

# IIROC NOTICE

## Rules Notice

### Request for Comments - Republication

Dealer Member Rules

*Please distribute  
internally to:*

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*Contact:*

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**14-0214**  
**September 18, 2014**

## **Client Relationship Model – Phase 2**

### **Performance reporting and fee / charge disclosure amendments to Dealer Member Rule 200 and to Form 1 that are scheduled to become effective on either July 15, 2015 or July 15, 2016**

#### **BACKGROUND**

IIROC is republishing for further public comment revised proposed amendments to Dealer Member Rule 200 and Form 1 (collectively the “IIROC 2015 and 2016 CRM2 Amendments”) to address the following remaining regulatory objectives identified under the Client Relationship Model project:

- Enhanced trade confirmation<sup>1</sup> and account statement reporting;
- Quarterly reporting on certain off-book client holdings;
- Annual account performance reporting; and
- Annual account fee / charge reporting.

IIROC has already announced the implementation of rule amendments to address the following regulatory objectives under the Client Relationship Model project:

- Account relationship disclosure;
- Management and disclosure of conflicts of interest;

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<sup>1</sup> Proposed amendments to the trade confirmation requirements are included in the proposed IIROC 2015 and 2016 CRM2 Amendments. These amendments, which are scheduled to become effective on July 15, 2016, would require trade confirmation disclosure whenever a deferred sales charge has been incurred by the client.



- Account suitability;
- Pre-trade compensation disclosure; and
- Enhanced trade confirmation reporting<sup>2</sup>.

Implementation of these amendments was announced on:

- March 26, 2012<sup>3</sup>, in the case of the amendments collectively referred to as the “IIROC CRM1 Amendments”, with all requirements to be effective by March 26, 2014; and
- May 29, 2014<sup>4</sup>, in the case of the amendments collectively referred to as the “IIROC 2014 CRM2 Amendments”, with all requirements to be effective by July 15, 2014.

The IIROC 2015 and 2016 CRM2 Amendments are being republished at this time in order to receive public comment on a revision to the proposed IIROC rule requirements that we have been requested to make by CSA staff. See “CSA staff request for revision” section below for further discussion of the CSA staff request.

## **SUMMARY OF THE NATURE AND PURPOSE OF THE REVISED PROPOSED AMENDMENTS**

### **History of previously proposed IIROC 2015 and 2016 CRM2 Amendments**

On December 12, 2013, IIROC published for public comment proposed amendments to Dealer Member Rules 29, 200 and 3500 and to Form 1 (the “IIROC CRM2 Amendments”) with the objective of adopting IIROC rule requirements that are substantially the same as the CSA CRM2 Amendments. On May 26, 2014, IIROC received CSA approval of those elements of its proposed IIROC CRM2 Amendments that were scheduled to be implemented on or before July 15, 2014 (the “IIROC 2014 CRM2 Amendments”). On May 29, 2014, IIROC issued Rules Notice 14-0133 to implement the IIROC 2014 CRM2 requirements, with all requirements to be effective by July 15, 2014. IIROC has not yet received CSA approval of the remainder of its proposed IIROC CRM2 Amendments (the “IIROC 2015 and 2016 CRM2 Amendments”) which are scheduled to be implemented in two stages on July 15, 2015 and on July 15, 2016.

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<sup>2</sup> Amendments to the trade confirmation requirements for debt security trades were announced on May 29, 2014 through the issuance of IIROC Rules Notice 14-0133. These amendments became effective on July 15, 2014.

<sup>3</sup> IIROC Rules Notice 12-0107 was issued on March 26, 2012 and set out implementation dates for the IIROC CRM1 Amendments ranging from immediately to March 26, 2014.

<sup>4</sup> IIROC Rules Notice 14-0133 was issued on May 29, 2014 and set out implementation dates for the IIROC 2014 CRM2 Amendments ranging from immediately to July 15, 2014.



Below is a detailed description of the five components of the previously proposed IROC 2015 and 2016 CRM2 Amendments, which were included as part of the package of IROC CRM2 Amendments, published for public comment on December 12, 2013:

**1. Trade confirmation disclosure of deferred charges** [proposed amended and renumbered Dealer Member Rule subsection 200.2(l)]

Pursuant to proposed Dealer Member Rule subsection 200.2(l), trade confirmation disclosure will be required on trade confirmations issued to Retail Customers where deferred sales charges have been incurred. This proposed requirement is consistent with the equivalent requirement introduced in paragraph 14.12(1)(c) of the CSA CRM2 Amendments.

**2. Client account statements** [proposed new subsection 200.1(c) and proposed amended and renumbered Dealer Member Rule subsection 200.2(d)]

Two amendments were introduced to the existing client account statement requirements as follows:

- A revision to the approach used to determine the “market value” of account security positions by introducing a “market value” definition in Dealer Member Rule subsection 200.1(c); and
- The introduction of a new requirement to provide Retail Customers with cost information for each account security position pursuant to proposed Dealer Member Rule sub-clauses 200.2(d)(ii)(F) and 200.2(d)(ii)(H).

These proposed requirements are consistent with the equivalent requirements introduced in sections 1.1, 14.11.1, and 14.14 of the CSA CRM2 Amendments, with the exception that there are differences in how IROC has defined the terms “book cost”, “market value” and “original cost”.

**3. Report on client positions held outside of the Dealer Member** [proposed new Dealer Member Rule subsection 200.2(e)]

A new report requirement was introduced in proposed subsection 200.2(e) requiring separate reporting on Retail Customer security positions held outside of a Dealer Member client account on which the Dealer Member continues to receive compensation. The report will require the disclosure of the same information required to be disclosed for account positions in the account statement – specifically name and quantity of each security position, as well as market value and cost information for each security position and aggregate market value and cost information for all security positions. These proposed requirements are consistent with the equivalent requirements introduced in sections 1.1, 14.11.1, and 14.14.1 of the CSA CRM2 Amendments, with the following exceptions:



- the IIROC proposals exclude off-book security positions issued by a scholarship plan, mutual fund or labour-sponsored investment vehicle from inclusion in the off-book report provided the Dealer Member receives no form of ongoing compensation on these positions - the equivalent CSA requirements require inclusion of these positions in the off-book report whether or not the Dealer Member receives ongoing compensation on these positions<sup>5</sup>;
- there are differences in how IIROC has defined the terms “book cost”, “market value” and “original cost”; and
- the IIROC proposals do not contemplate reporting on cash balances held outside of the Dealer Member by the client.

**4. Performance report** *[proposed new Dealer Member Rule subsection 200.2(f)]*

A further new report requirement was introduced in proposed subsection 200.2(f) to require annual performance reporting to Retail Customers. The information to be included in the new report, for the periods from account inception to report date and for the last 12 months, is as follows:

- total combined market value of cash and securities at the beginning of the period;
- total combined market value of all deposits and transfers in of cash and security positions;
- total combined market value of all withdrawals and transfers out of cash and security positions;
- total combined market value of cash and securities at the end of the period; and
- total combined change in market value for the period of all cash and security positions.

In addition, percentage return information for the most recent 1, 3, 5 and 10 years periods and for the period from account inception will also have to be included in the performance report as the information becomes available (i.e. the percentage return information requirements will be implemented prospectively).

These proposed requirements are consistent with the equivalent requirements introduced in sections 1.1, 14.11.1, 14.18 and 14.19 of the CSA CRM2 Amendments, with the following exceptions:

- there are differences in how IIROC has defined the term “market value”; and
- the IIROC proposals require the preparation of a consolidated performance report that covers the same accounts as any consolidated fee / charge report that is prepared for the client.

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<sup>5</sup> See the “CSA staff request for revision of IIROC 2015 and 2016 CRM2 Amendments” section below for further discussion.



**5. Fee / charge report** [proposed new Dealer Member Rule subsection 200.2(g)]

Finally, there is a new report requirement being introduced in proposed subsection 200.2(g) that requires annual fee / charge reporting to Retail Customers. The information to be included for the 12 months covered by the report is as follows:

- a discussion of the operating charges which might be applicable to the client's account;
- total amount of each type of operating charge;
- aggregate total amount of all operating charges;
- aggregate total amount of all transaction charges;
- aggregate total amount of all operating and transaction charges; and
- specific disclosures relating to debt security trade compensation taken, trailing commissions earned and other third party compensation earned during the year.

These proposed requirements are consistent with the equivalent requirements introduced in sections 1.1 and 14.17 of the CSA CRM2 Amendments, with the following exceptions:

- the IIROC proposals do not require that an annual fee / charge report be sent to the client if no fees or charges were paid by the client, either directly or indirectly, during the year; and
- the IIROC proposals require the preparation of a consolidated performance report that covers the same accounts as any consolidated fee / charge report that is prepared for the client.

**CSA staff request for revision of IIROC 2015 and 2016 CRM2 Amendments**

On June 16, 2014, IIROC received a letter from CSA staff setting out their comments on the proposed IIROC 2015 and 2016 CRM2 Amendments. As part of that letter, IIROC was informed that it was CSA staff's view that the proposed IIROC 2015 and 2016 CRM2 Amendments were not materially harmonized with the equivalent CSA requirements because of a difference between the scope of the client positions that IIROC proposed be included in its "Report on client positions held outside of the Dealer Member" and the scope of the client positions that the CSA will require be included in its "Additional Statement". Specifically:

- Pursuant to proposed Dealer Member Rule clause 200.2(e)(i), IIROC proposed that all off-book client named positions on which the Dealer Member receives ongoing compensation be included in the quarterly "Report on client positions held outside of the Dealer Member" that would be provided to the client.
- Pursuant to paragraphs 14.14.1(b) and 14.14.1(c) of National Instrument 31-103, the CSA will require that:
  - all off-book client named positions in securities issued by "a scholarship plan, a mutual fund or an investment fund that is a labour-sponsored investment fund corporation, or labour-sponsored venture capital corporation..."; and



- all other off-book client named positions in securities on which the Dealer Member receives ongoing compensation
- be included in the quarterly “Additional Statement” that must be provided to the client.

The substance of the scope difference is therefore that under previously proposed Dealer Member Rule clause 200.2(e)(i), positions in securities issued by a scholarship plan, a mutual fund or an investment fund that is a labour-sponsored investment fund corporation, or labour-sponsored venture capital corporation would not have to be included in the quarterly “Report on client positions held outside of the Dealer Member” that would be provided to the client, if the Dealer Member received no ongoing compensation on those positions.

To address this scope difference, the letter included a CSA staff request to revise proposed Dealer Member Rule clause 200.2(e)(i) to conform to the equivalent CSA rule requirements.

### **Revisions that have been made to the proposed IIROC 2015 and 2016 CRM2 Amendments**

IIROC staff have considered the CSA staff request and while we believe that the scope difference between our respective rules is immaterial, have revised proposed Dealer Member Rule clause 200.2(e)(i)<sup>6</sup> to conform the scope of client positions to be included in IIROC’s proposed “Report on client positions held outside of the Dealer Member” to that set out in the equivalent CSA rule requirements.

In addition, to ensure that this revision does not result in Dealer Members having to build a new capability to report on off-book positions to an immaterial number of clients and/or to report on an immaterial dollar amount of off-book client positions, IIROC will consider exemption requests from Dealer Members who can demonstrate that the costs of building and administering this new client reporting capability significantly outweigh the benefits to the client of also receiving off-book position information from their “dealer of record”<sup>7</sup>. In considering each exemption request, IIROC staff will need to be satisfied that the Dealer Member:

- has made a good faith effort to convert off-book client name positions into on-book nominee name positions;
- does not maintain material number or amount of off-book client named positions;
- is not promoting, or otherwise actively making available, the option of holding client-named positions off-book<sup>8</sup>; and
- does not receive any ongoing compensation on the off-book client named positions<sup>7</sup>.

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<sup>6</sup> To address the CSA staff request, new Dealer Member Rule sub-clause 200.2(e)(i)(B) has been included in the revised proposed IIROC 2015 and 2016 CRM2 Amendments.

<sup>7</sup> In the case of off-book client named mutual fund positions, clients already receive annual position information from the investment fund manager for the mutual fund.

<sup>8</sup> Exceptions will be made for certain accounts such as Registered Education Savings Plans (RESPs) and Registered Disability Savings Plans (RDSPs) where some client positions may only be held in client name.



The revised proposed IIROC 2015 and 2016 CRM2 Amendments, reflecting the above CSA staff requested revision and other immaterial revisions made to address public and CSA staff comments received, were approved by the IIROC Board of Directors on September 10, 2014.

The text of the revised proposed IIROC 2015 and 2016 CRM2 Amendments is set out in Attachment A. A black-line version of the revised proposed amendments, comparing the amendments to the equivalent provisions published by IIROC for public comment on December 12, 2013, is set out in Attachment B. A table, setting out a summary comparison of the major elements of the IIROC 2015 and 2016 CRM2 Amendments to the major elements of the equivalent CSA requirement and detailing all of the revisions that IIROC has made to its previously published proposals is included as Attachment C. Finally, IIROC's response to public comments received on the previously published version of the IIROC 2015 and 2016 CRM2 Amendments is included as Attachment D.

### **ISSUES AND ALTERNATIVES CONSIDERED**

In considering whether or not to revise the proposed IIROC 2015 and 2016 CRM2 Amendments to comply with the CSA staff request, IIROC staff compared the likely outcomes under two alternatives: (1) revising the proposals to comply with the CSA staff request; and (2) not revising the proposals.

IIROC staff recognizes that this revision to its proposals will likely have a significant impact on the costs that must be borne by its Dealer Members, in that they will be required to either build and maintain this new reporting capability or expend resources to demonstrate to IIROC that they should be exempted from this revised requirement to report to clients on their off-book positions. We are also concerned that clients may ultimately end up paying for any additional costs incurred by IIROC Dealer Members to comply with or to be exempted from this revised requirement.

IIROC staff also continue to believe that the proposed IIROC requirement to report to clients on their off-book positions only when the Dealer Member receives ongoing compensation on these positions:

- would have provided Dealer Members with a simple choice between:
  - building the new reporting capability and continuing to receive ongoing compensation on the off-book positions; and
  - not building the new reporting capability and not receiving ongoing compensation on the off-book positions
- would have resulted in consistent reporting treatment for off-book positions, rather than, for example, a different reporting treatment of mutual funds versus other investment products





- would have given Dealer Members a less costly process in determining whether or not they wished to build this new reporting capability<sup>9</sup>

IIROC staff also recognize that not revising our proposals will almost certainly result in the CSA refusing to approve our proposals. If CSA approval of the IIROC 2015 and 2016 CRM2 Amendments is not received, IIROC Dealer Members would be subject to both the IIROC and CSA client reporting requirements, including the requirement we've been requested by CSA staff to incorporate into the IIROC client reporting requirements.

Given that, it is highly likely that in either case IIROC Dealer Members will be subject to the CSA staff requested requirement, IIROC staff decided to revise the proposed IIROC 2015 and 2016 CRM2 Amendments to comply with the CSA staff request to make the conforming changes.

### **COMPARISON WITH SIMILAR PROVISIONS**

As the primary objective of the proposed IIROC 2015 and 2016 CRM2 Amendments is to adopt IIROC rule requirements that are substantially the same as rule requirements recently adopted by the CSA with respect to account statement, off-book position, account performance and account fee / charge reporting, a comparison with similar provisions in other jurisdictions is unnecessary.

### **EFFECTS OF THE REVISED PROPOSED AMENDMENTS ON MARKET STRUCTURE, DEALER MEMBERS, NON-MEMBERS, COMPETITION AND COSTS OF COMPLIANCE**

As previously stated, the primary objective of the proposed IIROC 2015 and 2016 CRM2 Amendments is to adopt IIROC rule requirements that are substantially the same as rule requirements recently adopted by the CSA with respect to account statement, off-book position, account performance and account fee / charge reporting. As such, implementation of IIROC 2015 and 2016 CRM2 Amendments should result in no greater impacts on IIROC Dealer Members than if the CSA requirements alone were implemented. Further, because implementation of the IIROC 2015 and 2016 CRM2 Amendments will result in IIROC Dealer Members having to comply with one set of client reporting and disclosure requirements, it is hoped that the implementation of these amendments will result in some modest burden reduction due to IIROC Dealer Members not having to comply with two sets of requirements.

The effect of the proposed IIROC 2015 and 2016 CRM2 Amendments will be to improve the quality of information that clients are provided regarding the performance of their investments and the fees and charges they are paying.

It is expected that the systems and cost impacts will be significant due to the introduction of the following new reports as part of the IIROC 2015 and 2016 CRM2 Amendments:

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<sup>9</sup> Less costly as firms would not have to also undertake an expensive process to trying to further reduce the size and amount of their off-book client-named positions and would not have to expend resources to apply for and receive an exemption from IIROC - both requirements under the revised IIROC 2015 and 2016 CRM2 Amendments.





- the quarterly “Report on client positions held outside of the Dealer Member” [*new Dealer Member Rule section 200.2(e)*];
- the annual “Performance report” [*new Dealer Member Rule section 200.2(f)*]; and
- the annual “Fee / charge report” [*new Dealer Member Rule section 200.2(g)*].

The extent of the systems and cost impacts associated with the creation and administration of these new reports will be influenced by:

1. *Report data requirements* –
  - (a) *Data collection* - Dealer Members will be required to collect more data elements to produce more reports (i.e. off-book position information, account-level trailing commission information)
  - (b) *Data retention* - Dealer Members will be required to store greater volumes of historical data to produce the reports (i.e. multi-year data sets will need to be readily available to calculate annualized percentage return information)
2. *Report line-item categorization requirements* - Dealer Members will be required to categorize existing data to produce these new reports (i.e. categorization of operating charges and transaction charges by type)
3. *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 requirements. 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.

These costs are also expected to be higher under the revised proposed IROC 2015 and 2016 CRM2 Amendments (as compared to the costs associated with the originally proposed IROC CRM2 Amendments) as discussed in the “Issues and Alternatives Section” above.

As detailed below, appropriate implementation dates are being proposed to allow Dealer Members time to make necessary systems changes.

#### **PUBLIC INTEREST DETERMINATION**

The revised proposed IROC CRM2 Amendments impose costs and restrictions on the activities of market participants that are proportionate to the goals of the regulatory objectives sought to be realized and the enhanced transparency and standards of dealing with clients that will result. The IROC Board has determined that the proposed IROC CRM2 Amendments are not contrary to the public interest.



## PROPOSED IMPLEMENTATION DATES

The proposed implementation dates for the revised proposed IROC 2015 and 2016 CRM2 Amendments are as follows:

<b>Proposed implementation dates</b>
<p><b>July 15, 2015:</b></p> <ul style="list-style-type: none"><li>• Subsections 200.1(a), 200.1(b) and 200.1(e) [definitions of “book cost”, “cost” and “original cost”]</li><li>• Subsection 200.1(c) [definition of “market value” for the purposes of client reporting]</li><li>• Definition (g) of the General Notes and Definitions to Form 1 [definition of “market value” for the purposes of regulatory reporting to IROC]</li><li>• Subparagraphs 200.2(d)(ii)(F) and 200.2(d)(ii)(H) and revised “Guide to Interpretation of Rule 200.2” Item (d) [Inclusion of position cost in quarterly client account statements]</li><li>• Paragraph 200.2(d)(iii) [Inclusion of deferred sales charge notation in account statements]</li><li>• Subsection 200.2(e) and “Guide to Interpretation of Rule 200.2” Item (e) [Report on client positions held outside of the Dealer Member]</li><li>• Paragraphs 200.3(a)(i) and 200.3(a)(ii) and subsection 200.3(b) [option of earlier date for position cost information]</li><li>• Subsection 200.4(a), subsection 200.4(c) preamble and paragraph 200.4(c)(i) [timing of sending documents to clients - report on client positions held outside of the Dealer Member to be sent within 10 days of sending account statement]</li></ul>
<p><b>July 15, 2016:</b></p> <ul style="list-style-type: none"><li>• Subsections 200.1(d), 200.1(g) and 200.1(h) [definitions of “operating charge”, “trailing commission” and “transaction charge”]</li><li>• Subsection 200.1(f) [definition of “total percentage return”]</li><li>• Subsection 200.2(f) and “Guide to Interpretation of Rule 200.2” Item (f) [performance report]</li><li>• Subsection 200.2(g) and “Guide to Interpretation of Rule 200.2” Item (g) [fee / charge report]</li><li>• Subsection 200.2(l)(v) [trade confirmation disclosure of deferred charges]</li><li>• Paragraphs 200.3(a)(iii) and 200.3(a)(iv) [option of earlier date for performance report information]</li><li>• Subsection 200.4(b) [timing of sending documents to clients - performance report and fee / charge report to be sent together]</li><li>• Paragraph 200.4(c)(ii) [timing of sending documents to clients - performance report and fee/charge report to be sent within 10 days of sending account statement]</li></ul>

## CLASSIFICATION OF AMENDMENTS AND FILING IN OTHER JURISDICTIONS

IROC has determined that the revised proposed IROC 2015 and 2016 CRM2 Amendments are Public Comment Rules and they will therefore be republished for further public comment.

The revised proposed IROC 2015 and 2016 CRM2 Amendments will be filed with each of IROC’s Recognizing Regulators, in accordance with s.3 of the Joint Rule Review Protocol contained in the IROC Recognition Order.

**IROC Notice 14-0214– Rules Notice – Request for Comments - Republication - Dealer Member Rules – Client Relationship Model – Phase 2; Performance Reporting and Fee / Charge Disclosure; Amendments to Dealer Member Rule 200 and to Form 1**



## **REQUEST FOR PUBLIC COMMENT**

Comments are sought on the proposed amendments. Comments should be made in writing. Two copies of each comment letter should be delivered by November 17, 2014 (within 60 days from the publication date of this notice). One copy should be addressed to the attention of:

Richard J. Corner  
Vice President and Chief Policy Advisor, Member Regulation  
Investment Industry Regulatory Organization of Canada  
Suite 2000, 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  
19<sup>th</sup> Floor, Box 55  
20 Queen Street West  
Toronto, Ontario, M5H 3S8  
[marketregulation@osc.gov.on.ca](mailto: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](http://www.iiroc.ca) under the heading “IIROC Rulebook - Dealer Member Rules – Proposed Policy”).

## **ATTACHMENTS**

[Attachment A](#) - Text of revised proposed amendments;

[Attachment B](#) - Black-line comparison of the revised proposed IIROC 2015 and 2016 CRM2 Amendments to equivalent previously proposed amendments published for public comment on December 12, 2013;

[Attachment C](#)- Comparison of equivalent IIROC 2015 and 2016 CRM2 Amendment and CSA rule requirements; and

[Attachment D](#) - Response to public comments received on previously proposed amendments.