begin with.

There are also costs of registration to worry about. Employees of the subsidiary firm need to be dually-registered in Canada and the U.S. Registering advisors in the U.S. is an expensive process for these firms. Once they're registered, they need to be trained. And training is ongoing, so this isn't a one-time fee. You see how the costs keep adding up.

Clearly, having to comply with two regulatory regimes is far too costly for many of our members looking to do business in the U.S. I understand there are five firms on the NBCN platform that have U.S. subsidiaries. I say, we're here to help!

So what have we done?

IIAC approached the SEC early this year and expressed our concerns. That led to formal meetings in July between the SEC and IIAC, where we shared these views - your views - in greater detail. Then, in September, we submitted a formal proposal to the SEC titled "Proposal for Mutual Recognition," outlining how our members would benefit from more liberal regulatory treatment in the U.S.

In the proposal, we got to the heart of mutual recognition. We encouraged the SEC to do away with the requirement for dual-registration of our firms, and to recognize our Canadian regulatory system as certainly being good enough for them. Think about it,

our regulatory structures are very similar, our business relationship is long and strong and we speak the same language. And let's not forget we have a free trade deal!

If mutual recognition happens, the benefits to our industry would be huge. It will remove the duplication in costs and free up Canadian firms to do business with U.S. institutional investors as they do with Canadian ones. Our dialogue with the Securities Exchange Commission is ongoing and we're confident that mutual recognition will happen for institutional firms.

4. Developing Best Practices and Tools for the industry

The fourth way the IIAC is helping our members is by developing a set of "best practices." Why should every firm "go it alone?" We believe that as a trade association, we can and *should* develop these best practices for our members. This works better than leaving it to each firm whenever new rules and regulations are tabled.

We have already begun creating best practices templates. For example, the IIAC is developing a model process for non-brokered private placements. The template ensures that advisors meet all their obligations to clients when doing these transactions. Basically, it sets out due diligence practices when selling a deal that has originated privately and arrived through a non-registrant.

We've also developed a best practices handbook called *Equity Capital Markets New Issue Practices*. Earlier this year the IIAC led a task force responsible for going through the existing handbook and updating it to reflect today's industry.

The handbook gives dealer participants in underwriting syndicates a clear set of best practices to follow during an underwriting transaction. It's for the use of all our members but particularly valuable for boutique firms participating in an underwriting syndicate with larger firms and for those firms doing underwriting on their own.

This Handbook will do several things:

1. Make the underwriting process as efficient as possible.
2. Give member firms a better understanding of their responsibilities and liabilities when participating in underwritings. And...
3. Make the process relevant to today's securities business.

We received a lot of valuable input from the task force, and we believe our members will strongly benefit from using it. Please visit the IIAC website for a copy.

So we've created best practices, and will continue to do so, making sure that individual members will not have to "reinvent the wheel."

In addition, to help firms comply with National Instrument (NI) 24-101, we have developed an institutional trade-matching page on our website which includes useful information and a collection of trade-matching statements. At the last count, we have over 250 trade-matching statements posted – that’s saving a lot of our members’ time and money. We are also working with the CSA to bring additional clarity and simplicity... and a bit more common sense... to the implementation of what is intended to be a principle-based rule.

And a final area where the benefits of simplification are only beginning to be felt, we are working with our members and our Tax Reporting Committee – to promote more automated ways of collaborating with CDS for information dissemination and less costly and impractical ways of interacting with the Canada Revenue Agency. A big win for us this year was the federal government’s decision to push back the date which trusts and limited partnership units must provide the data for T3s and T5013s. This will enable you and your carrying broker to get information to your clients more quickly and accurately.

But that’s not all.

5. Reducing Disclosure Materials

A fifth way IIAC is helping our members—and the final one I’ll be discussing today-- is by reducing the massive amounts of disclosure materials that have to be sent to clients.

Now I'm sure many of you in the room who manage the back offices are smiling, given the amount of this unnecessary paperwork that floods into your office every day. I'm sure it feels like it just never ends. It's nothing more than an information dump!

Mailing important material to investors *is* a good idea. But it has become too much of a good thing. Because issuers have discretion to send whatever materials they want to their shareholders, they dump this information on brokerage firms, who are obligated to send it to their investing clients.

I don't have to tell you what happens to a lot of this mail. That's right: it gets shredded. What also happens is that a lot of the good mail gets ignored along with the bad because there's just too much of it! Clients are annoyed, important messages get lost, trees die for all these mailings and all of you who run the back office are barely keeping up with all the paper.

As the voice of our industry, IIAC has written to the CSA expressing our willingness to work with them to reduce the amount of unwanted disclosure material our members have to provide their clients. In our submission to the CSA we said:

- The rules governing distribution of this material needs to be revised.

- A distinction should be made between documents that are important to all investors, such as proxy voting materials, and those that aren't.
- Issuers should not have to send information to dealer intermediaries for clients that have discretionary managed accounts.
- And advisers should have more freedom to oversee the flow of paper.

Whatever happened to the paperless office! You have my word: the IIAC will continue to work with the regulator to see that our clients are not flooded with unnecessary paper and that trees are not sacrificed in vain. We will press for a positive response.

Conclusion

As you can see, the IIAC is deeply committed to the success of our member firms, and has already taken on specific initiatives aimed at helping you reduce your regulatory burden and focus on growing your business.

You are a great audience to share these initiatives with. As introducer firms you have an extraordinary commitment to growth and business success. Over the past three years of the bull market, the introducer firm groups have outperformed the larger firms in terms of earnings, revenue and employment growth.

Clearly, you understand the need to keep your focus on business, not on the regulatory requirements that undermine business success.

There's no doubt that the regulator has a job to do. But our job at IIAC is to make sure that the regulator, in doing its job, doesn't prevent you from doing yours.

When it comes to unnecessary regulation I say: "Off with its head!"

Thank you for giving me this opportunity to share our vision and our commitment to you.



IAN C.W. RUSSELL, FCSI
President and Chief Executive Officer
Investment Industry Association of Canada

Ian C.W. Russell is President and CEO of the Investment Industry Association of Canada, a position he has held since the Association's inauguration in April 2006. Under Ian's leadership, the Association has successfully advocated for the industry on a broad range of regulatory and tax issues.

Previously, Ian headed the Industry Relations and Representation group of the Investment Dealers Association (IDA). His 20-year tenure at the IDA included resolving conflicts of interest around raising capital for small companies (The Hagg Committee), and setting standards for research analysts in the securities industry (The Crawford Committee). Before joining the IDA, Ian was a financial analyst for *The Bank Credit Analyst*, a respected international publication based in Montreal. He also spent six years at the Bank of Canada.

Ian has an honours degree in economics and business from the University of Western Ontario, and a post-graduate degree from the London School of Economics. He has completed the Partners, Directors and Officers Qualification Examination and is a Fellow of the Canadian Securities Institute.