Chapter 13

SROs, Marketplaces and Clearing Agencies

13.1 SROs

13.1.1 IIROC Rules Notice - Request for Comments – Republication - Dealer Member Rules - Proposals to Implement the Core Principles of the Client Relationship Model

IIROC RULES NOTICE
REQUEST FOR COMMENTS
REPUBLICATION - DEALER MEMBER RULES
PROPOSALS TO IMPLEMENT THE CORE PRINCIPLES OF THE CLIENT RELATIONSHIP MODEL

Summary of the nature and purpose of the proposed rules and amendments

The proposed Rules and amendments have been introduced to establish substantive requirements developed under the Client Relationship Model (CRM) Project for the purpose of addressing the following regulatory objectives:

1. Relationship disclosure;

2. Conflicts of interest management/disclosure;

3. Suitability assessment; and

4. Account performance reporting.

These matters should also be viewed as key elements of a broader CRM framework and complementary to the fundamental obligation of all dealers and their representatives to deal fairly, honestly and in good faith with their clients.

The Canadian Securities Regulators (CSA) will also be publishing for public comment proposed amendments to National Instrument 31-103 Registration requirements and exemptions, which, when implemented, will introduce new cost disclosure and performance reporting requirements to be complied with by all registered dealers and advisers. IIROC and the Mutual Fund Dealers Association of Canada (“MFDA”) are participating in the working group developing the CSA’s proposals.

New IIROC rules and amendments are subject to approval by the CSA. The CSA may decline to approve IIROC rules and amendments relating to cost disclosure and performance reporting if these omit aspects of the CSA’s proposals. In any event, once the CSA amendments are finalized, IIROC will amend its equivalent requirements, as necessary, to ensure that they are consistent with those of the CSA.

Disclosure of the details of the account relationship and the services to be provided are necessary to better inform retail clients of the nature of their account relationship. This disclosure, along with account cost and activity reporting will provide retail clients with important information to use in assessing the performance of investments in their account and whether their objectives and expectations for the account have been satisfied.

A new Rule has been proposed to clarify IIROC’s position regarding the management of material conflicts of interest. The Rule will require Dealer Members to develop and maintain policies and procedures to identify, disclose and address existing and potential material conflicts involving clients.

Amendments to the account suitability requirements have been introduced to enhance the level of investor protection for retail clients by ensuring that the suitability of investments in each client’s account is assessed whenever:

- a trade is accepted,
- a recommendation is made,
- securities are transferred or deposited into the account,
- there is a change of representative on the account, or

- there is a material change to the know-your-client information for the account.

Response to comments

Proposed rule changes to address the CRM issues were originally published by the Investment Dealers Association (IDA) in February, 2008. A revised version of the proposed rule changes was subsequently published by IIROC in April, 2009. IIROC staff's response to the comments received on the revised proposed amendments have been posted on the IIROC website (IIROC - Policy Proposals).

As noted below, IIROC staff have made revisions to the proposed CRM Rules and amendments to address comments received. IIROC staff has also developed proposed implementation periods for each of the proposal elements and have amended the previously circulated draft guidance notes. The revised proposed Rules and amendments, proposed implementation periods and revised draft Guidance Note are being re-published for comment for a period of 60 days with this Notice.

Description of the proposed Rules and rule-making process

Current IIROC Rules address some aspects of the core principles under CRM. However, there are significant gaps in other respects, such as the requirement to provide relationship disclosure information on account opening and the requirement to provide account performance reporting. The proposed Rules and amendments are designed to address the gaps that have been identified.

The CRM Project is essentially an extension of the earlier work of the Ontario Securities Commission (OSC) Fair Dealing Model Committee, which released the Fair Dealing Model Concept Paper (Concept Paper) in January, 2004. This Concept Paper envisioned extensive changes to the regulatory requirements applicable to retail client accounts, from the negotiation and documentation of the relationship at account opening to the transactional information and account reporting to be provided to clients on an ongoing basis.

In September 2004, the Fair Dealing Model initiative was brought under the umbrella of the broader Registration Reform Project (RRP) of the provincial securities commissions. The aim of RRP was to streamline and harmonize the registration regime and develop rules in certain key areas to apply to all registrants on a national basis. Under RRP, the Fair Dealing Model initiative was re-branded as the Client Relationship Model and its focus narrowed to the following three areas:

- account opening documentation;
- costs, conflicts and compensation transparency; and
- performance reporting.

Working groups consisting of industry and regulatory staff developed rulemaking recommendations for each of these areas. A joint rulemaking committee of the IDA and the Mutual Fund Dealers Association (MFDA) then drafted rule proposals in consultation with staff of the securities commissions. This was followed by an initial dealer review of the proposals by three joint IDA/MFDA industry subcommittees. Samples of proposed new disclosures were reviewed and commented on by approximately 370 advisors that participated an 11 city broadcast consultation that was held in August, 2006. These initial drafts were also distributed for comment to the IDA Compliance and Legal Section and the IDA Financial Administrators Section in September, 2006. Presentations on the contents of these initial drafts were provided to each of the IDA District Councils in October and November, 2006. In response to the comments received on these initial drafts, IDA staff re-drafted its proposals to focus more closely on the core CRM objectives and to factor in potential implementation issues.

As noted above, proposed Rule changes to address the CRM issues were published by the IDA in February, 2008 and subsequently revised and republished by IIROC Board in April, 2009. IIROC staff has reviewed the comments received in response to the February, 2008 and April 2009 publications. We have also conducted further consultations with investor representatives, industry associations, the MFDA and the provincial securities regulators. The proposed Rules and amendments brought forward for consideration with this Notice incorporate feedback received through the comment processes and these subsequent consultations.

The proposed Rules and amendments are summarized as follows:

(a) Relationship disclosure for retail client accounts

IIROC is proposing that every Dealer Member will provide its retail clients with the following information regarding the relationship they are entering into with the client:

- a description of the types of products and services offered by the Dealer Member;

- a description of the account relationship to which the client has consented;
- where applicable, a description of the process used by the Dealer Member to assess investment suitability, including a description of the process used to assess the client's "know your client" information, a statement as to when account suitability will be reviewed and an indication whether or not the Dealer Member will review suitability in other situations, including market fluctuations;
- a statement indicating material Dealer Member and adviser conflicts of interest and stating that future material conflict of interest situations, where not resolved, will be disclosed to the client as they arise;
- a description of all fees, charges and costs associated with operating the account and in making or holding investments in the account; and
- a description of account reporting the client will receive, including a statement identifying when account statements and trade confirmations will be sent to the client and a description of the Dealer Member's obligations to provide account performance information and a statement indicating whether or not percentage return information will be sent.

The obligations of Dealer Members to provide certain specific disclosures regarding suitability will vary for order-execution service accounts and managed accounts, in that there is no suitability obligation regarding order-execution service accounts and managed accounts must be monitored and supervised according to the specific, more rigorous standards imposed under Rules 1300 and 2500.

IIROC is not proposing to mandate the format of the disclosures, but will require that the information be:

- Provided to the client in writing at the time of account opening;
- Written in plain language; and
- Included in a document entitled "Relationship Disclosure".

Dealer Members are obligated to provide some of the relationship disclosure information under the current Rules. The proposed Rule allows for information already provided to clients to essentially be incorporated by reference as long as the relationship disclosure contains a description of this information and the client is specifically referred to the other documents.

Amendments have been made to the previous IIROC proposals published for public comment in April, 2009 to clarify that client acknowledgement must be obtained when either a relationship disclosure or "know your client" document is provided to the client.

(b) Conflicts management / disclosure

Rules relating to the management of specific conflicts of interest are already in place. To supplement these existing requirements, IIROC is proposing to adopt a general rule to require that all material conflict situations between the Approved Person and the client and between the Dealer Member and the client be addressed by either: avoiding the conflict, disclosing the conflict or otherwise controlling the conflict of interest situation.

Amendments have been made to the previous IIROC proposals published in April, 2009 to clarify the application of the general conflicts management / disclosure standard as it relates to material conflicts of interest between the Approved Person and the client and between the Dealer Member and the client. This has been accomplished by creating separate Rules setting out the obligations of the Approved Person and the Dealer Member, respectively, to address conflicts of interest. The revised wording recognizes that Dealer Members are more likely to have to deal with scenarios in which a Dealer Member must balance the competing interests of two or more of its clients.

(c) Account suitability for retail clients

In addition to the current suitability requirement for trades accepted and recommendations made on retail client accounts, IIROC is proposing that an account suitability review must be performed when certain "trigger" events occur (i.e., transfers/deposits into an account, material change in client circumstances, change in the account representative). It is currently an industry best practice to perform suitability assessments on a periodic basis irrespective of the "trigger" events.

IIROC is also proposing to clarify how suitability assessment reviews are to be performed. Specifically, proposed amended rules 1300.1(p) through (r) make it clear that all suitability assessment reviews must be performed by taking into consideration the client's "investment objectives and time horizon" and the "account's current investment portfolio composition and risk level."

IIROC staff is examining the possibility of introducing further changes to the suitability Rule, in addition to the amendments noted above. Some of these may include consequential amendments to conform the suitability requirements contained in Rule 1300 to the new relationship disclosure requirements. In particular, the proposed relationship disclosure requirements will require the Dealer Member to advise the client that he or she will be provided with a copy of the "know your client" information collected at account opening and when there are material changes to this information. The proposed amendments may also lead to changes in the supervisory requirements under Rule 2500.

Wording amendments have been made to the previous IIROC proposals published in April, 2009 regarding taking into consideration the client's investment time horizon and the account's current investment portfolio when performing suitability assessment reviews.

As a separate initiative, IIROC staff is republishing for comment guidance to Dealer Members and Registered Representatives on regulatory expectations for meeting their suitability requirements. The current version of this draft guidance, along with a consolidated response to the public comments received on the previous draft, is included as Attachment G.

(d) Account performance reporting for retail clients

In developing the proposed Rules on performance reporting, issues regarding security position cost disclosure, account activity disclosure and account percentage return disclosure were considered.

(i) Security position cost disclosure

IIROC is proposing to mandate that security position cost information be provided to all retail clients at least annually. When the proposed Rules were published for comment in February, 2008, input was requested as to the preference to require the disclosure of original cost or tax cost. No clear consensus was reached on this point. However, as we believe original cost provides the most useful information for the purpose of account performance, we have mandated in the proposed amendments that original cost be disclosed.

(ii) Account activity disclosure

IIROC is proposing to mandate that account activity information be provided to all retail clients on at least an annual basis. This reporting would require disclosure of the cumulative realized and unrealized capital gains on the client's account.

(iii) Account percentage return disclosure

IIROC is proposing to mandate that account percentage return information be provided to retail clients. As set out in Attachment E, Dealer Members not currently providing percentage return information to their retail clients will be given 2 years to implement this reporting requirement on a prospective basis. In addition, Dealer Members currently providing percentage return information to their retail clients, will be given six months from the date of implementation to adopt either a time weighted or dollar weighted calculation method acceptable to IIROC to calculate such information.

Amendments have been made to the previous IIROC proposals published in April, 2009 to mandate that account percentage return information be provided to all retail clients.

The proposed Rules and amendments were approved by the IIROC Board of Directors on June 24, 2010. The text of the proposed Rules and amendments is set out in Attachments A through D.

Issues and alternatives considered

In the course of working on the CRM project, IIROC staff consulted extensively with industry participants and the public. As a result, IIROC staff has been presented with a number of different alternatives and perspectives on the issues to be addressed.

Many commenters have raised questions regarding value of the proposed changes in light of the potential costs to industry participants. IIROC staff has continued to receive input on the cost issue throughout the rule-making process and is confident

that it is aware of, and has properly considered the issue. To minimize potential costs, wherever possible, IIROC staff has revised the proposal to provide greater flexibility to Dealer Members in complying with the new requirements without compromising the investor protection goals of the CRM project.

Many industry participants have also suggested that the regulatory objectives of CRM should be addressed through broad principles-based requirements alone. IIROC staff recognizes that there are advantages with principles-based Rules, but this objective must be balanced with the need to articulate clear and consistent minimum standards. IIROC staff believes that the proposed Rules and amendments strike an appropriate balance, setting out clear standards while allowing a sufficient degree of flexibility to accommodate differences in Dealer Members' business models.

Consideration was also given to the suggestion that a standard form boilerplate disclosure document be developed to address the relationship disclosure issue. However, while IIROC staff acknowledges that some aspects of the relationship disclosure information may be common to all Dealer Members, we also expect that there will be a great deal of variation between firms regarding the specific products and services provided and the processes Dealer Members put in place to deliver those products and services. We believe that the identification of these differences is essential information for clients to make informed choices as to the different options that are available to them. IIROC staff does not believe that the regulatory objectives of relationship disclosure can be satisfied by simply providing a standard form generic disclosure document that lists products and services that a Dealer Member may or may not offer without differentiating between firms.

The need for consistency across the various segments of the securities industry was also raised in many comments received by IIROC staff. Some of the inconsistencies in the approach to the CRM issues taken by IIROC, MFDA and the securities commissions are due to differences in the way business is conducted by the different types of registrants. In any case, staff has reviewed and revised the proposed changes with a view to ensuring, as much as possible, that there is consistency with the proposed requirements to apply to other industry sectors. To this end, the relationship disclosure content requirements have previously been amended and re-organized.

IIROC staff maintains the position that the relationship disclosure information should function as a foundation document that provides a single reference point for key information on the account relationship. However, in the interests of avoiding duplication of the information, the proposed Rule allows for disclosure provided to clients in other materials to be referenced. In such cases, the relationship disclosure must contain a summary description of the information and the client must be specifically referred to the other documents that have been provided.

On the issue of conflicts of interest, IIROC staff has made changes to the proposed Rule to clarify that Dealer Members and Approved Persons must "address" rather that "resolve" conflicts. Separate requirements dealing with the way in which material conflicts of interest must be addressed have also been developed for Dealer Members and Approved Persons. These separate requirements reflect the fact that IIROC recognizes that a Dealer Member, as a financial intermediary, is much more likely to encounter competing client interest situations than an Approved Person.

IIROC staff also notes the potential challenges pointed out by industry participants on the issue of performance reporting. To address the comments we received, the proposed Rule regarding activity reporting has been simplified so that Dealer Members will be required only to disclose the cumulative realized and unrealized income and capital gains/losses on the client's account and adequate implementation transition periods have been proposed for all three performance reporting elements. To provide Dealer Members with greater flexibility, the proposed Rule allows for percentage rates of return to be calculated by either a time weighted or dollar weighted calculation method acceptable to IIROC. The requirement to disclose returns, if reported, on a 1, 3, 5 and 10 year basis has been maintained, but as the requirement will apply on a prospective basis, it is not anticipated that it will create a significant compliance burden on Dealer Members.

Many commenters argued that performance reporting is strictly a service issue and that it should be left up to Dealer Members to decide whether they choose to provide any such reporting to clients. IIROC's primary mandate is however to protect the interests of investors and this responsibility involves, in part, setting minimum service levels for clients. IIROC's position is that it is reasonable to expect that clients receive position cost and account activity information to enable them to determine whether they have gained or lost money on the investments in their accounts and to receive percentage return information to enable them to determine the reasonableness of any gain or loss earned/incurred.

The proposed Rules and amendments will be subject to transition periods to allow for systems changes to be implemented before the amendments become effective. Included as Attachment E are the proposed transition periods (from date of implementation notice publication) for each CRM proposal requirement.

We will also be issuing guidance to clarify IIROC's expectations and answer questions on the application of the proposed Rules and amendments. A draft Guidance Note is attached as Attachment F.

As a separate initiative, we had previously published for public comment a draft Guidance Note on "Know Your Client and Suitability". Given that the CRM proposals contain proposed amendments relating to the acknowledgement of the know your

client information form and the suitability assessment requirements, we felt it appropriate to re-publish this draft notice as part of the CRM proposals. See Attachment G.

Comparison with similar provisions

The CRM-related proposals of the MFDA and the Canadian Securities Administrators (CSA) are summarized below.

For the purpose of comparison, we have also noted certain provisions set out in the U.K. and U.S. rules regarding account relationship disclosure and performance reporting. This information has been included to provide some background and context, but is not intended to serve as a comprehensive analysis of all relevant international requirements.

(a) Mutual Fund Dealers Association of Canada

As noted above, IIROC staff has been exchanging information and holding ongoing meetings with staff of the MFDA and the securities commissions with a view to developing harmonized rules to address the CRM issues.

The revised CRM proposal of the MFDA, is substantially similar to the IIROC proposed Rules and amendments in most respects. All of the core elements of the CRM project are addressed under both proposals, as are the proposed changes to the suitability requirements. Some noteworthy differences between the two proposals are summarized below:

- The MFDA proposal allows for the required disclosure elements to be disseminated in a variety of documents. IIROC's proposed Rule states that where specific information has already been provided to the client by the Dealer Member, the relationship disclosure information can simply include a general description and a reference to the other disclosure materials containing the required information. The revised IIROC requirement is intended to provide greater flexibility for Dealer Members than the previous IDA proposal which required that clients be provided with a single stand alone relationship disclosure document containing all of the mandatory information. The new proposed Rule allows Dealer Members to continue to use their existing processes to deliver specific information, such as fee disclosure, but maintains the requirement that clients be provided with a comprehensive user friendly source for at least basic account relationship information.

- Most of the specific relationship disclosure requirements are contained in both the IIROC and MFDA proposals. There are differences in that the IIROC proposal requires specific disclosure as to whether client accounts will be reviewed at times other that the regulatory minimum (such as in the event of a market disruption) and whether the client will be provided with percentage return information. The MFDA proposal does not require such disclosure. IIROC's position stems from the concern that clients may presume that their accounts are being reviewed by their representatives whenever significant market events occur and that they are entitled to receive percentage return information on statements. If these services are not to be provided, Dealer Members should advise clients accordingly, so that client expectations are properly managed.

- The MFDA performance reporting proposal does not require individual position cost disclosure, which is required under the IIROC proposal.

- The activity reporting requirements in the IIROC and MFDA proposals are similar in most respects. However, the MFDA proposes to mandate account activity disclosure for the current year only, while the IIROC proposal will require cumulative activity reporting.

- The MFDA amendments do not propose to mandate percentage return performance reporting.

Details of the proposed amended MFDA rules and policies can be accessed at www.mfda.ca.

(b) Canadian Securities Administrators

IIROC staff also participated in the development of National Instrument 31-103 (N1 31-1O3), which also addresses certain elements of the CRM project, in particular, relationship disclosure and conflicts management. NI 31-103 is intended, in part, to impose requirements similar in effect to the CRM proposals of the SROs on registrants that are not subject to SRO jurisdiction.

NI 31-103 may be accessed on the Ontario Securities Commission (OSC) website at
http://www.osc.gov.on.ca/documents/en/Securities-Category3/rule_20090918_31-103_3238-supplement.pdf

(c) United Kingdom

The U.K. Financial Services Authority ("FSA") also has implemented principles-based rules that address some of the issues raised under CRM.

The FSA Conduct of Business sourcebook (COBS) sets account relationship related disclosure requirements as follows:

- COBS 2.2 - A firm must provide appropriate information in a comprehensible form to a client about the firm and the types of products (including specific types of investments and investment strategies) and services offered by the dealer and the costs and associated charges relating to these products and services before these products and services are provided. This disclosure may be provided in a format that is standardized for the dealer.

- COBS 6.1 – Unless subject to COBS 9.6.5, a firm must provide retail clients the following information (along with other additional information) if relevant:

  (1) the name and address and contact details of the firm;

  (2) a statement that the firm is authorized and the name of the authorizing body (and the contact information for the authorizing body);

  (3) the nature, frequency and timing of reporting to be provided to the client;

  (4) disclosure regarding conflicts of interest;

  (5) disclosure regarding investments or cash held by the firm for a retail client;

  (6) information on costs and account charges; and

  (7) information on the investor compensation scheme to which the firm belongs.

- COBS 8.1 - Requirement to enter into a written basic agreement with a retail client setting out the rights and obligations of both parties.

- COBS 9.6.5 – A firm that offers "basic advice" on "stakeholder products" must provide clients with the following information:

  (1) the name and address of the firm;

  (2) a statement as to whether investment products being offered come from one company, a limited number of companies or the capital markets as a whole;

  (3) a statement that the service being offered is basic on a limited range of investment products;

  (4) a statement that the firm is regulated by the FSA;

  (5) a statement disclosing any product provider loans;

  (6) a description of the complaint handling process and the circumstances under which a client can refer a matter to the Financial Ombudsman Service; and

  (7) a description of the circumstances and the extent to the client will be entitled to compensation from the Financial Services Compensation Scheme.

On the issue of performance reporting, the FSA Handbook contains the following requirements:

- COBS 16.3 – Where a retail client has a managed account with a firm, a periodic statement must be provided every six months at a minimum (every three months if the client requests) which must include the following information (as referenced in the Conduct of Business Sourcebook Rule 16 Annex 2R):

  (1) market value of each position held;

(2) cash balance at the beginning and end of each reporting period;

(3) the performance of the portfolio during the reporting period;

(4) the fees and charges incurred during the reporting period;

(5) a comparison of the performance during the reporting period to a performance benchmark (if agreed to between the firm and the client); and

(6) details of the total amount of dividends, interest and other payments received during the reporting period and details of other relevant corporate actions.

The Conduct of Business Sourcebook can be accessed at FSA Handbook.

The FSA is continuing to look at ways to improve the interaction between consumers and industry participants and is in the process of conducting a Retail Distribution Review aimed at:

- improving the clarity for consumers of the characteristics of different service types and the distinctions between them;
- raising professional standards; and
- reducing the conflicts of interest inherent in remuneration practices and improving transparency of the cost of all advisory services.

Information relating to the FSA's Retail Distribution Review can be accessed at www.fsa.gov.uk.

(d) United States

Under the *Investment Advisers Act of 1940*, a registered adviser that gives personal advice is required to supply each prospective advisory client with a written brochure containing the information required under Part II of Form ADV. Additionally, the brochure is to be offered to current clients annually. Part II of Form ADV includes but is not limited to, the following:

- the approximate percentage of billings from each type of advisory service itemized in the form;
- the types of compensation arrangements used by the adviser, the fee schedule, and how to obtain a refund or end an advisory contract before its expiration;
- the types of clients of the adviser;
- the categories of investments about which the adviser offers advice;
- methods of security analysis, sources of information, and investment strategies;
- the education and business backgrounds of particular individuals;
- other business activities of the adviser;
- other financial industry activities or affiliations (including registration) of the adviser and related persons;
- participation or interest in client transactions; and
- information on the frequency, level, and triggering factors for account reviews and the nature and frequency of reports to clients on their accounts.

On the issue of account opening documentation, the Financial Industry Regulatory Authority (FINRA) has also provided some guidance to their members in the form of a new account application template. There is no regulatory requirement to use the sample form, or any portion of it. Rather, the intent of the form is to provide basic plain language examples of what a firm might use to describe client risk profile and issues the client should be aware of when evaluating account performance information. The form may be accessed at FINRA - Information Notice - 10/21/08.

Effects of proposed Rule on market structure, Dealer Members, non-members, competition and costs of compliance

The effect of the proposed Rules and amendments will be to improve the quality of information that retail clients are provided regarding their account relationships and with the performance of investments in their accounts. Retail clients will also be better served through more frequent monitoring of their accounts and better conflict management procedures at Dealer Members.

In developing the proposed Rules and amendments, the possibility of performing costs versus benefits analysis work was examined in some detail. An independent research company was hired to provide recommendations and assist in completing this work. Meetings involving staff from the IDA, MFDA, OSC, the Investment Funds Institute of Canada, the Investment Industry Association of Canada and representatives from investment dealers and mutual fund dealers were held to discuss the approach to be taken on the cost/benefit analysis. However, no agreement on the approach was reached. While the proposed formal cost/benefit analysis was not performed, substantial feedback from industry participants was provided throughout the rule development process in any case. As such, IIROC staff believes that it is sufficiently informed as to the potential impacts of the proposed Rules and amendments.

It is expected that the relationship disclosure and performance reporting proposals will give rise to the most significant information systems and cost impacts. Furthermore, the full extent of the relationship disclosure impacts will be influenced by:

1. *Relationship disclosure customization* – In order to accurately describe the account relationship being entered into with each client, Dealer Members will need to customize to a certain extent the relationship disclosure information they provide to address individual client account details[1]. This required customization will likely result in initial and ongoing compliance costs.

2. *Relationship disclosure implementation period for existing accounts* – A longer relationship disclosure implementation period for existing accounts will lessen the costs of initial compliance.

The extent of the systems and cost impact for the performance reporting requirements will be influenced by:

1. *Report data requirements* – Dealer Members will be required to warehouse greater amounts of historical information to produce the reports.

2. *Report calculation requirements* – Costs will likely increase where a greater number of calculations must be performed to generate the report.

The costs incurred may also differ between Dealer Members as many firms already furnish at least a portion of the information required under the new minimum standards. The effect on a particular Dealer Member can only be precisely determined by performing a firm specific assessment, but may include costs associated with the production of documents (including printing and mailing) and the imposition of new compliance and supervisory requirements.

As previously noted, an appropriately long transition period is being proposed (refer to Attachment E) to allow Dealer Members time to make necessary systems changes.

Apart from the issues described above, it is not expected that there will be other major technological systems impacts on Dealer Members as a result of the proposed Rules and amendments. Further, it is not anticipated that there will be other significant effects on Dealer Members or non-Dealer Members, market structure or competition.

It is believed that the benefits associated with the proposed requirements are significantly greater than the additional costs to Dealer Members. The proposed Rules and amendments do not impose any burden or constraint on competition or innovation that is not necessary or appropriate in the furtherance of IIROC's regulatory objectives. The proposed Rules and amendments do not impose costs or restrictions on the activities of market participants that are disproportionate to the goals of the regulatory objectives sought to be realized.

The IIROC Board has determined that the proposed Rules and amendments are not contrary to the public interest.

Anticipated effective date and implementation plan

IIROC anticipates that the proposed Rules and amendments will be made effective on a date to be determined by IIROC staff after receiving notification of approval by the requisite provincial securities commissions. The proposed transition periods for each of the CRM core principle elements are set out in Attachment E.

[1] It is expected that all Dealer Members will provide relationship disclosure information to clients that addresses at a minimum the account and products and services to be provided to the client, taking into consideration the client's risk tolerance and investment circumstances.

Classification of Rules and amendments and filing in other jurisdictions

IIROC has determined that the proposed Rules and amendments are Public Comment Rules and has directed that the proposed Rules and amendments be published for comment.

The proposed Rules and amendments will be filed with each of IIROC's Recognizing Regulators, in accordance with s.3 of the Joint Rule Review Protocol contained in the IIROC Recognition Order.

Request for public comment

Comments should be made in writing. One copy of each comment letter should be delivered within 60 days of the publication of this notice, addressed to the attention of:

Richard J. Corner
Vice President, Member Regulation Policy
Investment Industry Regulatory Organization of Canada
Suite 1600, 121 King Street West
Toronto, Ontario
M5H 3T9

Angie F. Foggia
Policy Counsel, Member Regulation Policy
Investment Industry Regulatory Organization of Canada
Suite 1600, 121 King Street West
Toronto, Ontario
M5H 3T9

A second copy should be addressed to the attention of:

Manager of Market Regulation
Ontario Securities Commission
20 Queen Street West
19th Floor, Box 55
Toronto, Ontario
M5H 3S8
marketregulation@osc.gov.on.ca

Those submitting comment letters should be aware that a copy of their comment letter will be made publicly available on the IIROC website (www.iiroc.ca under the heading "IIROC Rulebook - Dealer Member Rules – Proposed Policy").

Attachments

Attachment A - Proposed Amendments - New Rule XX00 - Relationship disclosure;

Attachment B - Proposed Amendments - New Rule XX00 - Conflicts of interest;

Attachment C - Proposed Amendments - Black-line copy of amended Rule 1300.1 - Supervision of accounts;

Attachment D - Proposed Amendments - Amendments to Rule 200.1 - Minimum Records;

Attachment E - Proposed transition periods from date of implementation notice publication; and

Attachment F - Draft Guidance Note, Client Relationship Model

Attachment G - Draft Guidance Note, Know your client and suitability

Attachment A

PROPOSALS TO IMPLEMENT THE CORE PRINCIPLES OF THE CLIENT RELATIONSHIP MODEL

PROPOSED AMENDMENTS - NEW RULE XX00 - RELATIONSHIP DISCLOSURE

1. New Rule XX00 is enacted as follows:

"**XX01. Objective of relationship disclosure requirements**

(1) This Rule establishes the minimum industry standards for relationship disclosure to retail clients at the time of opening an account or accounts. This Rule does not apply to accounts of institutional clients.

Relationship disclosure is a written communication from the Dealer Member to the client describing:

- the products and services offered by the Dealer Member;
- the nature of the account and the manner in which the account will operate; and
- the responsibilities of the Dealer Member to the client.

References in this Rule describing the obligations of the Dealer Member in relation to services provided on advisory and managed accounts apply equally to the Approved Persons of the Dealer Member providing services on such accounts.

This Rule should be reviewed in conjunction with:

- Rules 1300.1 and 1300.2 - Know your client, suitability and supervision;
- Rules 1300.3 to 1300.21 - Discretionary and managed accounts;
- Rule 2500 - Minimum standards for retail account supervision; and
- Rule 3200 - Minimum requirements for Dealer Members seeking approval under Rule 1300.1(s) for suitability relief for trades not recommended by the Dealer Member.

XX02. Definition of account relationship types

(1) An "advisory account" is an account where the client is responsible for investment decisions but is able to rely on advice given by a registered representative. The registered representative is responsible for the advice given. In providing this advice, the registered representative must meet an appropriate standard of care, provide suitable investment recommendations and provide unbiased investment advice.

(2) An "order-execution service account" is an account opened in accordance with "order-execution service" requirements set out in Rule 3200.

(3) A "managed account" is an account as defined in Rule 1300.3.

XX03. Form of relationship disclosure

(1) Dealer Members have the choice of providing customized relationship disclosure to each client, or appropriate standardized relationship disclosure to separate classes of clients.

(2) Where standardized relationship disclosure is provided to the client the Dealer Member must determine that the disclosure is appropriate for the client. Specifically, the disclosure must accurately describe:

(a) the account relationship the client has entered into with the Dealer Member; and

(b) the advisory, suitability and performance reporting service levels the client will receive from with the Dealer Member.

(3) Where a client has more than one account, combined relationship disclosure information may be provided as long as the Dealer Member determines that the combined disclosure is appropriate for the client in light of the relevant circumstances, including the nature of the various accounts.

XX04. Format of relationship disclosure

(1) The format of the relationship disclosure is not prescribed but:

(a) The relationship disclosure must be provided to the client in writing;

(b) The relationship disclosure must be written in plain language that communicates the information to the client in a meaningful way; and

(c) The relationship disclosure must include all the required content set out in Section XX05, or, where specific information has otherwise been provided to the client by the Dealer Member, a general description and a reference to the other disclosure materials containing the required information.

(2) Dealer Members may choose to provide the relationship disclosure as a separate document or to integrate it with other account opening materials.

XX05. Content of relationship disclosure

(1) The relationship disclosure information must be entitled “Relationship Disclosure”.

(2) Subject to subparagraphs (3) and (4), the relationship disclosure must contain the following information:

(a) A description of the types of products and services offered by the Dealer Member;

(b) A description of the account relationship;

(c) A description of the process used by the Dealer Member to assess investment suitability, including:

(i) a description of the approach used by the Dealer Member to assess the client’s financial situation, investment objectives, risk tolerance and investment knowledge and a statement that the client will be provided with a copy of the “know your client” information that is obtained from the client and documented at time of account opening and when there are material changes to the information;

(ii) a statement indicating that the Dealer Member will assess the suitability of investments in the client’s account whenever:

(A) a trade is accepted,

(B) a recommendation is made,

(C) securities are transferred or deposited into the account,

(D) there is a change in the registered representative, investment representative or portfolio manager responsible for the account, or

(E) there is a material change to the client’s “know your client” information; and

(iii) a statement indicating whether or not the suitability of the investments held in the account will be reviewed in the case of other triggering events not described in Rule 1300.1(r) and, in particular, in the event of significant market fluctuations;

(d) A description of the client account reporting that the Dealer Member will provide, including:

(i) a statement indicating when trade confirmations and account statements will be sent to the client;

(ii) a description of the Dealer Member's minimum obligations to provide performance information to the client and a statement indicating when account position cost and account activity information will be provided to the client; and

(iii) a statement indicating whether or not the provision of account percentage return information will be an option available to the client as part of the account service offering;

(e) A statement indicating Dealer Member and Approved Person conflicts of interest and stating that future conflict of interest situations, where not avoided, will be disclosed to the client as they arise;

(f) A description of all account service fees and charges the client will or may incur relating to the general operation of the account;

(g) A description of all charges the client will or may incur in making and holding investments by type of investment product;

(h) A listing of the account documents required to be provided to the client with respect to the account; and

(i) A description of the Dealer Member's complaint handling procedures and a statement that the client will be provided with a copy of an IIROC approved complaint handling process brochure at time of account opening.

(3) For order-execution service accounts, the Dealer Member does not have to provide the relationship disclosure information required under subparagraph 2(c), provided that disclosure is made in compliance with the requirements in Rule 3200.

(4) For managed accounts, the required disclosure referred to in subparagraph 2(c)(iii) does not apply and the relationship disclosure provided by the Dealer Member must include a statement that ongoing suitability is provided as part of the managed account services.

XX06. Review of relationship disclosure materials

(1) Pursuant to Rule 1300.2, the relationship disclosure provided to the client must be approved by a partner, director, officer or designated supervisor. This approval must occur regardless of the form the relationship disclosure takes. If the document is a standardized document, the supervisor who approves new accounts must ensure that the correct document is used in each client circumstance. If the relationship disclosure is a customized document for each client, the designated supervisor must approve each document.

XX07. Client acknowledgement of receipt of account related documents

(1) The Dealer Member must maintain an audit trail to evidence that account related documents required by IIROC Rules have been provided to the client. In addition, Dealer Members must obtain their clients' acknowledgement of receipt of the "know your client" information form and account relationship disclosure materials. A client signature acknowledging receipt is preferred, but not required. If the client's signature is not obtained, some other method of documenting the client's acknowledgement of receipt of this information must be used."

Attachment B

PROPOSALS TO IMPLEMENT THE CORE PRINCIPLES OF THE CLIENT RELATIONSHIP MODEL

PROPOSED AMENDMENTS - NEW RULE XX00 - CONFLICTS OF INTEREST

1. New Rule XX00 is enacted, as follows:

"XX01. Responsibility to identify conflicts of interest

(1) Each Dealer Member and, where applicable, Approved Person shall take reasonable steps to identify existing and potential material conflicts of interest between the interests of the Dealer Member or Approved Person and the interests of the client.

(2) Where an Approved Person becomes aware of an existing or potential material conflict of interest, the existing or potential conflict shall be reported immediately to the Dealer Member.

XX02. Approved Person responsibility to address conflicts of interest

(1) The Approved Person must consider the implications of any existing or potential material conflicts of interest between the Approved Person and the client.

(2) The Approved Person must address all existing or potential material conflicts of interest between the Approved Person and the client in a fair, equitable and transparent manner, and consistent with the best interests of the client or clients.

(3) Any existing or potential material conflict of interest between the Approved Person and the client that cannot be addressed in a fair, equitable and transparent manner, and consistent with the best interests of the client or clients, must be avoided.

XX03. Dealer Member responsibility to address conflicts of interest

(1) The Dealer Member must consider the implications of any existing or potential material conflicts of interest between the Dealer Member and the client.

(2) The Dealer Member must address the existing or potential material conflict of interest in a fair, equitable and transparent manner, and considering the best interests of the client or clients.

(3) Any existing or potential material conflict of interest between the Dealer Member and the client that cannot be addressed in a fair, equitable and transparent manner, and considering the best interests of the client or clients, must be avoided.

(4) The Dealer Member must adequately supervise how existing or potential material conflicts of interest between the Approved Person and the client are addressed by its Approved Persons pursuant to section XX02.

XX04. Responsibility to disclose conflicts of interest

(1) Unless a material conflict of interest has been avoided, the conflict of interest must be disclosed to the client in all cases where a reasonable client would expect to be informed:

(a) for new clients, prior to opening an account for the client; and

(b) for existing clients, either as the conflict occurs or, in the case of a transaction related conflict of interest, prior to entering into the transaction with the client.

XX05. Conflicts of interest policies and procedures

(1) Each Dealer Member shall develop and maintain written policies and procedures to be followed in identifying, avoiding, disclosing and addressing material conflict of interest situations."

Attachment C

PROPOSALS TO IMPLEMENT THE CORE PRINCIPLES OF THE CLIENT RELATIONSHIP MODEL

PROPOSED AMENDMENTS - AMENDED RULE 1300 - SUPERVISION OF ACCOUNTS

1. Rule 1300 subsections 1300.1(p) through (v) are repealed and replaced as follows:

"Suitability determination required when accepting order

(p) Subject to Rules 1300.1(t) and 1300.1(s), each Dealer Member shall use due diligence to ensure that the acceptance of any order from a client is suitable for such client based on factors including the client's current financial situation, investment knowledge, investment objectives and time horizon, risk tolerance and the account's current investment portfolio composition and risk level.

Suitability determination required when recommendation provided

(q) Each Dealer Member, when recommending to a client the purchase, sale, exchange or holding of any security, shall use due diligence to ensure that the recommendation is suitable for such client based on factors including the client's current financial situation, investment knowledge, investment objectives and time horizon, risk tolerance and the account's current investment portfolio composition and risk level.

Suitability determination required for account positions held when certain events occur

(r) Each Dealer Member shall, subject to Rules 1300.1(t) and 1300.1(u), use due diligence to ensure that the positions held in a client's account or accounts are suitable for such client based on factors including the client's current financial situation, investment knowledge, investment objectives and time horizon, risk tolerance and the account's current investment portfolio composition and risk level whenever one or more of the following trigger events occurs:

(i) Securities are received into the client's account by way of deposit or transfer; or

(ii) There is a change in the registered representative, investment representative or portfolio manager responsible for the account; or

(iii) There has been a material change to the client's life circumstances or objectives that has resulted in revisions to the client's "know your client" information as maintained by the Dealer Member.

Suitability of investments in client accounts

(s) To comply with the requirements under Rules 1300.1(p), 1300.1(q) and 1300.1(r), the Dealer Member must use due diligence to ensure that:

(i) The suitability of all positions in the client's account is reviewed whenever a suitability determination is required; and

(ii) The client receives appropriate advice in response to the suitability review that has been conducted.

Suitability determination not required

(t) Each Dealer Member that has applied for and received approval from the Corporation pursuant to Rule 1300.1(v), is not required to comply with Rule 1300.1(p), when accepting orders from a client where no recommendation is provided, to make a determination that the order is suitable for such client.

(u) Each Dealer Member that executes a trade on the instructions of another Dealer Member, portfolio manager, investment counsel, limited market dealer, bank, trust company or insurer, pursuant to Section I.B (3) of Rule 2700 is not required to comply with Rule 1300.1(p).

Corporation approval

(v) The Corporation, in its discretion, shall only grant such approval where the Corporation is satisfied that the Dealer Member will comply with the policies and procedures outlined in Rule 3200. The application for approval shall be accompanied by a copy of the policies and procedures of the Dealer Member. Following

such approval, any material changes in the policies and procedures of the Dealer Member shall promptly be submitted to the Corporation."

2. References in Rules1300 and 3200 to subsections 1300.1(p) and 1300.1(t) are amended as follows:

(a) References to existing subsection 1300.1(p) are repealed and replaced by references to new subsections 1300.1(p) and 1300.1(r); and

(b) References to existing subsection 1300.1(t) are repealed and replaced by references to new subsection1300.1(v).

Attachment D

PROPOSALS TO IMPLEMENT THE CORE PRINCIPLES OF THE CLIENT RELATIONSHIP MODEL

PROPOSED AMENDMENTS – AMENDED RULE 200.1 – MINIMUM RECORDS

1. Rule 200 is amended by renumbering existing subsections 200.1(d) through (n) as subsections 200.1(g) through (q).

2. Rule 200 is amended by adding new subsections 200.1(d), 200.1(e) and 200.1(f) as follows:

"(d) Client account cost reports for all accounts other than those held by institutional clients, itemizing security position cost information as follows:

(1) For all new security positions added to the account on or after the latest of:

(i) [Date of implementation],

(ii) The date the account was opened or

(iii) If applicable, the date the account was received in by the Dealer Member as a transferred account,

the original cost of the position.

(2) For all existing security positions in the account as of [Date of implementation], the original cost of the position.

Where original cost information is unavailable or is known to be inaccurate, Dealer Members may elect to provide market value information as at [Date of implementation], or as at an earlier date (referred to as "point in time market value") instead of original cost information, provided that it is done for all similar accounts and as at the same date.

Where the account was received in by the Dealer Member as a transferred account, the market value of the positions as at the date the account was received in via transfer (also referred to as "point in time market value") may be used instead of original cost.

For each security position, the current market value as at the report date shall be provided as a comparison to the cost information. The basis for costing each position (either original cost or point in time market value) must be disclosed.

Client account cost reports shall be sent to clients annually, at a minimum.

(e) For all accounts other than those held by institutional clients, client account performance information disclosing the annual and cumulative realized and unrealized income and capital gains in the client's account. This account performance information shall be sent to clients annually, at a minimum.

(f) For all accounts other than those held by institutional clients, client account performance reports itemizing account annualized compound percentage returns for the client's account.

Account annualized compound percentage return information

Where the account has existed for more than one year, account annualized compound percentage return information shall be provided indicating the account's performance for the past one, three, five and ten year periods and for the period since account inception. Where the account has existed for less than one year, account annualized compound percentage return information shall not be provided. The computational method used in determining annualized compound percentage return information shall be a method acceptable to the Corporation.

The report containing account annualized compound percentage return information shall be sent to clients annually, at a minimum."

3. The Guide to Interpretation of Rule 200.1 is amended by renumbering guide items (d) through (n) as guide items (g) through (q).

4. The Guide to Interpretation of Rule 200.1 is amended by adding new guide items (d) through (f) as follows:

"(d) "**Client account cost reports"**

Reports must include all client account security and other investment product positions held by the Dealer Member for the client in nominee name or physically in client name and all other client account positions for which the Dealer Member continues to receive compensation, subject to the exceptions below.

Where, pursuant to Rule 200.1(d)(2), the original cost information is unavailable and the point in time market value amount cannot be reliably measured for an individual position held, the cost information for the position shall be reported as not determinable.

Where the market value for a particular position cannot be reliably measured, the current market value information for the position shall be reported as not determinable. In such instance, a disclosure in the client account cost report shall inform the client that the information is not determinable and why the information is not determinable.

The information provided in the client account cost report may be provided to the client on either a dollar amount or dollar amount per share basis.

The client account cost report may be provided to the client as part of the client account statement, referred to in Rule 100.2(c), or separately.

(e) "**Cumulative account performance information"**

The cumulative account performance information must be determined based on all client account security and other investment product positions held by the Dealer Member for the client in nominee name or physically in client name and all other client account positions for which the Dealer Member continues to receive compensation, subject to the exceptions below.

Where there are one or more positions held in the client account for which the current market value is not determinable, the position(s) shall be considered to have no value in the determination of cumulative account performance. In such instance, a disclosure in the cumulative account performance information shall inform the client that the value of the positions has been set at nil for account performance calculation purposes and why.

At the option of the Dealer Member, clients may be provided with portfolio level (portfolio level being a consolidation of all account positions and debit/credit money balances of the same client) cumulative account performance information.

At the option of the Dealer Member, clients may instead be provided with cumulative account performance information that delineates advised/non-advised account positions.

The cumulative account performance information may be provided to the client as part of the client account statement, referred to in Rule 100.2(c), or separately.

(f) "**Account annualized compound percentage return information**"

The account annualized compound percentage return information must be determined based on all client security and other investment product positions held by the Dealer Member for the client in nominee name or physically in client name and all other client account positions for which the Dealer Member continues to receive compensation, subject to the exceptions below.

Where there are one or more positions held in the client account for which the current market value is not determinable, the position(s) shall be considered to have no value in the determination of annualized compound percentage returns. In such instance, a disclosure in the annualized compound percentage return information shall inform the client that the value of the position(s) has been set at nil for percentage calculation purposes and why.

At the option of the Dealer Member, clients may be provided with portfolio level (portfolio level being a consolidation of all account positions and debit/credit money balances of the same client) annualized compound percentage return information.

At the option of the Dealer Member, clients may instead be provided with annualized compound percentage return information that delineates advised/non-advised account positions.

Account annualized compound percentage return information may be provided to the client as part of the client account statement, referred to in Rule 100.2(c), or separately."

Attachment E

PROPOSALS TO IMPLEMENT THE CORE PRINCIPLES OF THE CLIENT RELATIONSHIP MODEL

PROPOSED TRANSITION PERIODS FROM DATE OF IMPLEMENTATION NOTICE PUBLICATION

Relationship disclosure requirements	
New clients	6 months
Existing clients	3 years
Conflicts of interest management / disclosure requirements	
Provisions relating to conflict identification and avoiding and addressing conflicts	Immediate
Provisions relating to conflict disclosure: (i) prior to opening an account (ii) inclusion of conflicts disclosure in relationship disclosure information provided to new clients (iii) inclusion of conflicts disclosure in relationship disclosure information provided to existing clients (iv) prior to entering into a transaction	 Immediate 6 months 3 years Immediate
Account suitability requirements	
Trigger event suitability assessment requirements	6 months
Account performance reporting requirements	
Security position cost disclosure	1 year
Account activity disclosure	1 year
Account percentage return disclosure (i) Where percentage return information is currently, provided, an IIROC approved calculation method must be used or the information may not be provided to any client (ii) Mandatory percentage return reporting for all retail clients	 6 months 2 years

Attachment F

IIROC RULES NOTICE

DRAFT GUIDANCE NOTE

DEALER MEMBER RULES

CLIENT RELATIONSHIP MODEL

INTRODUCTION

This Guidance Note provides guidance for Dealer Members on compliance with the new requirements introduced under the Client Relationship Model (CRM) project. The new Rules and amendments under the CRM project address:

1. Relationship disclosure;

2. Conflicts of interest management/disclosure;

3. Suitability assessment; and

4. Account performance reporting.

While each of these issues can be viewed in isolation, the intent of the CRM project is that the different elements work together within the larger CRM framework and the existing Rules. Essentially, each of the requirements is a part of the broader fundamental obligation of the Dealer Member and its representatives under National Instrument 31-505 to deal fairly, honestly and in good faith with clients.

Wherever possible, the new CRM requirements have been created with the intent of allowing Dealer Members to leverage off of existing processes. However, certain aspects will require Dealer Members to develop new systems, which may pose some significant operational challenges. Therefore, with the input of Dealer Members and other industry participants, IIROC staff have developed a transition plan for implementation of the CRM Rules and amendments. Details of the transition periods that have been approved by the IIROC Board are attached as Attachment XX to the related IIROC Rule Notice 10-xxxx announcing the implementation of IIROC's CRM requirements.

RELATIONSHIP DISCLOSURE REQUIREMENTS

Rule XX00 establishes minimum standards for client/firm relationship disclosure to be provided by Dealer Members to clients at the time of account opening. The policy rationale underlying the Rule is that all clients should have a good understanding of the services they will be provided when they open an account.

Form and format of relationship disclosure

The Rule provides for a degree of flexibility as to the form and format of the relationship disclosure, but in all cases the information must be in writing, in plain language and must contain all of the required elements set out in Section XX05. The Rule allows for standardized disclosure to be provided to particular groups of clients, or all clients. Where the Rule requires the Dealer Member to advise as to whether optional services can be obtained from the Dealer Member, the costs associated with such services must be provided.

Content of relationship disclosure

The relationship disclosure to be provided to the client must include a description of the products and services of the Dealer Member, the nature of the account and the responsibilities of the Dealer Member. IIROC staff understands that many Dealer Members are already providing clients with marketing information that includes at least some information on products, services and account types offered. However, to provide more complete information, the client should also be advised as to specific limitations and Dealer Member responsibilities that might exist for the different classes of accounts it offers (for example, an order-execution service account versus an advisory account). The relationship disclosure information will help the clients understand:

1. why the "know your client" information the client provides the Dealer Member is important;

2. what service levels the client can expect from the Dealer Member once the account has been opened; and

3. what information the Dealer Member will provide the client to update them on the status of the account.

One of the fundamentals in the advisory relationship is the requirement for the Dealer Member to satisfy the investment suitability requirements contained in Rule 1300.1. Accordingly, IIROC staff expects the Dealer Member to provide a fulsome, clear and meaningful explanation of its suitability obligation in the relationship disclosure information it provides to its clients (subparagraph (c) of Section XX05). To ensure accurate client understanding of this service, the relationship disclosure must include a description of both when and how suitability assessments will be made. Further, the client should be made aware of the limitations on the obligation and whether account suitability reviews will be performed in situations apart from those listed in the Rule. In particular, the Rule requires that clients be informed whether or not suitability reviews will be performed in response to significant market fluctuations. This will ensure that the client is aware of whether or not a portfolio suitability assessment will be performed during a period of significant market fluctuation.

The types of transaction, position and performance reporting to be provided to the client must also be disclosed to the client (subparagraph (d) of Section XX05). In the case of transaction and position reporting, the trade confirmation and account statement requirements themselves are unchanged; what has changed is that the client must be informed when this information will be sent to them. In the case of performance reporting, the requirements themselves are new and are being implemented over different transition periods as follows:

- Individual position cost disclosure - 1 year
- Account activity information - 1 year
- Account percentage return information - 2 years

As a result, in order to avoid having to regularly update the client relationship disclosures they are being provided, it may be more efficient for the Dealer Member to inform the client of its plans over the 2 year implementation period, so that the client is informed up-front as to the type(s) of performance reporting they will be provided immediately and the type(s) of reporting they can expect to receive over the next couple of years.

The disclosure required under subparagraph (e) is an extension of the new conflicts of interest management standards also introduced as part of CRM. Refer to the separate “Conflicts of interest management / disclosure requirements” section of this Guidance Note for further guidance on these new standards.

The disclosures required under subparagraphs (f), (g), (h) and (i) of Section XX05 are an extension of existing requirements relating to account operation and transaction fees/charges, account related documentation and client compliant handling. The Dealer Member requirements in these areas are unchanged; what has changed is that the client must be informed as part of the relationship disclosures of the types of fees/charges they can expect to incur, the account related documentation they will receive and the complaint handling process in place at the Dealer Member. Consistent with the requirements of National Instrument 31-103, IIROC staff expects the discussion of account operation and transaction fees/charges will include all charges a client may incur during the course of acquiring, selling or holding an investment product position, including amounts to be paid indirectly to the Dealer Member by the client. For example, mutual fund fees/charges disclosure should include a discussion of the management expenses that are deducted from fund performance by the mutual fund manager and the types of fees/charges that may be paid to the Dealer Member by the mutual fund manager from these collected management expenses.

Content differences for different account types

The obligations of Dealer Members to provide certain specific disclosures regarding suitability will vary for order-execution service accounts and managed accounts, in that there is no suitability obligation regarding order-execution service accounts and managed accounts must be monitored and supervised according to the specific standards imposed under Rules 1300 and 2500. Apart from these limited exceptions for order-execution service accounts and managed accounts, all of the required elements listed in Rule XX00 must be addressed in the Dealer Member’s relationship disclosure.

Other information that may be included in the relationship disclosure

Beyond the required content set out in Rule XX00, the Dealer Member may also elect to include additional information in the relationship disclosure. In consulting with Dealer Members in the rule development process, IIROC staff has noted that some Dealer Members currently recommend steps to be taken by their clients to maintain a successful relationship with the firm. These include:

1. Carefully and promptly reviewing all documentation provided by the Dealer Member that relates to the operation of the account, account investment recommendations, account investment transactions and account investment holdings. This would include the “know your client” information collection form maintained by the Dealer Member for the account; conflicts of interest disclosures; descriptions of all transaction costs and account service fees and charges relating to the account; trade confirmations; and account statements.

2. Promptly informing the Dealer Member of changes to the client's life circumstances or objectives that may materially affect the accuracy of the "know your client" information collection form maintained by the Dealer Member for the account.

3. Promptly informing the Dealer Member of any trade confirmation or account statement errors.

4. Proactively asking questions and requesting information about the account.

5. Contacting the Dealer Member immediately if the client is unsatisfied with the handling of the affairs in the account.

Client acknowledgement of receipt of important account related documents

To reflect the importance of the account relationship disclosure information and the "know your client" information collection form, receipt of these documents must be acknowledged by the client. While obtaining the client's signature is preferred, the requirements recognize that this is not always possible to obtain, particularly when the client is opening an account over the internet or from another location. As a result, where a signature cannot be obtained other forms of acknowledgement of client receipt such as a documented phone conversation or an e-mail or letter from the client are acceptable.

Discussion of relationship disclosure materials with clients

Although there are a variety of business models employed by Dealer Members, IIROC expects that in a typical face-to-face client meeting, the registered representative will sit down with the client and take him or her through the relationship disclosure materials, the "know your client" information collection form and other important account opening documentation in order to ensure that the client has a clear understanding of the documents' content. Through this review with the client the representative will collect the necessary "know your client" information, complete the account opening forms and obtain the required client signatures and/or acknowledgements. The client would then be provided with a copy of the forms and disclosure documents. Ideally, throughout this process, the client will be raising any questions and the representative will be providing meaningful responses. The intent of the relationship disclosure is to ensure that all clients have answers to some basic questions on the account relationship, whether or not the client raises these questions with their representative.

Clients that must be provided with relationship disclosure information

Dealer Members are required to provide the relationship disclosure information to all retail clients. In the case of retail clients of Dealer Members that are introducing brokers, this obligation must be met by the introducing broker. It is expected that new clients will be provided with the information at the time of account opening. IIROC staff acknowledges that there are significant logistical concerns involved in distributing the information to existing clients but believe it is equally important that existing clients clearly understand the relationship they have with their Dealer Member and advisor. To enable Dealer Members to address the logistical issues involved in distributing the information to existing clients, a three-year transition period to provide the information to existing clients has been adopted. This three-year period is consistent with IIROC's current expectations regarding the updating of key account related documents.

Significant changes to disclosure information

Where significant changes to the relationship disclosure information have occurred, it is expected that the Dealer Member will provide timely notice to clients of any changes. This could be accomplished by including details of the updated information with a regular client communication, such as the client statements.

As noted in Section XX07, Dealer Members are required to maintain an audit trail that evidences that the client has acknowledged receipt of the "know your client" information form and the account relationship disclosure materials. The "best practice" would be to obtain a signed client acknowledgement, but Dealer Members may also satisfy this requirement both for the initial disclosure and for subsequent updates through other means. Dealer Members that intend to rely on electronic delivery of the information would be expected to satisfy the requirements noted in IDA Member Regulation Notice MR-008.

CONFLICTS OF INTEREST MANAGEMENT / DISCLOSURE REQUIREMENTS

There are a number of provisions in the existing IIROC Rules that set out Dealer Member and Approved Person obligations relating to specific conflict of interest situations between Dealer Members and clients and between Approved Persons and clients. In addition to these existing specific obligations, Rule XX00 further clarifies the existing obligations that Dealer Members and Approved Persons have to manage conflicts of interest with their clients. These obligations require Dealer Members to have written policies and procedures in place for identifying and addressing material conflicts of interest and to carry out these policies and procedures. Rule XXOO also sets out a general framework for:

- identifying conflict of interest situations; and

- addressing conflict of interest situations through/by:
    - avoidance
    - disclosure
    - other approaches to control the situation

Approved Person responsibility to address conflicts of interest

- ***General requirement to address all conflicts of interest***

  Subsection XX02(2) requires that all existing or potential material conflicts of interest between an Approved Person and a client must be addressed by the Approved Person "in a fair, equitable and transparent manner, and consistent with the best interests of the client or clients." Conflicts can be addressed by avoiding, disclosing or otherwise controlling the conflict of interest situation. In addition to this general requirement to address material conflicts of interest between the Approved Person and the client:

  - Section XX02(3) requires that "Any existing or potential material conflict of interest between the Approved Person and the client that cannot be addressed in a fair, equitable and transparent manner, and consistent with the best interests of the client or clients, must be avoided."; and
  - Section XX04 requires that "Unless a material conflict of interest has been avoided, the conflict of interest must be disclosed to the client in all cases where a reasonable client would expect to be informed."

  As a result, the requirements collectively mandate when a conflict of interest between an Approved Person and a client must be addressed by avoiding the conflict, or must be addressed at least in part by disclosing the conflict of interest to the client. The requirements do not mandate the other approaches which must be used to further control the conflict of interest situation.

  Sub-section 13.4(2) of National Instrument 31-103 (N1 31-103) requires that "A registered firm must respond to an existing or potential conflict of interest".

  Having said that, material conflict of interest situations can only be addressed / responded to by:

  - avoiding the situation which gives rise to the conflict of interest; or
  - controlling the situation as much as possible and/or disclosing the conflict of interest.

  As with the other elements of the CRM project, the Rule requiring that material conflicts of interest be addressed should be read in light of the fundamental statutory obligation imposed on all registrants to deal with clients fairly, honestly and in good faith. The intent of IIROC Rule XX02 is to provide greater clarity to Dealer Members as to how these basic principles can be satisfied when considering conflict of interest situations.

  In a number of cases, Approved Persons will address conflict of interest situations by disclosing it to the affected clients. However, in other cases, to properly address a material conflict, the Dealer Member may need to implement policies and procedures and the Approved Person will need to carry out procedures that go beyond simple disclosure. For instance, NI 31-103 requires registrants to execute a written agreement as well as providing prescribed disclosure prior to entering into a referral arrangement with a client. Other types of personal financial dealings, if permitted, may also necessitate additional measures, such as requiring the client to obtain independent advice before entering into a transaction.

- ***Conflict* avoidance**

  Subsection XX02(3) requires that "Any existing or potential material conflict of interest between the Approved Person and the client that cannot be addressed in a fair, equitable and transparent manner, and consistent with the best interests of the client or clients, must be avoided." When determining whether a conflict of interest between an Approved Person and a client must be avoided, Approved Persons should consider:

  - the interests of the client(s) involved; and
  - whether it is feasible to address the conflict of interest in any way other than by avoiding the situation giving rise to the conflict of interest.

Further, the guidance in Companion Policy 31-103CP provides the following general examples of material conflict of interest situations that must be avoided:

- the conflict of interest involves confidential, commercially sensitive or material, non-public information which the Dealer Member is prohibited from disclosing to the client and a reasonable client would expect to be provided with this information
- the conflict of interest is inconsistent with the interests of the client and/or there is a high risk of harm to the client and the situation cannot be addressed in any fashion to reduce this inconsistency/risk of harm; and
- the situation that gives rise to the conflict of interest is unethical or otherwise contrary to capital markets integrity

Consistent with the avoidance standard set out in Section XX02(3), the following are examples of specific rules that stipulate conflict of interest situations between an Approved Person and a client which must be avoided by the Approved Person:

1. A Registered Representative or Investment Representative may not engage in another gainful occupation if the specific occupation introduces inappropriate conflicts of interest, disrupts continuous client service or is disreputable [IIROC Dealer Member Rule 18].

2. A registered individual must not act as a director of another registered firm that is not an affiliate of an individual's sponsoring firm [NI 31-103, Section 4.1].

Conflict of interest situations between Dealer Members and clients

- ***General requirement to address all conflicts of interest***

Subsection XX03(2) requires that all existing or potential material conflicts of interest between a Dealer Member and a client must be addressed "in a fair, equitable and transparent manner, and considering the best interests of the client or clients." In applying this requirement, it is recognized that it is not always possible or practical for a Dealer Member to address all conflicts of interest in the best interests of each client when the conflict of interest situation involves multiple clients with competing interests.

The general approaches used by Approved Persons to address conflicts of interest between themselves and their client(s) must also be followed by Dealer Members when addressing conflict of interest situations between Dealer Member(s) and their clients. As previously stated, material conflict of interest situations can only be addressed / responded to by:

- avoiding the situation which gives rise to the conflict of interest; or
- controlling the situation as much as possible and/or disclosing the conflict of interest.

Companion Policy 31-103CP also sets additional guidance when the conflict of interest situation involves multiple clients with competing interests. Specifically, Dealer Members "should make reasonable efforts to be fair to all clients" and "should have internal systems to evaluate the balance of these [client] interests." The conflict of interest that arises between a Dealer Member's corporate client, issuing public securities and the Dealer Member's retail clients, who will be offered the new issue, is cited as an example of a competing interests scenario.

- ***Conflict avoidance***

Subsection XX03(3) requires that any "material conflict of interest between the Dealer Member and the client that cannot be addressed in a fair, equitable and transparent manner, and considering the best interests of the client or clients, must be avoided." In applying this subsection, Dealer Members should consider the same factors as an Approved Person would consider when assessing whether to avoid a conflict of interest with a client.

Consistent with the avoidance standard set out in Section XX03(3), the following are examples of specific rules that stipulate conflict of interest situations between a Dealer Member and a client which must be avoided by the Dealer Member:

1. All client orders must be given priority over all proprietary orders for the same security at the same price in order to avoid a conflict of interest between the Dealer Member and its client with respect to that trading opportunity [IIROC Dealer Member Rule 29.3(A)].

2. A Dealer Member shall not trade, or permit or arrange to trade, in reliance upon information regarding trades that have been made or which will be made for any discretionary or managed account [IIROC Dealer Member Rule 1300].

3. A Dealer Member is prohibited from issuing a research report for an equity or equity related security relating to an issuer for which the Dealer Member acted as manager or co-manager of (i) an initial public offering of equity or equity related securities, for 40 calendar days following the date of the offering, or (ii) a secondary offering of equity or equity related securities, for 10 calendar days following the date of the offering [IIROC Dealer Member Rule 3400.14].

- ***Supervision***

  Subsection XX03(4) requires that "The Dealer Member must adequately supervise how existing or potential material conflicts of interest between the Approved Person and the client are addressed by its Approved Persons pursuant to section XX02." This requirement is consistent with the general expectation that Dealer Members should adequately supervise all activities they undertake; in this case the conflict of interest management activities of their Approved Persons.

Conflict of interest disclosure

As previously stated, Section XX04 requires disclosure to the client of a material conflict of interest situation that has not been avoided "in all cases where a reasonable client would expect to be informed."

When determining whether a conflict of interest must be disclosed to the client, the guidance in Companion Policy 31-103CP requires Dealer Members to consider whether the conflict of interest affects the services that are being provided or that are proposed to be provided. As part of this guidance, the example of a registered individual recommending a security they own is cited and it is suggested that "this may constitute a material conflict which should be disclosed to the client before or at the time of the recommendation".

Consistent with the disclosure standard set out in XX04, the following are examples of specific Rules that stipulate conflict of interest situations which must be disclosed to the client by the Dealer Member:

1. Where one client has guaranteed the account obligations of another client, such that there are potentially conflicting client interests, the Dealer Member must disclose to the guarantor in writing that the suitability of the transactions in the guaranteed client's account will not be reviewed in relation to the guarantor's risk tolerance or investment objectives [IIROC Dealer Member Rule 100].

2. Each confirmation issued for trades involving securities:

   - of the Dealer Member or a related issuer of the Dealer Member, in the course of a distribution to the public; or

   - of a connected issuer of the Dealer Member

   must state that the securities are issued by the Dealer Member, a related issuer of the Dealer Member or a connected issuer of the Dealer Member, as the case may be. [IIROC Dealer Member Rule 200]

3. Dealer Members must comply with the following disclosure requirements for analyst research reports:

   (a) Dealer Members must disclose information in a research project which might reasonably be expected to indicate a potential conflict of interest on the part of the Dealer Member or the analyst in making a recommendation with regard to the issuer.

   (b) Any Dealer Member that distributes research reports to clients or prospective clients in its own name must disclose its research dissemination policies and procedures on its website or by other means.

   (c) Dealer Members must disclose in research reports if in the previous 12 months the analyst responsible for preparing the report received compensation based upon the Dealer Member's investment banking revenues.

   (d) Dealer Members must disclose in research reports if and to what extent an analyst has viewed the material operations of an issuer. Dealer Members must also disclose where there has been a payment or reimbursement by the issuer of the analyst's travel expenses for such visit.

   [IIROC Dealer Member Rule 3400]

In general, the guidance in Companion Policy 31-103CP concludes that the only scenario under which a material conflict (that has not been avoided) would not be disclosed to the client under the "reasonable client" test would be where the Dealer Member has taken other steps to control the conflict of interest and has effectively ensured, with reasonable confidence, that the risk of loss to the client has been eliminated. As a result, disclosure is fundamental in addressing / responding to material conflicts of interest.

The disclosure should be timely and meaningful to the client. Specifically, disclosure should be made before the product or service related to the conflict is sold or provided to the client. Further, the disclosure should be sufficient to provide the client with an understanding of the specific conflict. A generic form of disclosure simply stating that conflicts may arise will not satisfy the Dealer Member's obligation to respond to specific conflict of interest situations that may arise.

Furthermore, disclosure and informed consent is not an appropriate alternative to conflict avoidance in those cases where avoiding the conflict is the only reasonable response. Implied or expressed consent does not discharge a Dealer Member from the obligations to comply with their regulatory requirements.

Compensation-related conflicts of interest

Many conflict of interest situations are compensation-related, where the Approved Person's / Dealer Member's interest in being compensated for a transaction or service is inherently in conflict with a client's interest in growing their wealth. As part of the requirement to address these compensation-related conflicts of interest and consistent with the requirements set out in subsections XX02(2) and XX03(2) to address conflicts of interest:

- The Dealer Member should ensure its product and service offerings, including the fees associated with such offerings, are consistent with the overall wealth building objectives of its clientele; and

- The Approved Person should, in addition to determining, where applicable, whether a certain product or service is suitable for the client, ensure that the transaction, account and service fees and costs to be charged are fair and are properly disclosed to the client.

On the topic of compensation practices, Companion Policy 31-103CP states that "Registered firms should consider whether any particular benefits, compensation or remuneration practices are inconsistent with their obligations to clients, especially if the firm relies heavily on commission-based remuneration. For example, if there is a complex product that carries a high commission, the firm may decide that it is not appropriate to offer that product."

SUITABILITY ASSESSMENT

Trigger event suitability assessment requirements

Rule 1300 has been amended to expand the suitability obligations of the Dealer Member beyond the requirement to assess trade suitability at the time a trade recommendation is made. The intent is to provide investors with an added level of protection in situations where the risk profile of the client and the account portfolio diverge over time. Amended Rule 1300.1(r) requires that the account suitability be reviewed when any of the following additional triggering events occurs:

1. securities are transferred or deposited into the account,

2. there is a change of representative on the account, or

3. there is a material change to the "know your client" information for the account.

The general expectation is that all account suitability reviews required under Rule 1300 will be completed in a timely manner. In most cases, this means that the review should be completed within one day after the Dealer Member or its representative becomes aware of the fact that one of the triggering events noted in the Rule has occurred. Where warranted in a given case, such as a transfer of a block of accounts to a new advisor, a "reasonable time" standard would apply. In any case, and with the exception of automated transactions, the required account suitability reviews should be completed prior to, or at the time of, any subsequent trade within the account.

IIROC staff does not expect that Dealer Members would perform reviews in situations where a change in client information is not material or the Dealer Member is not made aware of the change in circumstances. The Dealer Member's policies and procedures should address the issue of materiality and ways to encourage clients to provide updates on changes to client information.

Suitability assessment requirement amendments under study

IIROC staff is in the process of considering further changes to the suitability requirements and providing guidance as to staff expectations for Dealer Member compliance. In some respects these will key off of other amendments under the CRM project (such as the requirement to provide each client a copy of their KYC information and the requirement to supervise compliance with the new suitability requirements). Additional guidance to Dealer Members will be issued[2] as part of this initiative.

PERFORMANCE REPORTING

One of the most significant parts of the CRM project is the creation of new standards for performance reporting. Many Dealer Members have, for some time, provided performance reporting to clients as one of the services they offer. The amendments to Rule 200.1 now require that certain basic performance information be provided to all clients, as each client should have sufficient information to:

- determine whether they have gained or lost money on the investments in their accounts; and
- make informed assessments of account performance over time.

Specifically, Dealer Members are now required to provide all retail clients with security position cost, account activity and percentage return information, in accordance with the transition periods set out in IIROC Rules Notice XX-XXXX, which announced the implementation of the IIROC CRM project Rule amendments.

Account position cost reporting

Annual client account position cost reports for all new and existing security positions must include the original cost of the position. The cost amount that must be disclosed, original cost, is the total amount paid for a security, including any commissions and related fees/charges.

Account activity reporting

Furthermore, Dealer Members must send client account performance information disclosing the annual and cumulative realized and unrealized income and capital gains in the client's account. The annual realized/unrealized income and capital gains in an account is the difference between the account opening market value and the account closing market value, net of account deposits and withdrawals. The cumulative realized/unrealized income and capital gains in an account is the sum of annual amounts reported for the years covered by the performance reporting.

Account percentage return reporting

Finally, Dealer Members must annually send percentage return information to clients, which must cover longer performance periods (i.e., 1, 3, 5 and 10 year periods and for the period since account inception date (or rule implementation date)) as the information becomes available.

IIROC staff has noted a number of operation issues regarding performance reporting, and these have been discussed at length in the rule making process. Many issues were pointed out to IIROC staff with respect to potential problems with the quality and availability of historical data. To eliminate these issues, Rule 200.1 allows Dealer Members to report the required information on a go forward basis as of the implementation date of the Rule.

Reporting transition provisions, options and exceptions

In order to in part address the operational challenges associated with performance reporting generally, the Rule and associated guidance allow for certain transition provisions, options and exceptions. In addition to the Rule implementation transition period, it was determined that certain transition provisions were necessary to ensure that the performance reporting requirements could be implemented on a prospective basis. Transition provisions are necessary to address the situation where at the implementation date, market value information and/or original cost information is unavailable for one of more account positions. Specifically, the transition provisions allow:

- for a "point in time market value" to be used as a proxy for original cost for positions held at implementation date where original cost information is unavailable (provided that this approach is disclosed to the client);
- for "no cost" or "cost not determinable" to be reported as the original cost for positions held at implementation date

[2] A draft of this proposed additional guidance, the draft Guidance Note entitled "Know your client and suitability", has been included as Attachment G to the Client Relationship Model proposals.

where neither original cost information nor a "point in time market value" is available (provided that this approach is disclosed to the client) – in such instance "no value" or "value not determinable" must also be reported as the market value of the position

- for "no value" or "value not determinable" to be reported as the market value for positions held at implementation date where the market value for the position cannot be reliably measured

Options for complying with the performance reporting requirements are necessary to facilitate clear reporting to the client. To assist in this objective, the performance reporting requirements give Dealer Members certain options to allow:

- for separation of performance reporting from the client account statement, which is a statement of client positions held on the control of the Dealer Member;

- in the case of individual position original cost information, that original cost information may be provided as either a dollar amount or as a dollar amount per share, provided the comparable market value information is provided on the same basis;

- in the case cumulative and percentage return information, for separation of reporting of information relating to non-advised positions from the reporting related to advised positions and for exclusion of previous performance information relating to transferred in positions; and

- in the case cumulative and percentage return information, for combined reporting across multiple accounts of the same client.

Limited exceptions to the performance reporting requirements have also been adopted to deal with unique account situations that may occur after implementation date. The exceptions allow:

- in the case of individual position original cost information, the reporting of a "point in time market value" (i.e., market value at time of transfer) as a proxy for original cost for positions transferred into the account after implementation date where original cost information in unavailable or where the Dealer Member has determined it does not want to include the performance of positions while they were held outside of the Dealer Member; and

- in the case of individual position original cost information, for "no value" or "value not determinable" to be reported as the market value comparative for positions held after implementation date where the market value for the position cannot be reliably measured.

In some situations, original cost information for account positions previously provided to clients may be subject to subsequent adjustments. For example, this would apply to account positions that have been subject to re-organizations. In such cases, the general rule to follow would be to adjust the position original cost in line with the information provided by the issuer. Dealer Members may contact IIROC staff regarding questions on specific cases, if required.

Performance reporting frequency

Under Rule 200.1(d), original cost information must be provided to all retail clients on at least an annual basis. Many Dealer Members already provide tax cost information in each client statement that is sent and therefore may decide to provide original cost information as a third column in this statement.

Under Rule 200.1(e), account activity information must be provided to all retail clients on at least an annual basis. To meet the requirement, Dealer Members must disclose the cumulative realized and unrealized capital gains on the client's account. Again, the expectation is that this information will be reported on a go forward basis to avoid issues with historical data.

Under Rule 200.1(f), percentage return information must be provided to all retail clients by the end of the rule implementation transition period of 2 years. The percentage return information must be reported on a 1, 3, 5, 10 year and since account inception basis, determined prospectively as information becomes available and must be calculated in accordance with a method acceptable to IIROC. For the purpose of the Rule, Dealer Members are advised that both dollar-weighted and time-weighted methods are acceptable to IIROC. In particular, this includes the Dietz and modified Dietz methods, daily valuation and any method permitted under the Global Investment Performance Standards endorsed by the CFA Institute.

Attachment G

IIROC RULES NOTICE

DRAFT GUIDANCE NOTE

DEALER MEMBER RULES

KNOW YOUR CLIENT AND SUITABILITY

This Guidance Note does not purport to amend statutory requirements or applicable IIROC Dealer Member Rules relating to the "know your client" and suitability obligations. Rather, it sets out IIROC's interpretation, expectations and suggested best practices relating to existing requirements in the IIROC Dealer Member Rules, as recently amended to implement the CSA Registration Reform Project.

While the best practices set out in this Guidance Note are intended to present acceptable methods that can be used to comply with the aforementioned IIROC requirements, they are not the only acceptable methods. Dealer Members may use alternative methods, provided that those methods demonstrably achieve the overall objective of the Rules. In any event, Dealer Members are encouraged to adopt a risk based approach when setting internal compliance procedures.

The Guidance Note also discusses certain of the Client Relationship Model proposals that will, when implemented, introduce additional suitability obligations.

OVERVIEW OF THE REQUIREMENTS

Dealer Members and Registered Representatives are reminded that compliance with the suitability requirements is fundamental to compliance with general business conduct standards and is essential to good business practice. The suitability requirement is also complementary to the fundamental obligation under securities legislation for all Dealer Members and their representatives to deal fairly, honestly and in good faith with clients. The fundamental obligation includes a duty to disclose known or discoverable risks to the investor before entering into any transaction for a particular security.

Most of the issues discussed in this Guidance Note apply to retail clients in an advisory relationship; however, some of the principles discussed may also be applicable when dealing with other types of clients or relationships. As previously noted, the Guidance Note does not purport to amend statutory requirements or applicable IIROC Dealer Member Rules relating to the "know your client" and suitability obligations. Accordingly, if a Rule does not apply to a particular type of client then any discussion or guidance provided with respect to that Rule will also not apply. For example, the obligation to deal fairly, honestly and in good faith with clients applies to all types of clients and relationships. The requirement to update the client's information at the time of material change applies to all clients. On the other hand, the requirement to determine a client's investment objectives and risk tolerance does not apply to institutional clients, as they are subject to a different suitability standard, or to clients who trade through order execution-only accounts.

COMPLIANCE WITH KNOW YOUR CLIENT REQUIREMENTS

The first step in satisfying IIROC's suitability requirements is to satisfy the new account application and "know your client" requirements.

Collection of "know your client" information - New account application requirements

Pursuant to current IIROC Dealer Member Rules, a new account application is required for each customer[3]. IIROC Dealer Member Rule 1300.2 requires that each account be opened pursuant to a new account form which includes, at a minimum, the applicable information required by Form 2, also referred to as the New Account Application Form. The information set out in Form 2 includes, among other things, the client's personal information, financial information, risk tolerance, investment objectives, and disclosure of whether the client is an insider of a public corporation.

Dealer Members should note that the recent amendments to IIROC Rules to implement the Registration Reform project eliminated the use of the word "form" from the term "new account application form" to recognize that the completion of account applications and the collection of "know your client" information is frequently completed/done electronically.

Conditions under which one account application may be used for more than one account:

In accordance with recent Rule amendments which were necessary to implement the CSA Registration Reform Project, Dealer

[3] IIROC Dealer Member Rule 2500, Part II – Opening New Accounts, Introduction.

Member Rule 2500 has been amended to allow a Dealer Member to obtain one account application for multiple accounts (e.g. a client's cash, margin and certain registered accounts) of the same client[4] provided that:

- in the case of individuals, the account beneficial owner is the identical individual for all of the accounts;
- in the case of non-individuals, the account beneficial owner is the identical legal entity for all of the accounts;
- the client's investment objectives and risk tolerance are identical for all of the accounts;
- the Dealer Member has the ability to supervise each of the accounts, including the review of "know your client" information updates and orders for suitability purposes, on a multiple-account basis; and
- the client understands and acknowledges that the information collected in the one application will be used to assess suitability on a multiple-account basis.

Given these conditions, not all accounts of the same client can necessarily be opened using a single account application.

Examples of accounts where a separate account application would be required:

As explained above, in order to be able to rely on a single account application for multiple accounts of the same client, the beneficial owner of each account must be identical. Accordingly, a separate account application would be required if that same client held a beneficial interest in a joint, corporate or trust account.

Joint account - The beneficial owners of a joint account are not identical to the beneficial owner of an individual account.

Corporate account - Although the ultimate beneficial owner of a personal corporation may be the same individual as the client who has a cash or margin account, the same account application can not be used to open a corporate account, given that the account holder is the corporation and not the corporation's beneficial owner / shareholder. The information required to complete the account application is therefore, the corporation's information. Furthermore, the shareholders (beneficial owners) of a corporation are separate and distinct from the corporate legal entity. The contractual relationship arising out of the creation of the account is between the Dealer Member and the corporation.

Trust accounts - "In Trust For" accounts also require a separate account application as they have unique investment objectives that are determined by the Trustee, in accordance with the terms of the trust. Furthermore, there is no contractual relationship between the Dealer Member and the beneficial owner(s) of the trust. Rather, the contractual relationship is between the Dealer Member and the trustee, who is required to operate the account in accordance with the terms of the trust.

Know your client information items to be collected and assessed

Under the current rules, there are several questions that Registered Representatives must ask their clients in order to satisfy their "know your client" obligation and equip themselves to conduct a proper suitability assessment. Some of the information collected, such a client's net worth, age and investment experience, can be answered by the client. Other factors, such a client's risk tolerance and investment objectives may, however require further discussion and assessment. Registered Representatives are reminded that the client's investment objectives and risk tolerance must be assessed based on the client's financial and personal circumstances and must be reasonable in light of those circumstances. The reasonableness of such information should be reviewed by the Registered Representative and the Dealer Member during the account opening and account approval process. For example, designating an 80% high risk tolerance for an elderly client may be unreasonable if the client has a modest net worth and has opened the account to invest a substantial portion of her net worth. On the other hand, the 80% high risk tolerance may not be unreasonable if the elderly client has a substantial net worth and opens an account to invest a small fraction of her net worth.

Time horizon

As per Dealer Member Rule 1300, a client's investment objectives, risk tolerance, investment knowledge and financial situation must be considered when assessing the suitability of orders and recommendations. Dealer Members are reminded that the factors set out in Dealer Member Rules 1300.1(p) and (q) are not exhaustive. In order to meet the "know your client" requirements, Registered Representatives need to understand the client's personal circumstances which include understanding the client's time horizon. The client's age is one indication of the client's time horizon. Although time horizon is not a separate requirement, in order to properly assess and record a client's investment objectives and risk tolerance, Registered Representatives should consider the client's time horizon. Time horizon should be determined by considering when the client

[4] Recent amendments to implement the CSA Registration Reform Project approved by the IIROC Board of Directors on June 25, 2009 were implemented on September 28, 2009.

will need to access some or all of their money. Where a client identifies his / her time horizon, the Registered Representative has the responsibility to assess its feasibility and reasonableness in comparison to the client's age, risk tolerance, and other particular circumstances.

Periodic updates and review

The account information must be updated any time there is a material change in a client's circumstances.[5] The following procedures are considered best practices for satisfying this requirement:

- Registered Representatives periodically inquire with each client as to whether there are any material changes in the client's circumstances. It is also acceptable for a Registered Representative to make such inquiries when the Registered Representative meets a client to review his/her portfolio, otherwise corresponds with the client to discuss other account related matters or annually contacts the client to verify the accuracy of the account information.

- The Dealer Member, in its account opening documentation, clearly informs clients of the client's obligation to notify their respective advisors any time there is a material change in their circumstances.

- Where Registered Representatives conduct periodic suitability reviews, use the review discussion as an opportunity to confirm with the client as to whether there are any material changes in the client's circumstances.

COMPLIANCE WITH THE SUITABILITY ASSESSMENT REQUIREMENTS

Pursuant to IIROC Dealer Member Rules, orders and recommendations need to be reviewed to ensure that they are suitable for the particular client.[6] Suitability needs to be considered in light of other investments within the client's account or accounts and in relation to his / her financial condition, investment knowledge, investment objectives and risk tolerance. The issue of whether the requisite suitability analysis should consider other investments in a client's account or accounts is discussed later in this Guidance Note.

The regulatory obligation to ensure that orders and recommendations are suitable includes not only an obligation to ensure that the specific security is suitable for the client but also that the order type, along with the trading strategy recommended and/or adopted are also suitable for the client. As an example, the risk profile of a client who fully pays for a position in a specific security as a core long term holding is significantly different from the risk profile of a client buying the same security on margin, as part of a day trading strategy.

Dealer Members are also reminded that the suitability analysis starts before the order is even received, recommended or executed. The Dealer Member and Registered Representatives, at the time of account opening, should ensure that the account type (margin, trust, option accounts, etc.) is appropriate for the client given the client's particular circumstances.

Furthermore, Dealer Members and Registered Representatives need to understand the risks and other characteristics associated with the investment products they approve or recommend for sale.

Product suitability

The suitability assessment obligations include a requirement to know and understand the characteristics and risks associated with any investment product approved or recommended to clients. Dealer Members have the responsibility to assess the risks associated with the products that Dealer Members approve for sale. Registered Representatives should understand, and be able to clearly explain to the client, the reasons that a specific security is appropriate and suitable for the client.

Please refer to the "Best Practices for product due diligence" Guidance Note 09-0087 published on March 25, 2009 which sets out IIROC's expectations regarding procedures and criteria that Dealer Members should consider when assessing and introducing products that they approve or recommend for sale. As explained in that Guidance Note, adequate procedures for reviewing products before they are offered to clients can greatly enhance the ability to detect unsuitable recommendations.

Account suitability vs. multiple account suitability

Consistent with the collection of "know your client" information for multiple accounts, IIROC Rules permit that a single set of "know your client" information may be used, for suitability assessment purposes, for multiple accounts held by the same client provided that:

- the beneficial owner is the identical individual or legal entity for all of the accounts;

[5] IIROC Dealer Member Rule 2500 and 2700.
[6] IIROC Dealer Member Rule 1300.

- the client's investment objectives and risk tolerance are identical for all of the accounts;
- the Dealer Member has the ability to supervise accounts, including the review of "know your client" information updates and orders for suitability purposes, on a multiple-account basis; and
- the client understands and acknowledges that the information collected in this single set of "know your client" information will be used to assess suitability on a multiple-account basis.

To clarify, the question of whether suitability must be assessed on either a single account or multiple-account basis will depend on: i) whether the client has identical objectives and risk tolerance for all of those accounts; ii) the client's agreement or understanding with the Dealer Member in that regard; and iii) the Dealer Member's ability to supervise on a multiple-account basis. Once that has been decided, the basis upon which suitability will be assessed should be evidenced on the client's account application and applied consistently throughout the relationship. This would also mean that once a Dealer Member sets up the account on a certain basis (for example that suitability of orders and recommendations will be assessed on a multiple-account basis) the Dealer Member and Registered Representative cannot assess suitability on a different basis from time to time (for example on a single account basis).

Unsuitable investments

An unsuitable investment and/or recommendation is one that is inconsistent with the client's personal circumstances including financial situation, investment knowledge, investment objectives, risk tolerance as current composition, duration and risk level of the other investments within the client's account or accounts at the time of the investment and/or recommendation.

Dealer Members and Registered Representatives have a general suitability requirement with respect to orders they accept or trades they recommend.[7] Dealer Members and Registered Representatives also have a statutory obligation to deal with clients fairly, honestly and in good faith. As a result, whenever an unsuitable investment is identified within an account, either at the time of the investment is recommended or the investment order is accepted or subsequent to that time, there is an obligation to take appropriate action. An unsuitable investment may be identified by the Registered Representative at the time of updating the client's account information, to reflect a material change in the client's circumstances as required by IIROC Dealer Member Rule 2500, or when conducting a periodic suitability review. The Dealer Member may identify an unsuitable investment within an account when conducting supervisory activities, including account activity reviews as required by Dealer Member Rule 2500. The obligation to take appropriate action when an unsuitable investment is identified within an account is consistent with Dealer Member Rule 2500, which explains that the meaning of the term "review" includes a preliminary screening to detect items for further investigation.

An account may include an unsuitable investment for a variety of reasons, for instance there may have been a previously executed unsolicited order or an unsuitable recommendation by a former Registered Representative. Furthermore, a sector related change or material change in an issuer's circumstances may cause a shift in the risk associated with a particular security. Where an unsuitable investment is identified within an account, the Registered Representative should take appropriate measures to ensure the client receives advice considering the client's objectives, risk tolerance, and other particular circumstances. An appropriate measure or course of action may include contacting the client in a timely manner to recommend changes. Where a client does not want to dispose of the unsuitable investment, it may be appropriate to recommend changes to other investments within the account in order to ensure the suitability of the overall portfolio. In any event, Registered Representatives are encouraged to contact the client in order to discuss their concerns and to document any actions that they take in response to the issue. Registered Representatives should consult their Supervisor or Compliance Department personnel regarding the Dealer Member's internal policies in handling unsuitable investments.

Unsolicited unsuitable orders

Where a Registered Representative receives an unsolicited order that is unsuitable in relation to the client's objectives, risk tolerance and other particular circumstances, it is not sufficient to merely mark the order as unsolicited. The Registered Representative needs to take appropriate measures to deal with the unsuitable order. The extent of the Registered Representative's obligation partially depends on his/her relationship with the client. Appropriate measures may include providing clients with cautionary advice and documenting the details of the cautionary advice, or recommending changes to other investments within the account. In any event, Registered Representatives are encouraged to document any actions that they have taken. If the Registered Representative is unsure of how to deal effectively with an unsuitable order, they should consult their Supervisor or Compliance Department personnel in order to understand the Dealer Member's internal procedures for dealing with this issue.

[7] Dealer Member Rules 1300.

Inappropriate updates

When a potentially unsuitable investment is identified within a client's account or a potentially unsuitable order is received from the client, the Registered Representative should discuss with the client whether there have been any changes to the client's circumstances that would warrant amendments to the "know your client" information.

Registered Representatives should note that it is inappropriate to update or alter the client's "know your client" information in an effort to justify the suitability of an investment, order or recommendation that is otherwise unsuitable for the client.

To clarify, the Registered Representative should remind the client of the "know your client" information previously collected and update that information only if there is a material change in the client's circumstances. The Registered Representative should not be soliciting the client's consent to change their "know your client" information if the purpose of the change is solely to create the appearance of a suitable order.

Pending proposals

As per the proposed Client Relationship Model, IIROC is proposing to amend its Dealer Member Rules to require that a suitability analysis also be performed whenever one or more of the following triggering events occur:

- any time there is a material change in the customer's circumstances;
- when there is a change in the registered representative, investment representative or portfolio manager assigned to the account; or
- when securities are received into the client's account by way of deposit or transfer.

The current suitability assessment requirements, set out in IIROC Dealer Member Rule 1300, are triggered when either an order is accepted from a client or a trade is recommended to a client.

Best practices for maintaining a suitable client account

It is advantageous to clients, Dealer Members and the industry as a whole, as well as consistent with good business practices, that Registered Representatives and Dealer Members conduct more holistic suitability reviews.

In other words, Dealer Members are encouraged to adopt best practices which would not only allow them to comply with the current order / recommendation-triggered suitability assessment requirements set out in IIROC Dealer Member Rule 1300.1, but also assist in the ongoing maintenance of a suitable client portfolio. The best practices would include:

- Adopting policies and procedures requiring, when appropriate, periodic suitability reviews of client accounts:
- Conducting suitability reviews of accounts that may be affected by significant market events;
- Conducting suitability reviews of accounts holding securities of an issuer that has undergone a material change in its risk profile; and
- Adopting written policies and procedures that require a suitability review of an account at the time of the account is transferred to a new advisor or a new Dealer Member, or where there is a material change in a customer's circumstances.

Attachment G

IIROC RULES NOTICE

GUIDANCE NOTE – DRAFT

DEALER MEMBER RULES

Know your client and ~~Suitability Guidelines~~suitability

This Guidance Note does not purport to amend statutory requirements or applicable IIROC Dealer Member Rules relating to the "know your client" and suitability obligations. Rather, it sets out IIROC's interpretation, expectations and suggested best practices relating to ~~the know your client and suitability~~existing requirements ~~as currently reflected~~ in the IIROC Dealer Member Rules~~.~~, as recently amended to implement the CSA Registration Reform Project.

While the best practices set out in this Guidance Note are intended to present acceptable methods that can be used to comply with the aforementioned IIROC requirements, they are not the only acceptable methods. Dealer Members may use alternative methods, provided that those methods demonstrably achieve the overall objective of the Rules. In any event, Dealer Members are encouraged to adopt a risk based approach when setting internal compliance procedures.

The Guidance Note also discusses ~~these requirements in relation to the proposed~~certain of the Client Relationship Model ~~and the recent Amendments to implement the CSA Registration Reform Project.~~proposals that will, when implemented, introduce additional suitability obligations.

OVERVIEW OF THE REQUIREMENTS

Dealer Members and Registered Representatives are reminded that compliance with the suitability requirements is fundamental to compliance with general business conduct standards and is essential to good business practice. The suitability requirement is also complementary to the fundamental obligation under securities legislation for all ~~dealers~~Dealer Members and their representatives to deal fairly, honestly and in good faith with clients. The fundamental obligation includes a duty to disclose known or discoverable risks to the investor before entering into any transaction for a particular security.

~~The first step towards satisfying the suitability requirements is to satisfy the new account application and know your client requirements.~~

Most of the issues discussed in this Guidance Note apply to retail clients in an advisory relationship; however, some of the principles discussed may also be applicable when dealing with other types of clients or relationships. As previously noted, the Guidance Note does not purport to amend statutory requirements or applicable IIROC Dealer Member Rules relating to the "know your client" and suitability obligations. Accordingly, if a Rule does not apply to a particular type of client then any discussion or guidance provided with respect to that Rule will also not apply. For example, the obligation to deal fairly, honestly and in good faith with clients applies to all types of clients and relationships. The requirement to update the client's information at the time of material change applies to all clients. On the other hand, the requirement to determine a client's investment objectives and risk tolerance does not apply to institutional clients, as they are subject to a different suitability standard, or to clients who trade through order execution-only accounts.

COMPLIANCE WITH KNOW YOUR CLIENT REQUIREMENTS

The first step in satisfying IIROC's suitability requirements is to satisfy the new account application and "know your client" requirements.

Collection of "know your client" information - New account application requirements

Pursuant to current IIROC Dealer Member Rules, a new account application is required for each customer[1]. IIROC Dealer Member Rule 1300.2 requires that each account be opened pursuant to a new account form which includes, at a minimum, the applicable information required by Form 2, also referred to as the New Account Application Form. The information set out in Form 2 includes, among other things, the client's personal information, financial information, risk tolerance, investment objectives, and disclosure of whether the client is an insider of a public corporation.

Dealer Members should note that the recent amendments to IIROC Rules to implement the Registration Reform project eliminated the use of the word "form" from the term "new account application form" to recognize that the completion of account applications~~,~~ and the collection of ~~*KYC*~~"know your client" information~~,~~ is frequently completed/done electronically.

[1] IIROC Dealer Member Rule ~~2500~~2500, Part II – Opening New Accounts, Introduction

Conditions under which one account application may be used for more than one account:

~~As per the~~In accordance with recent Rule amendments which were necessary to implement the CSA Registration Reform Project, Dealer Member Rule 2500 has been amended to allow a Dealer Member to obtain one account application ~~to be obtained for each customer[2]. IIROC takes the position that a single account application may be used for a client or for multiple accounts held by~~for multiple accounts (e.g. a client's cash, margin and certain registered accounts) of the same client[2] provided that:

- in the case of individuals, the account beneficial owner is the identical individual for all of the accounts;
- in the case of non-individuals, the account beneficial owner is the identical legal entity for all of the accounts;
- ~~The~~the client's investment objectives and risk tolerance are identical for all of the accounts ~~covered by the application; ~~;
- ~~In the case of individuals, the beneficial owner is identical for all of the accounts or in the case of non-individual accounts, the entity is identical for all of the accounts;~~
- the Dealer Member has the ability to supervise each of the accounts, including the review of "know your client" information updates and orders for suitability purposes, on a multiple-account basis; and
- ~~The client understands that the accounts on the same account application will be assessed for suitability on a multiple account or portfolio~~the client understands and acknowledges that the information collected in the one application will be used to assess suitability on a multiple-account basis~~; and~~ .
- ~~The Dealer Member has the ability to conduct supervision, including reviewing orders for suitability and updating KYC information, on a multiple account or client basis.~~

~~Accordingly, subject to the above noted considerations, the same account application may be used for multiple accounts of the same client such as a client's cash, margin and certain registered accounts on the basis that the beneficial owner is identical for all of these accounts. IIROC staff are considering proposing the above noted conditions as rule amendments.~~

Given these conditions, not all accounts of the same client can necessarily be opened using a single account application.

Examples of accounts where a separate account application would be required:

~~Based on the above noted conditions~~As explained above, in order to be able to rely on a single account application for multiple accounts of the same client, the beneficial owner of each account must be identical. Accordingly, a separate account application would be required ~~for a~~if that same client's held a beneficial interest in a joint ~~account~~, corporate ~~account and~~or trust account.

Joint account - The beneficial owners of a joint account are not identical to the beneficial owner of an individual account.

Corporate account - Although the ultimate beneficial owner of a personal corporation may be the same individual as the client who has a cash or margin account, the same account application can not be used ~~on the basis~~to open a corporate account, given that the account holder ~~recorded is the Corporation, rather than the~~is the corporation and not the corporation's beneficial owner / shareholder. The information ~~recorded on~~required to complete the account application is therefore, the ~~Corporation~~corporation's information. Furthermore, the shareholders (beneficial owners) of a corporation are separate and distinct from the corporate legal entity. The contractual relationship arising out of the creation of the account is between the Dealer Member and the ~~Corporation~~corporation.

Trust accounts - "In Trust For" accounts also require a separate account application as they have ~~different interests and objectives. There~~unique investment objectives that are determined by the Trustee, in accordance with the terms of the trust. Furthermore, there is no contractual relationship between the Dealer Member and the beneficial owner(s) of the trust. ~~The "In Trust For" account is directed and controlled by the trustee, and subject to~~ Rather, the contractual relationship is between the Dealer Member and the trustee, who is required to operate the account in accordance with the terms of the trust.

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[2] ~~Recent amendments to implement the CSA Registration Reform Project approved by the IIROC Board of Directors on June 25, 2009 were implemented on September 28, 2009.~~

[2] Recent amendments to implement the CSA Registration Reform Project approved by the IIROC Board of Directors on June 25, 2009 were implemented on September 28, 2009.

Know your client information items to be collected and assessed

Under the current rules, there are several questions that Registered Representatives must ask their clients in order to satisfy their "know your client" obligation and equip themselves to conduct a proper suitability assessment. Some of the information collected, such a client's net worth, age and investment experience, can be answered by the client. Other factors, such a client's risk tolerance and investment objectives may, however require further discussion and assessment. Registered Representatives are reminded that the client's investment objectives, and risk tolerance must be assessed based on the client's financial and personal circumstances. The stated investment objectives and risk tolerance and must be reasonable in light of those circumstances. The reasonableness of such information should be reviewed by the Registered Representative and the Dealer Member during the account opening and account approval process. For example, designating an 80% high risk tolerance for an elderly client may be unreasonable if the client has a modest net worth and has opened the account to invest a substantial portion of her net worth. On the other hand, the 80% high risk tolerance may not be unreasonable if the elderly client has a substantial net worth and opens an account to invest a small fraction of her net worth.

Time horizon

As per Dealer Member Rule 1300, a client's investment objectives, risk tolerance, investment knowledge and financial situation must be considered when assessing the suitability of orders and recommendations. Furthermore, inDealer Members are reminded that the factors set out in Dealer Member Rules 1300.1(p) and (q) are not exhaustive. In order to meet the "know your client" requirements, Registered Representatives need to understand the client's personal circumstances which include understanding the client's time horizon. The client's age is one indication of the client's time horizon. Although time horizon is not a separate requirement, in order to properly assess and record a client's investment objectives and risk tolerance, Registered Representatives should consider the client's time horizon. Time horizon should be determined by considering when the client will need to access some or all of their money. Where a client identifies his / her time horizon, the Registered Representative has the responsibility to assess its feasibility and reasonableness in comparison to the client's age, risk tolerance, and other particular circumstances.

Periodic updates and review

The account application information must be updated any time there is a material change in a client's circumstances.[3] The following procedures are considered Best Practicesbest practices for satisfying this requirement:

- Registered Representatives periodically, or at a minimum annually, inquire with each client as to whether there are any material changes in the client's circumstances. It is also acceptable for a Registered Representative to make such inquiries when the Registered Representative meets a client to review his/her portfolio, orotherwise corresponds with the client to discuss other account related matters. or annually contacts the client to verify the accuracy of the account information.

- Registered Representatives conduct periodic suitability reviews, at a minimum annually, and use the review discussion as an opportunity to inquire with the client as to whether there are any material changes in the client's circumstances.

- The Dealer Member, as part ofin its account opening documentation, clearly informs clients of the client's obligation to notify their respective advisors any time there is a material change in their circumstances.

As noted above, the account application will need to be updated anytime there is a material change in a client's circumstances.

- Dealer Members andWhere Registered Representatives should note that under the proposed Client Relationship Model, in order to comply with the suitability requirements, the positions held in the client's account(s) would have to be reviewed any time the KYC information is updated as a result of aconduct periodic suitability reviews, use the review discussion as an opportunity to confirm with the client as to whether there are any material changechanges in the client's circumstances[4].

COMPLIANCE WITH THE SUITABILITY ASSESSMENT REQUIREMENTS

Pursuant to IIROC Dealer Member Rules, orders and recommendations need to be reviewed to ensure that they are suitable for the particular client[54]. Suitability needs to be considered in light of other investments within the client's account or portfolio,accounts and in relation to his / her financial condition, investment knowledge, investment objectives and risk tolerance.

[3] IIROC Dealer Member Rule 2500 and 2700
[4] IIROC Dealer Member Rule 1300 as per proposed Client Relationship Model
[5] IIROC Dealer Member Rule 1300
[4] IIROC Dealer Member Rule 1300

The issue of whether the requisite suitability analysis should consider other investments in a client's account or accounts is discussed later in this Guidance Note.

The regulatory obligation to ensure that orders and recommendations are suitable includes not only an obligation to ensure that the specific security is suitable for the client but also that the order type, along with the trading strategy recommended and/or adopted are also suitable for the client. As an example, the risk profile of a client who fully pays for a position in a specific security as a core long term holding is significantly different from the risk profile of a client buying the same security on margin, as part of a day trading strategy.

~~The~~Dealer Members are also reminded that the suitability analysis starts before the order is even received, recommended or executed. The Dealer Member and Registered Representatives, at the time of account opening, should ensure that the account type (margin, trust, option accounts, etc.) is ~~suitable~~appropriate for the client ~~in relation to his / her~~given the client's particular circumstances. ~~Secondly, the~~

Furthermore, Dealer Members and Registered Representatives need to understand the risks and other characteristics associated with ~~securities~~the investment products they approve or recommend for sale.
~~Furthermore, as per the proposed Client Relationship Model, IIROC Dealer Member Rules are proposed to be amended to require a suitability analysis whenever one or more of the following triggering events occur:~~

- ~~any time there is a material change in the customer's circumstances;~~
- ~~when there is a change in the registered representative, investment representative, or portfolio manager; or~~
- ~~when securities are received into the client's account by way of deposit or transfer. In the interim, Dealer Members and Registered Representatives are encouraged to adopt the practices outlined above to enhance compliance with the existing suitability requirements~~.

Product suitability

The suitability assessment obligations include a requirement to know and understand the characteristics and risks associated with any investment product approved or recommended to clients. Dealer Members have the responsibility to assess the risks associated with the products that Dealer Members approve for sale. Registered Representatives should understand, and be able to clearly explain to the client, the reasons that a specific security is appropriate and suitable for the client.

Please refer to the "Best Practices for product due diligence" Guidance Note 09-0087 published on March 25, 2009 which sets out IIROC's expectations regarding procedures and criteria that Dealer Members should consider when assessing and introducing products that they approve or recommend for sale. As explained in ~~the~~that Guidance Note, adequate procedures for reviewing products before they are offered to clients can greatly enhance the ability to detect unsuitable recommendations.

Account suitability vs. multiple account suitability

Consistent with the collection of "know your client" information for multiple accounts, IIROC Rules permit that a single set of "know your client" information may be used, for suitability assessment purposes, for multiple accounts held by the same client provided that:

- the beneficial owner is the identical individual or legal entity for all of the accounts;
- the client's investment objectives and risk tolerance are identical for all of the accounts;
- the Dealer Member has the ability to supervise accounts, including the review of "know your client" information updates and orders for suitability purposes, on a multiple-account basis; and
- the client understands and acknowledges that the information collected in this single set of "know your client" information will be used to assess suitability on a multiple-account basis.

To clarify, the question of whether suitability must be assessed on either a single account or multiple-account basis will depend on: i) whether the client has identical objectives and risk tolerance for all of those accounts; ii) the client's agreement or understanding with the Dealer Member in that regard; and iii) the Dealer Member's ability to supervise on a multiple-account basis. Once that has been decided, the basis upon which suitability will be assessed should be evidenced on the client's account application and applied consistently throughout the relationship. This would also mean that once a Dealer Member sets up the account on a certain basis (for example that suitability of orders and recommendations will be assessed on a multiple-account basis) the Dealer Member and Registered Representative cannot assess suitability on a different basis from time to time (for example on a single account basis).

Unsuitable investments

An unsuitable investment and/or recommendation is one that is inconsistent with the client's personal circumstances including financial situation, investment knowledge, investment objectives, risk tolerance as current composition, duration and risk level of the other investments within the client's account or accounts at the time of the investment and/or recommendation.

Dealer Members and Registered Representatives have a general suitability requirement with respect to orders they accept or trades they recommend[6]. As previously stated, once the Client Relationship Model proposal is in effect, the suitability assessment requirements will continue after the order is executed, upon the occurrence of various triggering events[7]. As part of the general suitability requirements.[5] Dealer Members and Registered Representatives also have a statutory obligation to deal with clients fairly, honestly and in good faith. As a result, whenever an unsuitable investment is identified within an account, there is a responsibilityeither at the time of the investment is recommended or the investment order is accepted or subsequent to that time, there is an obligation to take appropriate action. An unsuitable investment may be identified by the Registered Representative at the time of updating the client's account information, to reflect a material change in the client's circumstances as required by IIROC Dealer Member Rule 2500, or when conducting a periodicalperiodic suitability review as discussed on page 4 of this Guidance Note. The Dealer Member may identify an unsuitable investment within an account when conducting supervisory activities, including account activity reviews as required by Dealer Member Rule 2500. The responsibilityobligation to take appropriate action when an unsuitable investment is identified within an account is consistent with Dealer Member Rule 25002500, which explains that the meaning of the term "review" includes a preliminary screening to detect items for further investigation.

An account may include an unsuitable investment for a variety of reasons including, for instance there may have been a previously executed unsolicited order, or an unsuitable recommendation by a former Registered Representative. Furthermore, a sector related change or material change in an issuer's circumstances may cause a shift in the risk associated with a particular security. Where an unsuitable investment is identified within an account, the Registered Representative should take appropriate measures to ensure the client receives advice considering the client's objectives, risk tolerance, and other particular circumstances. An appropriate measure or course of action may include contacting the client in a timely manner to recommend changes. Where a client does not want to dispose of the unsuitable investment, it may be appropriate to recommend changes to other investments within the account in order to ensure the suitability of the overall portfolio. In any event, Registered Representatives are encouraged to contact the client in order to discuss their concerns and to document any actions that they take in response to the issue. Registered Representatives should consult their Supervisor or Compliance Department personnel regarding the Dealer Members'Member's internal policies in handling unsuitable investments.

Unsolicited unsuitable orders

Where a Registered Representative receives an unsolicited order that is unsuitable in relation to the client's objectives, risk tolerance and other particular circumstances, it is not sufficient to merely mark the order as unsolicited. The Registered Representative needs to take appropriate measures to deal with the unsuitable order. The extent of the Registered Representative's obligation partially depends on his/her relationship with the client. Appropriate measures may include providing clients with cautionary advice and documenting the details of the cautionary advice, or recommending changes to other investments within the account. In any event, Registered Representatives are encouraged to document any actions that they have taken. If the Registered Representative is unsure of how to deal effectively with an unsuitable order, they should consult their Supervisor or Compliance Department regardingpersonnel in order to understand the Dealer Member's internal procedures infor dealing with the above noted circumstances, including whether it is appropriate to refuse the order.this issue.

Inappropriate updates

When anа potentially unsuitable investment is identified within a client's account or anа potentially unsuitable order is received from the client, the Registered Representative should discuss with the client whether there have been any changes to the client's circumstances that would warrant amendments to the KYC"know your client" information.

Registered Representatives should note that it is inappropriate to update or alter the client's KYC"know your client" information in an effort to justify the suitability of an investment, order or recommendation that is otherwise unsuitable for the client.

Best practices for maintaining a suitable client portfolio

The following are recommended Best Practices that will contribute to maintenance of a suitable client portfolio:

6 Dealer Member Rules 1300 and 2500
7 Proposed Client Relationship Model
5 Dealer Member Rules 1300

- ~~Considering whether a suitability review should be conducted when there are significant market changes and conducting such review where appropriate;~~

- ~~Conducting a suitability review where there is a material change of risk associated with an issuer, whose securities are held by specific customers; and~~

- ~~Written policies and procedures regarding the need to conduct a suitability review at the time of transfer to a new advisor, transfer to a new Dealer Member, or where there is a material change in a customer's circumstances. As noted above, these events would trigger a suitability review under the proposed Client Relationship Model.~~

To clarify, the Registered Representative should remind the client of the "know your client" information previously collected and update that information only if there is a material change in the client's circumstances. The Registered Representative should not be soliciting the client's consent to change their "know your client" information if the purpose of the change is solely to create the appearance of a suitable order.

Pending proposals

As per the proposed Client Relationship Model, IIROC is proposing to amend its Dealer Member Rules to require that a suitability analysis also be performed whenever one or more of the following triggering events occur:

- any time there is a material change in the customer's circumstances;

- when there is a change in the registered representative, investment representative or portfolio manager assigned to the account; or

- when securities are received into the client's account by way of deposit or transfer.

The current suitability assessment requirements, set out in IIROC Dealer Member Rule ~~1300 are triggered at the time of acceptance of an order or making a recommendation. As discussed above, the Proposed Client Relationship Model amendments will also introduce the obligation to conduct suitability reviews when certain triggering events occur in order to ensure that the client's portfolio remains appropriate for him/her.~~ 1300, are triggered when either an order is accepted from a client or a trade is recommended to a client.

Best practices for maintaining a suitable client account

It is advantageous to clients, ~~firms~~Dealer Members and the industry ~~overall, and~~as a whole, as well as consistent with good business practices, that Registered Representatives and Dealer Members conduct ~~suitability reviews using a~~ more holistic ~~approach as suggested above~~suitability reviews.

In other words, Dealer Members are encouraged to adopt best practices which would not only allow them to comply with the current order / recommendation-triggered suitability assessment requirements set out in IIROC Dealer Member Rule 1300.1, but also assist in the ongoing maintenance of a suitable client portfolio. The best practices would include:

- Adopting policies and procedures requiring, when appropriate, periodic suitability reviews of client accounts:

- Conducting suitability reviews of accounts that may be affected by significant market events;

- Conducting suitability reviews of accounts holding securities of an issuer that has undergone a material change in its risk profile; and

- Adopting written policies and procedures that require a suitability review of an account at the time of the account is transferred to a new advisor or a new Dealer Member, or where there is a material change in a customer's circumstances.

~~Comments on the draft Suitability Guidelines may be delivered in writing or by fax or e-mail within 75 days of the date of this notice to:~~

~~Sherry Tabesh-Ndreka, Policy Counsel~~
~~Investment Industry Regulatory Organization of Canada~~
~~121 King Street West, Suite 1600~~
~~Toronto, Ontario~~
~~Canada M5H 3T9~~
~~Fax: (416) 943-6760~~
~~Email: stabesh@iiroc.ca~~

General comments:

We received the following general comments:

- Concerns about the application of the Guidance Note to clients of suitability-exempt Dealer Members and institutional clients. Comments that the Guidance Note should be labeled as applying to retail clients only.

IIROC's staff response: As noted at the beginning of the Guidance Note, this Guidance Note does not purport to amend any existing requirements.

Pursuant to Dealer Member Rule 1300.1(r), a Dealer Member is not subject to the suitability requirements if it has satisfied the Corporation that it meets the requirements set out in Dealer Member Rule 3200 and has received the requisite approval. It is our position that the Guidance Note does not need to repeat every rule and exemption within the IIROC Dealer Member Rules. If a Dealer Member is not subject to the suitability requirements set out in the rules, then it is not subject to any guidance provided with respect to the suitability requirements.

Similarly, if a particular type of suitability assessment does not apply to institutional clients, then any discussion of it in the guidance note also does not apply to institutional clients. For example, we recognize that the suitability assessment requirements set out in Rule 2700, do not require an assessment of investment objectives and risk tolerance. Therefore any discussion in the Guidance Note with respect to investment objectives and risk tolerance would not apply to institutional clients. However, we do not believe that the Guidance Note should be labeled as "retail only" on the basis that some of the discussions are relevant to institutional clients. For example the discussion of the obligation to deal fairly, honestly and good faith with clients is not limited to retail clients; it is equally applicable to institutional clients and retail clients subject to suitability exemption. Furthermore, any discussion of material change and reasonableness of know your client (KYC) information (i.e. investment knowledge) is relevant to institutional clients. We have clarified this in the Guidance Note.

- Concerns that the Guidance Note is creating new obligations without going through the rule making process and question the order of issuing a Guidance Note prior to the rule changes.

IIROC's staff response: The intent of the Guidance Note was not to create new requirements or to amend the current requirements. The intent of the Guidance Note is to provide Dealer Members with guidance and best practices on how to comply with the current requirements. We have clarified this in the Guidance Note.

- Concerns that the Guidance Note refers to the Client Relationship Model (CRM) extensively and that CRM has not yet been approved.

IIROC's staff response: While we recognize that the CRM proposals have not yet been approved, we support the principles that have been proposed and to the extent relevant, we have suggested that Dealer Members consider adopting these principles. However, we have clarified the distinction between the proposed requirements (i.e., the CRM proposals) and those practices that relate to the existing requirements.

- Concerns about the triggering events introduced through CRM.

IIROC's staff response: Any substantive comments received with regards to the rule amendments under the CRM proposals have been addressed, as appropriate, under the CRM proposals.

- Comments that IIROC needs to develop more comprehensive guidelines for Dealer Members on the application, implementation and administration of KYC and suitability rules. A set of guidelines should also be provided for the investors that would address, among other things, limitations of KYC and suitability.

IIROC's staff response: We will consider this suggestion for future initiatives.

- One comment requests that we define unsuitable recommendation in such a manner that even an otherwise suitable security subject to unsuitable trading practices be considered unsuitable.

IIROC's staff response: We agree and have clarified this in the Guidance Note.

- Two commentators requested additional criteria to be included as part of the KYC and suitability process including: loss tolerance, education, health, tax bracket, liquidity, fees associated with products.

- One commentator requested that environmental, social and governance (ESG) issues should be considered as part of the suitability assessment. The commentator suggested that IIROC should mandate that inquiries be made with regards to ESG factors, rather than a check box approach.

IIROC's staff response: The considerations set out in current 1300.1(p) and (q) are not exhaustive. Other considerations that are important to a particular client should also be assessed as part of any suitability review. Specific to the suggested additional considerations:

- Loss tolerance is an approach to assessing risk tolerance, an existing required consideration in the rules;
- Education is a factor in assessing investment knowledge, an existing required consideration in the rules;
- Health is a factor in determining investment objectives, an existing required consideration in the rules;
- Tax bracket is only relevant if the client is relying on (and paying) the Dealer Member for tax advice. The Dealer Member has a responsibility to know the tax considerations associated with potential trade recommendations but generally does not have the responsibility to know the client's individual tax situation;
- Investment liquidity and fees are important factors in determining whether a particular investment is suitable for a client but they are not KYC related considerations, which is the focus of the considerations set out in current 1300.1(p) and (q); and
- Environmental, social and governance (ESG) issues are considerations in determining investment objectives, an existing required consideration in the rules.

In summary, the existing list of factors was never intended to be exhaustive – the intention was to delineate the material KYC considerations in determining the suitability of a trade/order. We have however added "time horizon" and the "account's current investment portfolio composition, duration and risk level", as part of the CRM proposals, as new factors to be considered as part of the suitability assessment. We believe with these revisions the material considerations are adequately detailed in subsections 1300.1(p) and (q) and proposed new subsection 1300.1(r).

- One commentator requested that IIROC introduce a new requirement that KYC information be signed.

IIROC's staff response: We agree in principle with this comment and have included proposed requirements in the latest CRM proposals for the client to be provided with a copy of their KYC information and for the client to acknowledge receipt of this information.

- One commentator suggested that categories of low, medium or high are not meaningful without definitions.

IIROC's staff response: These risk definitions are currently under review and will be addressed as part of a separate project.

- One commentator suggested that if the client is not proficient in English or French, then the KYC has to be translated and the translator must sign the KYC.

IIROC's staff response: Canadians speak over 200 languages. The individuals whose first language is not English or French represent approximately 20% of Canada's population. Although we agree with the principle of the comment, this type of requirement would be unreasonably onerous.

- One commentator suggests allowing the use of risk based approach.

IIROC's staff response: We encourage Dealer Members to use a risk based approach in determining which best practices set out in the Guidance Note should be incorporated into their KYC policies and procedures. We have clarified this in the Guidance Note.

- One commentator suggested that although suggestions relating to continuing review of suitability can be beneficial, the regime is one that imposes a high fiduciary obligation upon the advisors.

IIROC's staff response: The Guidance Note does not create or impose a fiduciary obligation on advisors. Rather, the Guidance Note provides guidelines on how to best comply with the suitability requirements and to ensure that all trades and recommendations remain suitable for the client. The Guidance Note does not mandate continuing suitability but instead offers suggestions and best practices to help ensure that the clients interests are protected under a suitability standard.

- One commentator suggested Registered Representatives that have a direct relationship with clients are compensated on the basis of commissions and therefore, the relationship has grown more towards an order taker. The commentator suggests proceeding with caution so that the regulatory structure doesn't change the relationship from a co-operative one to one where the client's obligations are being reduced.

IIROC's staff response: There are currently three types of relationships: order execution only, advisory and managed accounts. The guidelines set out in this Guidance Note are in reference to an advisory relationship only. The intent is not to reduce a client's obligations but rather to remind advisors that the nature of the advisory relationship carries certain obligations that go beyond order taking. IIROC Dealer Member Rule 3200 was introduced to recognize that different standards apply to an order execution only relationship.

- Suggestion to harmonize the draft Guidance Note with the MFDA guidelines

IIROC's staff response: We had considered the issues discussed in the MFDA guidelines and incorporated them to the extent appropriate.

- Two of the comment letters also included comments about issues that are outside of this project such as the CSA mutual fund disclosure, performance reporting, CRM relationship disclosure, personalized rates of return, inconsistencies that exist in an advisory relationship, as well as change to CSA's registration reform KYC related amendments.

IIROC's staff response: We will not be specifically responding to these comments as they are not related to this Guidance Note.

COMMENT RELATING TO SPECIFIC PROVISIONS:

We received the following comments with regards to ***Conditions under which one account application may be used for more than one account:***

- Supportive of the ability to apply one set of investment objectives and risk tolerance to multiple accounts held by the same client and supportive of the restrictions used in this process

IIROC'S staff response: No comments.

- A single account application should be able to encompass multiple accounts with differing objectives and risk tolerance, provided that it is made clear to clients.

IIROC'S staff response: We disagree. It is important that the KYC information collected in the account application be the same for all accounts covered by the application. Specifically, a comingling of different account investment objectives and risk tolerances would lead to an "averaging" of objectives and risk tolerances, and in turn, result in the use of an "averaging" approach to determining suitable trades within each account. Use of this approach would significantly increase the risk of unsuitable investments occurring within individual accounts.

- The section should be redrafted for greater clarity to specifically identify which types of registered accounts can or can not be aggregated

- Identify the types of registered accounts that can or cannot be aggregated

- Long term plans such as RRSPs have a uniquely identifiable KYC

IIROC's staff response: As noted in the Guidance Note, if the investment objectives and risk tolerance are identical to the client's other accounts, and provided the other conditions set out are satisfied, then those accounts can be aggregated. There is no standard prescriptive list that can be provided to address each unique client situation that may arise.

- Requiring separate account applications based on different objectives and risk tolerance is an artificial construct and lacks flexibility.

- If one form is required for each account, operational difficulties would arise from updating all forms every time there is a material change in the client's circumstances.

- Application cannot be used if the client's objectives and risk tolerance are not identical.

IIROC's staff response: The reference to application is not about the application *forms* but rather the use of one set of information for the purpose of assessing suitability. We are not prescribing separate forms. We have updated the Guidance Note to clarify our intention.

- Clients should be asked how they would like their suitability assessed. Also, suggest making the language between bullets 3 and 4 consistent.

IIROC's staff response: We agree. This is precisely the message that we are attempting to convey through condition 3 of this section. We have updated the Guidance Note to clarify the proper intent.

- One commentator has concerns over confusion that may arise if the account can be viewed in the context of a single account or multiple accounts and may have a negative impact on the client's compliant.

IIROC's staff response: The intention of this requirement is that when one application is used and one set of know your client information is collected for multiple accounts, the client must be informed that suitability assessments will be performed by considering the combined positions held in these multiple accounts. Assessing suitability on an account by account basis when one set of know your client information has been collected for multiple accounts (and vice versa) would not be acceptable.

- Only if a client has an integrated financial plan, should a multi-account application be considered

IIROC's staff response: The existence of an integrated financial plan should not on its own be used to determine whether multiple account suitability assessment can be used.

We received the following comments on the **Know Your Client Information** section of the draft Guidance Note:

- Questions about focus on investment objectives and risk tolerance and not other factors such as investment experience

IIROC's staff response: Factors such as a client's net worth, age and investment experience are generally easier to verify / assess as being reasonable than investment objectives and risk tolerance. The Guidance Note therefore focuses in assessing the reasonableness of investment objectives and risk tolerance in relation to the client's personal and financial circumstances. We have clarified this in the Guidance Note.

- Comment that use of reasonableness of data is subjective and it is hard to supervise.

- Comment that approval of new accounts and KYC updates should include objective review of the KYC information submitted

IIROC's staff response: We agree that reasonableness of some of the factors such as investment objectives and risk tolerance may be subjective. However, the supervisory obligations should be performed to a reasonable standard.

- Suggestion that many firms do not establish a risk tolerance for clients as a separate stand alone factor given the difficulty defining risk

IIROC's staff response: We would like to remind all firms that in order to satisfy the requirements set out in Dealer Member Rule 1300.1(p) and (q), they must establish a client's risk tolerance level.

- Suggestion that can not force a client to change objectives even if some one thinks that it is unreasonable

IIROC's staff response: The Guidance Note is not suggesting that clients be forced into setting specific objectives that may not be acceptable to them. The Guidance Note suggests that Registered Representatives and Dealer Members assess the reasonableness of those objectives. This may mean that if an objective or stated risk tolerance is unreasonable, then it should at the very least be discussed with the client.

- Supportive of the concept of reasonableness but suggestion to use example

IIROC's staff response: The Guidance Note has been updated accordingly.

- Suggestion that loss capacity and income tax should be added as new factors

- Suggestion that Guidelines require that NAAF be signed, and that the Dealer Members advise clients of the importance of the NAAF and that clients may use it in dispute resolution and that it contains an obligation to keep relevant information up-to-date

IIROC's staff response: The IIROC requirements are not intended to list every factor that may be relevant in a specific client account situation; rather the key factors are listed. Asking a client about their loss capacity is an approach to assessing their risk tolerance, an existing factor. Asking a client about their income tax situation would infer that the Dealer Member and the advisor are responsible for meeting the client's overall tax planning needs. While knowing the tax advantages of one potential investment recommendation versus another is an important factor in deciding on what recommendation to make, providing overall tax planning advice to a client is not an existing advisory account obligation unless the client separately contracts for these services.

The guidelines do not require that the new account application form, the form used to collect "know your client" information, be signed because this is not a current IIROC rule requirement. We agree with the comment in principle, however, and have included proposed requirements for the client to be provided with a copy of their "know your client" information and for the client to acknowledge receipt of this information in the latest CRM proposals.

We received the following comments with regards to the **Time Horizon** section of the draft Guidance Note:

- Questions why time horizon is highlighted more than other factors and that focusing on it gives the impression that it is an item that needs to be documented in the current application

- Agrees that time horizon is an important factor but it is an extension of the client's investment objectives and risk tolerance. How would the question be framed in an automated type of suitability review when combined with investment objectives and risk tolerance.

- Determining a single time horizon is a flawed exercise, as everyone has multiple liability spread across multiple time horizons

- Suggestion that time horizon should be introduced as a new factor within the Rules

- One commentator does not agree that "Time horizon is not a separate requirement" and that it should always be considered

IIROC's staff response: Currently, Dealer Member Rules 1300.1(p) and (q) require that suitability for an order or recommendation be assessed based on factors *including* client's financial situation, investment knowledge, investment objectives and risk tolerance. The factors set out in 1300.1(p) and (q) are not exhaustive. Although, time horizon is not currently specifically set out as a separate requirement to be considered under the IIROC Dealer Member Rules 1300.1(p) or (q), it is an important factor to consider. The importance of time horizon is currently set out in the Conduct and Practices Handbook (CPH). Similarly, we have discussed time horizon in the Guidance Note as we agree that it is an important factor that needs to be assessed based on the client's investment objectives and risk tolerance. We will also consider whether time horizon should be included as a specific requirement as part of future Rule amendments.

Dealer Members should also note that we are not suggesting that a single time horizon is appropriate in all cases. In some cases allocating multiple time horizons for different portions of the account may be more appropriate.

We received the following comments with regards to the **Periodic updates and review** section of the draft Guidance Note:

- Suggestion that IIROC should mandate a minimum annual suitability review

- Suggestion that mandatory annual review unnecessary

- Suggestion that the "minimum annual review" is imposing a new requirement through the Guidance Note, rather than a best practice

- Rather than an annual inquiry, the Guidance Note should simply discuss the obligation of RRs to be aware of material change as communicated by the client and it should emphasize that clients also have an obligation to notify their advisors with respect to material changes

- Suggestion that recommending an annual suitability review is inconsistent with current IIROC Dealer Member Rules and proposed CRM as CRM included an optional suitability review

IIROC's staff response: We agree that the current requirement to identify material changes should be separately discussed from the best practice approaches to identifying material changes. The language in the Guidance Note has been revised to provide this distinction.

We are unsure as to how this suggested best practice is inconsistent with CRM. The CRM proposal suggests that if the Dealer Member conducts suitability reviews upon other triggering events, in addition to those mandated by CRM, then it should be disclosed to the client. In this Guidance Note we suggest that periodic suitability reviews could contribute to maintenance of a suitable client portfolio. Such practice is not mandated. We have clarified this in the Guidance Note.

- Language should be revised to allow for client information to be updated any time there is a material change in the client's circumstances rather than having to update the actual account application
- Suggestion to revise wording to clarify that it is not the actual account application that needs to be updated but rather the information contained within it
- Suggestion to clarify what is a material change
- Question as to whether putting client's information on the statements would suffice
- Suggestion that each year the KYC must be updated after consultation with the client and the update must be signed by the client and a copy provided to the client

IIROC's staff response: We agree that it is the client information and not the account application that needs to be updated.

Currently, IIROC Dealer Member Rules require client information to be updated any time there is a material change in the client's circumstances. The advisor must update the client information as soon as they become aware of a material change in the client's information. The suggested annual follow-up is to ensure that clients have not inadvertently failed to inform their advisor of the change in the material circumstances.

The question of whether a change is material depends on the facts. For example, a $10,000 increase in annual income may be significant for one client but not for another client.

The current IIROC Dealer Member Rules do not require the original application or any update to the client's information to be signed by the client. We have included proposed requirements for the client to be provided with a copy of their "know your client" information and for the client to acknowledge receipt of this information in the latest CRM proposals.

We received the following comments with regards to the **Compliance with Suitability Assessment Requirements** section of the draft Guidance Note:

- Agreement that account type must be suitable
- Statement that account type suitability is beyond present suitability requirements and proposed CRM suitability triggering events. It is unclear how an account type suitability review would occur.

IIROC's staff response: The discussion of the importance of the appropriateness of account type is consistent with the guidance currently set out in the CPH. It would appear that some Dealer Members do not consider the appropriateness of the type of account that they open for a client. Dealer Members are reminded that the current IIROC Dealer Member Rules require a Designated Supervisor to approve all new accounts.

- Some firms open margin accounts for all clients but only if the margin facility is used, then suitability is an issue to be considered

IIROC's staff response: For firms that open only margin accounts, we agree that the appropriateness can be determined before making the margin lending feature available to the client.

- Concerns about the impact that the Guidance Note could have on existing rule that Dealer Members must have procedures for recording that the new advisor has reviewed the information.

IIROC's staff response: We do not believe that the Guidance Note will have any adverse impact on the above noted requirement.

- Include additional guidance that Registered Representatives should record the measure that they have taken to deal with unsuitable investments within an account. Registered Representatives should document their conversation with clients.

IIROC's staff response: We agree that Registered Representatives should record the measures that they have taken to deal with unsuitable investments within an account and that they should document their conversation with clients. We have incorporated this into the Guidance Note.

We received the following comments with regards to the **Product Suitability** section of the draft Guidance Note:

- One commentator suggests that the product due diligence guidelines are clear and recommends removal of this section

IIROC's staff response: The benefit of removing this section is not clear. The section is intended as a reference to the Product Due Diligence Guidance Note and explains its relationship to this Guidance Note.

- Suggestion to distinguish between the Dealer Member's product due diligence obligation (make product available) and the advisor's obligation (determine if suitable)

IIROC's staff response: We believe that this distinction is adequately addressed in the first paragraph of the Product Due Diligence section of the Guidance Note.

- One suggestion that anyone having less than five years of experience should not be allowed to offer hedge products in a client's portfolio

IIROC's staff response: This proposal will be considered as part of future rule amendments.

We received the following comments with regards to the **Unsuitable Investments** section of the draft Guidance Note:

- Define what is an unsuitable investment

IIROC's staff response: An unsuitable investment and/or recommendation is one that is inconsistent with the client's personal circumstances including financial situation, investment knowledge, investment objectives and risk tolerance as well the other investments within the client's account or accounts at the time of the investment and/or recommendation. Although we believe this definition is consistent with the current industry understanding, we have updated the Guidance Note to reflect the definition.

- Clarify if a Registered Representative has any additional responsibility with regards to an investment that they have cautioned against. Suggestion to clarify that no further obligation.

IIROC's staff response: We generally agree that if the Registered Representative has cautioned the client against a particular investment, and has documented the discussion, then that may be sufficient in many cases. This is one type of issue that we encourage Dealer Members to address as part of their policies and procedures on how to deal with investments which the Dealer Member or Registered Representative has identified as unsuitable for the client.

- If the ultimate focus is the suitability of the overall portfolio and the other investments continue to remain suitable, what should be changed? Suggestion to remove this provision as nothing should be changed.

IIROC's staff response: We are unsure about the meaning of the comment. If all of the investments within the portfolio are suitable, then there is no need for change. The suitability determination relates to whether a particular security is suitable in relation to the client related factors and in relation to the others investments within the client's account or portfolio. The question of whether there should be a change or re-balancing only comes up when a particular security is not suitable for the client in relation to his/her particular circumstances and in comparison to other investments within the account or accounts. As previously mentioned the question of whether the comparison should be to an account or to a group of accounts depends on the conditions set out in the Guidance Note.

- Suggestion for IIROC to clarify what should be contained in a Dealer Member's policies and procedures

IIROC's staff response: It is our position that it is not useful for IIROC to mandate how Dealer Members should specifically handle each unsuitable investment.

- One commentator suggests that if an unsuitable investment is identified within an account, contact with the client should be mandatory

IIROC's staff response: We generally agree with the comment. We have amended the language in the Guidance Note to suggest contact with the client as a best practice. We will consider this proposal for future rule amendments.

- Suggestion that commercially available software should be used to identify unsuitable investments

IIROC's staff response: We do not disagree that commercially available software may be useful to assist in identifying unsuitable investments. Reliance upon commercially available software for this purpose does not relieve the Dealer Member or the Registered Representative of their responsibilities. Such software may be used to assist Registered Representatives with their suitability analysis or Supervisors with their supervision responsibilities. The ultimate responsibility lies with the Registered Representative and the Supervisor.

- Comment that Dealer Members and Registered Representatives have a duty to disclose known or discoverable risks to the investor before entering into any transaction for that security.

IIROC's staff response: We agree with the comment. Disclosure of such risks is part of the duty to act fairly, honestly and in good faith with clients.

We received the following comments with regards to the **Unsolicited Unsuitable Orders** section of the Guidance Note:

- Agrees that Registered Representative's obligation with respect to dealing with an unsolicited unsuitable order depends on his/her relationship with the client

- Suggestion for IIROC to clarify what should be contained in a Dealer Member's policies and procedures

- Request clarification on whether a Registered Representative has any further responsibility with respect to an investment that they have cautioned against

IIROC's staff response: We generally agree that if the Registered Representative has cautioned the client against an unsolicited unsuitable order and has documented the discussion, then it may be sufficient in many cases. This is one of the issues that we expect Dealer Members to include as part of their policies and procedures on how to deal with unsolicited unsuitable orders. Dealer Members may impose a higher expectation on their Registered Representatives. Some Dealer Members may choose to direct their Registered Representatives to refuse any unsolicited orders that are unsuitable. Others may be satisfied with caution and documentation, while some may wish to deal with each situation on a case-by-case basis. It is up to the Dealer Member to set their policies in this regards.

- Comment that the Guidance Note is silent on situations where a client contacts a sales associate to place potentially unsolicited unsuitable orders. Suggestion to include some recommended best practices

IIROC's staff response: When an Investment Representative receives an order from a client, in order to comply with current Dealer Member Rule 1300.1(p), the Investment Representative should refer the order to or discuss the order with the Registered Representative in order to ensure the suitability of the order. This is particularly the case when the order is unsolicited on the basis that the client and the Registered Representative have not previously discussed the order.

We received the following comments with regards to the **inappropriate updates section of the Guidance Note:**

- Agree that it is inappropriate to update KYC to simply justify suitability of an order

- One commentator cautions that if a client gives orders inconsistent with objectives and insists on it after receiving caution, then appropriate to change the KYC information.

IIROC's staff response: It is only appropriate to change the KYC information if there is a change in the client's circumstances. If the client's investment objectives have changed, then the KYC needs to be updated. If the client's information such as investment objectives has not changed, then it would be more appropriate to provide caution to the client and document the discussion, or refuse the order.

- One commentator states that updating KYC to justify suitability of an order is a "malicious act and should be categorized as fraudulent as it is unethical and unprofessional and illegal".

IIROC's staff response: This section has been updated to clarify that the KYC information can only be updated with the consent of the client and that the advisor should not revise the know your client information to justify the suitability of the order.

We received the following comments with regards to the **Best Practices for maintaining a suitable client portfolio** section of the draft Guidance Note:

- Concerns about difficulty of conducting a suitability review every time the market goes up or down

IIROC'S staff response: The Guidance Note does not mandate or suggest that a suitability review should be conducted each time that the market goes up or down. Rather, it suggests considering whether a suitability review should be conducted at the time of significant market changes, and conducting a review if determined to be appropriate, could contribute to the maintenance of a suitable client portfolio. We have updated the language in the Guidance Note to clarify this intent.

- Comment that significant market changes by themselves should have no immediate impact on account suitability when there is no change in the client's KYC or risk profile of investments as defined in a fund's prospectus. Suggestion that there should be no rule for market fluctuations as determinants for suitability reviews and these references should be removed from the guidelines.

IIROC's staff response: There are circumstances under which a market fluctuation may impact the risk profile of the product (fund or otherwise). The change in the risk profile of a client's account or portfolio, as a result of market fluctuations, should be considered when making recommendations or accepting orders.

The comment seems to suggest that for certain products, the suitability obligation is solely based on the risk tolerance set out in the prospectus. As with any product, complete reliance on the prospectus is not sufficient.

There is no requirement to do a periodic suitability review at the time of market fluctuations or otherwise. The Guidance Note suggests that considering whether a suitability review should be conducted at the time of significant market changes, and conducting a review if determined to be appropriate, could contribute to maintenance of a suitable client portfolio. We have updated the language in the Guidance Note to clarify this intent.

- Monitoring compliance with this section is extremely difficult and would take the advisor's focus away from managing client's investments. This review should instead be part of the next trade or other suitability review triggering events. Focus on market changes and issuer risk does not properly capture the relationship that advisors have with their clients and how they manage their clients' portfolios.

IIROC's staff response: We are not clear as to why the commentator believes that monitoring account positions in the event of a significant market change or change in the risk of a specific issuer takes the advisor's focus away from managing a client's investments. In fact, it is our position that it contributes to proper monitoring of the client's investments.

We received the following comments regarding the references to an **annual suitability review** proposed in the Guidance Note:

- Agree with principle surrounding this guideline however, concerned about mandatory reviews as: it will be difficult for firms to manage and supervise; depending on the relationship between the client and advisor, the client would let the advisor know upon occurrence of material change; some clients with mutual funds only have a longer term time horizon and annual review not necessary; a requirement for annual review does not factor in the requirement to keep informed of material changes

IIROC's staff response: The language in the Guidance Note has been updated to clarify that we are not mandating an annual suitability review. However, periodic suitability reviews are a best practice and the reference to the annual suitability review is for those circumstances where an advisor does engage in annual or periodic suitability reviews.

- Suggestion that current understanding of proper suitability assessment is to do an ongoing suitability review

IIROC's staff response: That is currently considered a best practice. Furthermore, it is mandated by some firms.

- If IIROC was to mandate an annual suitability review, how would that work with market changes and suggestion that suitability review should be done at that time.

IIROC's staff response: The suggestion that suitability review should be conducted annually is in reference to those circumstances where the advisor has not for other reasons reviewed the client's account or portfolio for suitability during the last 12 months.

- Clarify use of the term suitability reviews and IIROC's expectation of suitability reviews

IIROC's staff response: We have added clarifying remarks to the first three paragraphs within the suitability assessment section of the Guidance Note.

- Agreement with best practice of an annual suitability review to renew the relationship and opportunity to confirm overall financial status but does not agree that should be mandatory

IIROC's staff response: No comments.

- Comment that CRM allows Dealer Members to include a statement as to whether a suitability review will be done based on other triggering events. The draft Guidance Note is inconsistent by stating that you should use other triggering events.

IIROC's staff response: It is our position that the Guidance Note is not inconsistent with CRM. The CRM proposal suggests that if the Dealer Member conducts suitability reviews upon other triggering events, in addition to those mandated by CRM, then it should be disclosed to the client. In this Guidance Note we discuss those situations where advisors or Dealer Members conduct periodic or annual suitability reviews, in addition to the existing requirements and the CRM requirements, once implemented.