

November 27, 2019

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Dear Sirs and Mesdames:

Re: Proposed Amendments Respecting Non-Clients

The Investment Industry Association of Canada (the “IIAC or “we”) appreciates the opportunity to respond to the request for comments on IIROC’s Proposed Amendments Respecting Non-Clients. The IIAC is the national association representing the investment industry’s position on securities regulation, public policy and industry issues on behalf of our 120 IIROC-regulated investment dealer members in the Canadian securities industry¹.

Changes to the Non-Client Definition

Replacing “Non-client” with “Dealer Related Person”

The IIAC believes IIROC’s proposed replacements for the definitions of a “non-client order” or “non-client account” with new definitions of “Dealer Related Person order” and “Dealer Related Person account” are too broad and open to interpretation. While, the proposed rules may be appropriate for some smaller independent dealers, the bank-owned dealers have numerous affiliates and internal employees in support related roles who would be unnecessarily classified and no better supervised as a result of the adoption of these broad new definitions. The definitions, if adopted, would potentially include all persons (full-time employees and contingent employees), whether, directly employed by the dealer or not, with access to a dealer’s records and systems that reflect trade and position related data. It is important to note that currently, a large number of employees in these roles have access to position and trade data but are not equipped to use to their advantage. The IIAC would like to inquire as to whether IIROC has oversight responsibility over non-dealer employees.

Employees in various roles at dealers could have access to this data depending on the specific functions required for their jobs. This could include employees performing specific back-office functions, who while

¹ For more information visit, <http://www.iiac.ca>

they may have access to this information, would not be using it on an ongoing basis. As a further example, the IIAC is concerned that employees who compile statistics about “most active” issues on the stock exchange or make use of quantitative data to conduct technical analysis or other trading-based quantitative analyses, might be caught as dealer related persons under the new definition. While we agree that this information holds value and may even affect interest in a trade, it is not confidential and there is no impropriety in using it. Lastly, employees of a dealer in Technology, Finance, or administrative Head Office functions would technically have access to such data but would not be able to use that information to their advantage due to well managed policies and information barriers. As a result, we would like to request that the definitions should clarify that the “trading-related information” must be either pre-trade information or must relate to clients of the Dealer Member.

The IIAC fully understands IIROC’s concerns regarding frontrunning, client priority, and inappropriate use of internal material information about a dealer or issuers. We would like to suggest that IIROC adopt a definition that targets only those employees at a dealer who are directly involved in client dealings, have direct access to live orders as well as trading staff, corporate finance and research staff, and managerial staff who have direct oversight pertaining to these operations. Furthermore, we would suggest amending part (ii) of the definition to include “material trade related information that has not been exposed to the market that is in the Dealer Members’ possession and would reasonably be expected to affect interest in the purchase or sale of a security or the execution of a trade.” This would provide a remedy to IIROC’s concerns as this definition would capture registrants, branch staff, and head office staff who may be able to benefit from access to sensitive information. This definition would exclude employees who are not in a position to abuse this data as well as employees who may have access to subsets of this data such as back office staff, Technology and Finance department employees and a majority of other infrastructure groups. These non-dealer employees would be subject to policies, procedures and controls through the affiliate that would govern the inappropriate use of any sensitive or confidential client or trading information they may have access to. As such, we do not believe that there is any merit to include these employees under the scope of the proposed definition. The IIAC wants to highlight that the exercise to increase the scope of this practice to include incidental or potential access to less market-impactful information, such as historical trades, and deem these employees as non-clients, will require significant investment with little to no benefit.

Updating Non-Client Status

The requirement to validate and update non-client status every twelve months would represent a significant burden for dealers. Registered representatives are already obligated to ensure that their client information remains current and material changes are identified and documented in a timely manner. This obligation is already inherent in all client interactions. If they are required to perform the same exercise at the end of every twelve-month period, it would add an unnecessary administrative and supervisory burden on the dealers, especially for non-client accounts belonging to employees of other dealers. The proposal, as currently interpreted, would effectively cause every dealer to canvass their entire client population on an annual basis to validate client and non-client accounts respectively. This would be a significant annual undertaking.

It is important to mention that If the non-client definition is based on documented control and not influence over an account, firstly, dealers will have to remove a large number of accounts that fall under the current definition of non-client, however, the deemed non-client will still have influence over these accounts. Secondly, non-clients will still have control over these accounts and would still be able to use these accounts as a proxy to take advantage of client and issuer information.

Employee of the “Affiliate” of a Dealer Member or “Related Entity” of a Participant

The IIAC would like to request further clarity on how, including accounts controlled by employees of an affiliate of a Dealer Member or related entity would impact accounts for employees of other dealers. A dealer does not have any effective method to validate the status of these accounts other than through Know Your Client (KYC) information and there is certainly no way for a dealer to validate the status of employees of affiliates or related companies of other dealers. Tackling this from a supervisory perspective would be fairly difficult in our opinion.

Moreover, it is difficult for the bigger integrated firms when someone is in a corporate support area that supports retail and institutional clients. We would like clarity regarding which restrictions they would follow.

Scope of Confidential Information

The definition of material non-public information (MNPI) can be open to interpretation and may be problematic for dealers. While the IIAC understands that it would be based on securities legislation and on the definitions and interpretations of these terms under the applicable statute, we would like to request that IIROC further narrow the scope of this definition to make it easier for dealers to interpret and apply. Due to information barriers built into the systems at dealers, we expect that fewer employees would have access to such information due to given controls related to information barriers. As dealers are required to ensure they have effective information barriers along with policies and procedures to support these information barriers, we would also appreciate some clarity on what IIROC intends to achieve by including employees with access to MNPI. Effective information barriers should already preclude employees from using any information they have access to.

Transition to New Definitions

The IIAC believes that if IIROC adopts these new definitions as outlined in the Proposed Amendments, the undertaking will be a significant project requiring surplus resources and time. This would result in a full reassessment of existing non-clients and all existing clients to determine if any of their status should be converted to non-client. In addition, all account documentation and KYC forms would also need to be updated to reflect the new definition. We believe this project would take a material amount of time to complete.

Responses to IIROC's Specific Questions:

- 1. Would replacing the “non-client orders” definition with an alternate term, such as “Dealer Related Person order”, be helpful to Dealer Members in clarifying the meaning and scope of the Proposed Amendments?**

The IIAC agrees that it is meaningful to create the new definition of client related orders to replace professional orders, but only if the definition is unambiguous, can be implemented effectively with seamless supervision, and is not overreaching in that it does not place employees of affiliates at a disadvantage. It is our understanding that not all employees of a firm would be considered Dealer Related Persons and that having access to the ISM platform is considered as having access to confidential information. Since this is a principle-based approach where dealers have the flexibility to define a Dealer Related Person, we request further clarity on how this would impact businesses that have over 50 Dealer members on their books.

- 2. What are the impacts to Dealer Members in terms of implementing the Proposed Amendments?**

We believe a significant amount of work would be required to efficiently implement the Proposed Amendments in terms of operations, supervision, controls, testing and administration. Dealers would have three main tasks at hand: 1) systems and operational changes to re-assess all existing accounts in the book of records to determine which one falls under the client vs non-client definitions and arrange to update and/or open new accounts, file documentation, and assign new account identifiers accordingly; and 2) implementing a new process for continuous updating of employee accounts as they move to different roles within organizations There is also the requirement to conduct a review every twelve months. 3) It will be challenging to administer meaningful controls and provide evidence of testing. This is due to the fluctuating nature of both, impacted employees and applicable issuers.

These would entail substantial costs in terms of time and funding as well as significant dedicated resources. Firms would also need to thoroughly review their compliance policies to make sure they are in line with the new definitions. This exercise is a considerable undertaking for dealers.

- 3. IIROC is proposing that the implementation date be at least 180 days following the publication of the Notice of Approval. Is this time period sufficient to make any necessary operational and technological changes? Are there any specific considerations which IIROC should take into account in establishing an implementation deadline?**

We believe the proposed time required to implement the required operational and technological changes is insufficient while considering the significant time and effort that would be required to effectively assess each firm's client accounts. If we were to define a time period, at least one to two years should be allocated to properly and fully implement these new changes, unless a phased approach is permissible. Our recommendation for a longer implementation period stems from the fact that firms are currently still trying to implement other regulatory projects mandated by IIROC.

4. **To minimize the impact on Dealer Members, should IIROC take a phased approach to the implementation of the Proposed Amendments, such as having separate phases for new and existing accounts? For example, Phase 1 would apply to new accounts opened on or after the publication of the Notice of Approval, and Phase 2 would apply to all other accounts. What specific considerations should IIROC take into account in establishing the implementation period for each phase?**

The IIAC believes that a phased approach would be beneficial, however it would still need to be structured to provide dealers with the maximum amount of time to complete and implement systems and administrative changes efficiently. In terms of specific items, we suggest that IIROC consider the distinction between existing and new clients as there would be a more significant impact on dealers' existing clients and keeping this in mind, firms would require a lengthier implementation duration. We anticipate a phased approach will also be necessary to manage the costs of operational and technical enhancements.

5. **Should the requirement to update with respect to the status of Dealer Related Person accounts be specific to the type of account, or should there be one standard for all accounts? If we set one standard for all accounts at an annual basis, would this align with Dealer Members' current practices?**

The IIAC believes there is no added value to have an annual review as dealers are already obligated to remain aware of material changes and to update client accounts within a timely manner upon becoming aware of such changes. Currently, RRs are alerted, and they update client accounts when there is a material change to the clients' personal circumstances. Order Execution Only (OEO) firms are reliant upon the client to disclose any material changes, including those of this specific nature.

Furthermore, we would like to request clarification from IIROC on whether firms need to make a distinction between internal and external dealer related person accounts and also what IIROC's expectations are regarding updating external accounts.

We thank IIROC for considering our comments and if you have any questions with respect to the foregoing, we kindly ask that you contact the undersigned at tevans@iiac.ca. Thank you.

Sincerely,



Todd Evans
Managing Director
Investment Industry Association of Canada