

November 10, 2017

**Attention:**

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**RE: IIROC Proposed Provisions Respecting Client Identifiers**

The Investment Industry Association of Canada (“IIAC” or “Association”) appreciates the opportunity to provide comment on IIROC Notice 17-0109 (the “Notice” or “Proposal”) detailing proposed provisions respecting client identifiers. An industry working group of IIAC Member firms assisted in evaluating the Proposal.

Under the Proposal, IIROC would amend UMIR and Dealer Member Rules to require client identifiers on each order sent to a marketplace and each reportable trade in a debt security. The identifier would take the form of a Legal Entity Identifier (LEI) or, for clients not eligible for an LEI, their account number. The Proposal also includes new or amended provisions in respect of identifiers surrounding electronic trading.

The industry recognizes the potential benefits stemming to IIROC from the Proposal, namely improved surveillance, investigatory and data analysis capabilities. The IIAC also appreciates the potential benefits of the Proposal to Canadian markets broadly. In fact, the IIAC was an early proponent of the global Legal Entity Identifier system (“GLEIS”) and participated alongside other industry bodies during its initial

development. We understand, therefore, why regulators globally have increasingly turned to utilizing LEIs in carrying out their responsibilities<sup>1</sup>.

However, IIROC also correctly acknowledges in its Notice that the impacts of the Proposal on Dealer Members, marketplaces, investors and vendors may be significant to achieve compliance. It is imperative, therefore, that careful consideration be given on how to implement a client identifier framework without major disruption to market participants or market functioning.

### Industry Comments and Concerns

A review of the Proposal with our members revealed several areas of concern or in need of further clarification from IIROC.

1. IIROC proposes its Dealer Members ensure that eligible clients obtain LEIs as part of the onboarding process for new clients or as part of its account documentation review for existing clients.

Discussions with members provided us insight on the processes and work effort involved in meeting this requirement.

Firstly, IIROC Dealer Members would have to undertake a segmentation of all their existing clients and accounts to identify those eligible for LEIs. While the significant majority of the approximately 12 million customer accounts currently serviced by the Canadian brokerage industry<sup>2</sup> we believe are not eligible to obtain an LEI, IIROC Dealer Members will still have to conduct due diligence on their full account base to ensure compliance with the Proposal.

Furthermore, for some clients or accounts, eligibility for an LEI may not be easily discernable. While the global LEI system does not cover natural persons when they are acting in a private capacity, individuals acting in a business capacity may be eligible to obtain LEIs provided they conduct an independent business activity<sup>3</sup>. Some of our members' "retail" clients and accounts, therefore, may be caught in scope. Types of retail accounts that our members identified as warranting consideration include certain formal/informal trust accounts, numbered corporation accounts, investment club accounts etc. Given IIROC's understanding of these accounts is it IIROC's intent for such accounts to obtain an LEI?

We suspect our members may encounter strong push-back from any "retail" clients asked to obtain an LEI, likely resulting from the clients' unfamiliarity with the global LEI framework or from the out-of-pocket expense required to obtain an LEI.

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<sup>1</sup> A comprehensive list of regulations globally that require the use of LEIs is provided by the [Global LEI Foundation](#)

<sup>2</sup> IAC Estimate based on statistics from Corporate Insights, Retail Brokerage and Distribution Report, Winter 2017

<sup>3</sup> See LEI Foundation [Statement on Individuals Acting in a Business Capacity](#)

Requiring beneficial owners of these accounts to obtain and maintain an LEI may, therefore, represent a significant client service issue for our members that outweighs the benefits derived to IIROC. We therefore believe the Proposal, as currently worded, may be overly broad, inadvertently captures small retail clients that trade infrequently, and generally runs counter to the initial intent of the global LEI initiative.

It is also not clear from the Notice what the implications to the Dealer Member are in situations where the client: i) disagrees with the Dealer's assessment of the client's need for an LEI or ii) refuses to obtain an LEI or cannot obtain an LEI in advance of a trade. Is IIROC's expectation that the Dealer Members be prohibited from entering orders for the account or is there another alternative being contemplated by IIROC?

2. IIROC proposes that Dealer Members be required to ensure that client LEIs are renewed on an annual basis and do not lapse.

Our members are still working to estimate the total number of potential clients that would be required to obtain an LEI. Currently, approximately 24,000 LEI's have been issued by Canada.<sup>4</sup> We suspect a primary driver for some of these clients to obtain an LEI was their mandated use for trade reporting in OTC derivatives markets<sup>5</sup>. Expanding the scope of LEI to capture all debt and equity transactions could materially increase the numbers of clients requiring an LEI.

Given the potential large number of impacted clients, we believe it unreasonable to place the onus of ensuring LEIs are renewed annually by clients solely on the shoulders of the IIROC Dealer Member. This should be a shared responsibility. Clients should have the primary responsibility of ensuring their LEIs remain current. Local Operating Units of the LEI system should also be proactively reaching out to entities whose LEI is about to lapse. The openness of the GLEIS also allows Regulators requesting the LEI information to have good visibility on lapsing LEIs and they too can potentially play a role in ensuring LEIs are maintained up to date. This is something the industry would like to explore further with IIROC.

3. For clients not eligible to obtain an LEI, IIROC proposes their account number be used as the identifier.

Members seek to better understand IIROC's intended use of client account numbers for monitoring investor market activity. Given that client account numbers differ from one dealer to the next, IIROC will not have full visibility on the marketplace activity of any given individual with accounts across multiple dealers. In absence of the rationale, members have questioned, whether the benefit to IIROC justifies the additional industry expense for conforming to this requirement.

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<sup>4</sup> Source: Global LEI Foundation [website](#)

<sup>5</sup> Use of LEI for Derivatives Trading can be found in OSC Rule 91-507, MI 96-101, and other securities regulations.

4. IIROC seeks feedback on the potential industry costs stemming from the Proposal.

Without the detailed requirements, it is difficult for us to estimate the total industry costs stemming from the Proposal. However, we have attempted below to give you some sense of the magnitude of the industry efforts involved.

To meet the compliance requirements of the Notice, IIROC Dealer Members will have to undertake considerable systems enhancements. This can include updates to client management systems to include LEI information as part of the client profile and maintaining a firm wide database of LEI information. IIAC Members expressed most concern with respect to modifications to their order entry systems which may be required to capture the client identifier from a separate system or database and submit in encrypted format to marketplaces. These are core systems for our members and require special handling. Any changes to the systems, therefore, would also entail significant internal testing as well as testing with external partners such as marketplaces and service providers.

IIROC Members will also incur some direct and indirect costs as part of the client LEI registration/renewal process. Members will have to devote resources for client outreach to inform them of the new requirement for client identifiers and possibly educate them on the self-registration process for LEIs. We suspect that in some cases IIROC dealer members may have to facilitate an 'Assisted Registration' to obtain the client's LEI, potentially resulting in a direct cost to the dealer.

Furthermore, to accommodate the IIROC Proposal Dealer Members would also have to revise current account opening documents, such as the KYC, to capture LEI information where necessary. The process some members follow in revising their standard documentations can be lengthy, possibly as long as one year, as it typically requires collaboration with external partners such as print vendors. The costs of printing and shipping new account opening documents also needs to be considered. Providing a longer implementation period would allow IIROC Members to consume their existing stockpile of account opening documents before committing to new ones.

In its Notice IIROC rationalizes that the added costs to industry stemming from the Proposal will be offset, in part, by the reduced number of IIROC queries dealers will have to respond to. However, Members have been accustomed to such queries and have implemented policies and procedures for handling them efficiently and effectively without draining their resources. The Proposal will likely risk new types of queries being directed to the dealers, either from IIROC (resulting from the expanded data set) or clients seeking to better understand how their client account identification will be used and protected.

5. Our understanding of the Proposal is that the client identifier is required at time of order entry.

A major concern noted by Members is that for some transactions, the beneficial end client cannot be identifiable at time of order entry. For example, common industry practice is to operate "bulk" accounts for large institutional investors where the dealer executes a block transaction to purchase a large number of shares in a listed company and, then subsequently allocates the purchase to various sub-accounts of the client as instructed. Each sub-account can, in some cases, represent a separate

client or legal entity. A similar situation arises for retail investors who have opted for a professionally managed account in where the Investment Advisor may execute a block order which would later get distributed among the many client accounts sharing the same mandate. What is IIROC's expectations for the handling of such accounts for the purposes of meeting the requirements of the Notice? We do not see a policy rationale for looking through to the end-client in these situations given that the investment decision rests elsewhere. **The client identifier requirement should be rolled-up to the bulk-account level.** We believe this would be consistent with how dealers currently report under IIROC Rule 2800C *Debt Securities Transaction Reporting*. Any policy departure from IIROC could translate into material changes to dealers' debt transaction reporting systems.

6. The proposal requires all IIROC Dealer Members, including those that are non-Participants, to ensure all clients have an appropriate client identifier and that non-Participant dealers pass on the correct client identifier to their executing dealers.

This will have procedural and systems implications for IIROC Dealer Members operating under an introducing broker ("IB")/carrying broker ("CB") relationship or engaging in "jitney" arrangements.

While client identifiers such as account numbers are commonly exchanged currently between the IB and CB, for situations where it is determined that an LEI is required, new documentation and systems modifications may be required.

With respect to jitney arrangements, UMIR already requires the Executing Dealer to mark an order as a "jitney order" and for properly identifying the Originating Dealer. Members are requesting clarity if the Proposal requires additional look through to the end client of the Originating Dealer. If so, the industry would have to develop procedures and mechanisms for collecting and transmitting this information as well.

7. The Proposal requires unique client identifiers for clients of a foreign dealer equivalent whose orders are entered under a routing arrangement (RA) and are automatically generated on predetermined basis.

In this case, the LEI of the foreign dealer equivalent would have to be provided as well as the unique identifier for the end-client (though the unique identifier of the end client would not need to take the form of an LEI or account number). Members commented that logistically, this requirement would be a challenge to implement given RAs may involve several layers of participants making it difficult to identify the ultimate end-client at time of order entry.

8. IIROC proposes that orders passing through a marketplace utilize encrypted keys for client identifiers to ensure that client information is only visible to IIROC<sup>6</sup>.

We concur that special care be taken to preserve the confidentiality of client sensitive information. Encryption of client identifiers would help in this regard. Our understanding is that the market places would pass through the identifiers to IIROC “as is” (i.e. still encrypted) and that at no point would the market places themselves have visibility of the client identifier. Please confirm.

Furthermore, despite IIROC’s commitment to safeguard sensitive information, our members recognize that regulators are not immune from the growing threat of cyber criminals. Vulnerabilities recently revealed at the Securities and Exchange Commission (SEC) has prompted the SEC to answer difficult questions surrounding its cyber defenses<sup>7</sup>. The SEC has also been asked by Congress representatives to reconsider the breadth of confidential information it aims to collect as part of its impending Consolidated Audit Trail system and to defer the launch of the system until there is full confidence in the SEC’s cybersecurity measures. Similarly, our members have an interest in obtaining more details from IIROC on how it plans preserve the confidentiality of the client information it will obtain under the Proposal. Specifically, who at IIROC will have access to the information, how will it be stored, and what actions will IIROC take in event of a data breach? Furthermore, because IIROC permits both the CSA and the Bank of Canada to access the information, similar questions need to be asked of these institutions.

Members also request details on the permanence of the data IIROC collects under the Proposal. Specifically, how long will IIROC maintain the data on its servers? The repercussions of a data breach can perhaps be mitigated by limiting the amount of data IIROC stores on its servers. We see no reason to keep all historical data on IIROC servers indefinitely.

9. In the Notice IIROC provides a high-level view of the benefits stemming from the proposal, namely improved surveillance, investigatory and data analyses capabilities for the regulator.

However, the Notice does not provide specifics on how client identifiers will be utilized by IIROC (or the CSA and Bank of Canada). These details would be relevant to IIROC Dealer Members because:

- a. They may be helpful as Dealers contemplate how to incorporate client identifiers as part of their internal supervisory frameworks.
- b. They will help Dealers respond to queries from clients seeking information how their identifiers will be used by the regulators.

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<sup>6</sup> Transaction files containing client identifiers in the trading of debt securities would continue to use SFTP, as the information is directly reported to IIROC through each Dealer’s reporting gateway.

<sup>7</sup> See [Testimony](#) by SEC Chairman Jay Clayton before the Committee on Banking, Housing and Urban Affairs

10. In its Notice IIROC asks if a phased-in implementation approach should be followed.

Given the magnitude of change being proposed by IIROC in the Notice, a phasing in approach or introducing certain carve-outs from the requirements, may provide for a more efficient implementation while still meeting IIROC's objectives.

We are specifically concerned that numerous low risk accounts of limited size or with little trading activity may be unnecessarily caught up in the requirement to obtain an LEI<sup>8</sup>. Members considered the feasibility of introducing a de-minimis threshold, either based on account size or trade frequency/volume, below which an LEI would not be required. However, Members concurred that this approach, though sensible in principle, would be very difficult for dealers to implement in practice and for IIROC to monitor compliance.

A possible alternative approach may rest with leveraging the dealers' procedures and systems already developed as part of IIROC Rule 2800C *Transaction Reporting of Debt Securities*. Rule 2800C requires dealers to distinguish client trades as "retail" or "institutional". The Proposal can build on Rule 2800C by requiring client identifiers only for those accounts identified by the dealer member as being "institutional". While this will capture a more limited universe of customers than what is contemplated currently in the Proposal, the customers covered will likely represent the largest value of transactions. Institutional clients will also likely either already have an LEI or generally be more understanding of the requirement to obtain one, where required.

Given that client account numbers would be the identifiers utilized for most "retail" accounts and that those identifiers will be of limited value to IIROC in carrying out their market surveillance function, extending the Proposal to "retail" clients should be revisited by IIROC at some later date.

Lastly, we understand the regulatory division of the Montreal Exchange may also be considering a requirement for client identifiers and likely to face some similar issues to IIROC. We would, therefore, encourage IIROC and the Montreal Exchange to maintain an open dialogue in this area.

Thank you for considering our comments. We would be happy to arrange a meeting with IIAC Members to further discuss any part of this submission.

Sincerely,

*"Jack Rando"*

Jack Rando  
Managing Director  
Investment Industry Association of Canada

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<sup>8</sup> See section #1 on page 2