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Canadian Investment Regulatory Organization
Organisme canadien de réglementation des investissements

Rules Bulletin

Request for Comments
DC Rules

25-0080

March 27, 2025

Comments Due By: June 25, 2025

Contact:
Member Regulation Policy
Email: memberpolicymailbox@ciro.ca

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Rule Consolidation Project – Phase 5

Executive Summary

The Canadian Investment Regulatory Organization (**CIRO**) is publishing for comment Phase 5 of its Rule Consolidation Project rule proposals.[1] The Rule Consolidation Project will bring together the two member regulation rule sets currently applicable to investment dealers[2] and to mutual fund dealers[3] into one set of member regulation rules applicable to both categories of CIRO Dealer Members.[4]

The objective of Phase 5 of the Rule Consolidation Project (**Phase 5 Proposed DC Rules**) is to adopt requirements that are common to the IDPC and MFD Rules and have been assessed as having differences deemed to be significant with potential material impacts on stakeholders.[5]

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1 Rules Bulletin 23-0089 published on June 30, 2023, announced the Rule Consolidation Project objectives, principles and roadmap. Rules Bulletin 23-0147, Rules Bulletin 24-0007, Rules Bulletin 24-0145 and Rules Bulletin 24-0293 proposed new rules as part of Phase 1, Phase 2, Phase 3 and Phase 4 of the Rule Consolidation Project, respectively.

2 CIRO Dealer Members that are registered as an investment dealer or are registered as both an investment dealer and a mutual fund dealer are required to comply with the CIRO Investment and Partially Consolidated (**IDPC**) Rules.

3 CIRO Dealer Members that are registered as a mutual fund dealer and not registered as both an investment dealer and a mutual fund dealer are required to comply with the CIRO Mutual Fund Dealer (**MFD**) Rules.

4 Where a CIRO Dealer Member is a participant in one or more of the markets overseen by CIRO they also must comply with the CIRO Universal Market Integrity Rules (**UMIR**). UMIR will not be consolidated with other CIRO Rules as part of this project and will continue as a separate CIRO rule set.

5 Important stakeholders that were considered include investors, the public, investment dealers and their Approved Persons and employees, mutual fund dealers and their Approved Persons and employees and CIRO itself.

The Phase 5 Proposed DC Rules involves the adoption of rules relating to:

- outsourcing and service arrangements,
- continuing education,
- reporting and handling of complaints, internal investigations and other reportable matters,
- recordkeeping and client reporting,
- financial solvency,
- client asset use and custody, and
- financing arrangements.

How to Submit Comments

Comments on the Phase 5 Proposed DC Rules should be in writing and delivered by June 25, 2025 (90 days from the publication date of this Bulletin) to:

Member Regulation Policy
Canadian Investment Regulatory Organization
Suite 2600
40 Temperance Street
Toronto, Ontario M5H 0B4
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A copy should also be delivered to the Canadian Securities Administrators (**CSA**):

Trading and Markets
Ontario Securities Commission
Suite 1903, Box 55
20 Queen Street West Toronto, Ontario M5H 3S8
e-mail: TradingandMarkets@osc.gov.on.ca

and

Capital Markets Regulation
B.C. Securities Commission
P.O. Box 10142, Pacific Centre
701 West Georgia Street, Vancouver, British Columbia, V7Y 1L2
e-mail: CMRdistributionofSROdocuments@bcsc.bc.ca

Commentators should be aware that a copy of their comment letter will be made publicly available on the CIRO website at www.ciro.ca

Table of Contents

1. Background

One of the initial CIRO priorities is to consolidate the IDPC Rules and MFD Rules into one set of rules, the CIRO Dealer and Consolidated (**DC**) Rules, applicable to both investment dealers and mutual fund dealers.

The primary objectives of this consolidation work are:

- to achieve greater rule harmonization to:
  - ensure like dealer activities will be regulated in a like manner,
  - minimize regulatory arbitrage between investment dealers and mutual fund dealers,
- where practical and appropriate, adopt less prescriptive, more principles-based rule requirements to facilitate rules that are scalable and proportionate to the different types and sizes of dealer and their respective business models, and
- improve access to and clarity of the rules applicable to all CIRO Dealer Members.

Taking these objectives into consideration, the following decisions have been made relating to the structure and content of the DC Rules:

Matter	Decision
Rule organization structure and numbering approach	Use the IDPC Rule organization structure
Rule drafting convention	Standard rule with, where applicable, alternative compliance approaches to accommodate business model differences
Rule drafting style	Plain language
Rule development and implementation approach	The entire set of DC Rules will be implemented as a whole with an appropriate transition period.

The fifth phase of the Rule Consolidation Project focuses on:

- outsourcing and service arrangements (DC Rule 2400),
- continuing education (DC Rule 2700),
- reporting and handling of complaints, internal investigations and other reportable matters, (DC Rule 3700),
- recordkeeping and client reporting (DC Rule 3800),
- financial solvency (DC Rule 4100, 4200, DC Form 1),
- client asset use and custody (DC Rule 4300, 4400), and
- financing arrangements (DC Rule 4500, 4600).

Rule Series	Title and Description
1000	***Interpretation and Principles Rules****– provisions relating to:* • ***Definitions of common application throughout the rules – DC Rule 1200*** ○ ***Definition of the term "monthly financial report"***
2000	***Dealer Member Organization and Registration Rules – provisions relating to:*** • ***Acceptable Back Office and Service Arrangements – DC Rule 2400***

	• ***Continuing Education Requirements for Approved Persons – DC Rule 2700***
3000	***Business Conduct and Client Accounts Rules*** *– provisions relating to:* • ***Reporting and Handling of Complaints, Internal Investigations and Other Reportable Matters – DC Rule 3700*** • ***Recordkeeping and Client Reporting – DC Rule 3800***
4000	***Dealer Member Financial and Operational Rules*** *– provisions relating to:* • ***General Dealer Member Financial Standards – Minimum Capital, Early Warning, Financial Reports and Auditors – DC Rule 4100*** • ***General Dealer Member Financial Standards – Disclosures, Internal Controls, Calculations of Prices and Professional Opinions – DC Rule 4200*** • ***Protection of Client Assets – Segregation, Custody and Client Free Credit Balances – DC Rule 4300*** • ***Protection of Client Assets – Safekeeping Client Assets, Safeguarding Cash and Investment Products, and Insurance – DC Rule 4400*** • ***Financing Arrangements – Repurchase Market Trading Practices – DC Rule 4500*** • ***Financing Arrangements – Cash and Securities Loan, Repurchase Agreement, and Reverse Repurchase Agreement Transactions – DC Rule 4600***
5000	**Dealer Member Margin Rules** – Rules concerning margin requirements
6000	**Reserved** for future use
7000	**Debt Markets and Inter-Dealer Bond Brokers Rules** – Rules concerning debt market trading activities and inter-Dealer bond brokers
8000	**Procedural Rules - Enforcement** – Rules concerning investigations, enforcement proceedings, disciplinary proceedings, hearing committees, and rules of practice and procedure
9000	**Procedural Rules - Other –** rules concerning compliance examinations, approvals and regulatory supervision, regulatory review procedures, opportunities to be heard, alternative dispute resolution, and CIPF requirements.

2. Phase 5 Proposed DC Rules

This Bulletin describes the Phase 5 Proposed DC Rules where we propose substantive changes to dealer requirements that may have material impacts. Non-material changes to dealer requirements are detailed in the table of concordance and other supporting appendices. The following documents have been included as appendices to this Bulletin to provide details of the Phase 5 Proposed DC Rules:

- a clean copy of the Phase 5 Proposed DC Rules is included as Appendix 1,
- a blackline comparison of the Phase 5 Proposed DC Rules to the equivalent IDPC Rules (or previously proposed DC Rules) is included as Appendix 2,[6]

[6] A blackline comparison of the Phase 5 Proposed DC Rules to the equivalent MFD Rules has not been included as it was determined - due to the decision to use the existing IDPC Rule approaches to rule organization, numbering and drafting language (i.e., plain language), - that including the comparison would not assist in reviewing the proposed amendments.

- a clean copy of the Proposed DC Form 1 is included as Appendix 3,
- a blackline comparison of the Proposed DC Form 1 to the equivalent IDPC Form 1 is included as Appendix 4,[7]
- a table of concordance comparing:
  - the Phase 5 Proposed DC Rules to any existing equivalent requirements in the IDPC Rules, MFD Rules, and National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations*
  - and Proposed DC Form 1 to any existing equivalent requirement in IDPC Form 1, and MFD Form 1,

  is included as Appendix 5,
- a table comparing the existing IDPC Rules and MFD Rules complaint handling and reporting regimes with the Phase 5 Proposed DC Rules approach to the proposed definition of "serious misconduct" is included as Appendix 6, and
- an impact analysis of the Phase 5 Proposed DC Rules, as well as a summary of impacts by topic of related requirements, is included as Appendix 7.

In the next sections of this Bulletin, we summarize the key elements of the Phase 5 Proposed DC Rules, which in most cases adopt existing rule provisions from the IDPC Rules, the MFD Rules, or both sets of existing rules. We also discuss how all proposed provisions differ from their corresponding IDPC Rule or MFD Rule provision in the Table of Concordance (Appendix 5).

2.1 Decisions on significant differences with potential material impact to stakeholders

In this section of the Bulletin, we discuss decisions made in Phase 5 of the Rule Consolidation Project on the most significant differences in requirements within the IDPC and MFD Rules.

2.1.1 Additional account services we are proposing to allow mutual fund dealers to offer

As described in the Phase 4 bulletin, it has been decided that CIRO will proceed with the proposal to allow mutual fund dealers the ability to:

- offer margin accounts to clients in some scenarios, provided that certain conditions are met, and
- use client free credit cash balances within their operations.

In the Phase 5 Proposed DC Rules, we have limited these additional account services to Level 4 mutual fund dealers because only these mutual fund dealers offer client investment products in nominee name, which allows the dealer the ability to use the positions in the client account as collateral for margin debts.

The use of free credit cash balances is generally connected to margin lending, since the client free credits are used in the dealer's operations to finance the client debits. Although a Level 3 mutual fund dealer may hold client cash, we are not proposing to

[7] A blackline comparison of the Proposed DC Form 1 to the equivalent MFD Form 1 has not been included as it was determined - due to the decision to use the existing IDPC Form 1 approach to schedule organization, that including the comparison would not assist in reviewing the proposed amendments.

extend the ability for these mutual fund dealers to use client free credit cash balances within their operations, given that a Level 3 mutual fund dealer is handling client cash temporarily for purposes of settling client name transactions.

2.1.1.1 Margin Accounts

In the Phase 5 Proposed DC Rules we propose that if a Level 4 mutual fund dealer chooses to offer margin accounts or use client free credits, they must meet financial solvency standards equivalent to those that apply to investment dealers. This proposal allows Level 4 mutual fund dealers to offer more services, provided they comply with these higher standards, ensuring that similar activities are regulated in a like manner. Additionally, this approach also allows Level 4 mutual fund dealers with relatively simpler business models to continue their operations without the burden of meeting higher standards designed for more complex business models.

At the time we published the Phase 2 amendments for public comment, we did not propose to allow mutual fund dealers to offer margin loans to clients (proposed DC Rule 5100), as this possibility was still under consideration by CIRO staff. We recently announced when we published the Phase 4 amendments for public comment that we would be proposing to give mutual fund dealers this option.[8] To codify this option, we have proposed amendments:

- to a number of margin lending-related rule requirements to include Level 4 mutual fund dealers within scope, and
- that establish the conditions under which a Level 4 mutual fund dealer is permitted to offer margin lending.

The proposed conditions are listed in Phase 5 Proposed DC Rule subsection 5112(2) and include required compliance with DC Rule requirements for:

- margin accounts in sections 3245 to 3247,
- the sending of account statements in section 3851,
- minimum capital provisioning in sub-clause 4111(3)(i)(f),
- the filing of the audited annual Form 1 within the timeline specified in sub-clause 4151(1)(i)(a),
- the filing of an agreed-upon procedures report as required under subsection 4190(1),
- the segregation of fully paid and excess margin securities in sections 4310 to 4332,
- the calculation of margin required for client account margin for investment product positions and position offsets in Series 5000,

[8] Refer to section 2.1 of CIRO Rules Bulletin 24-0293 for the details relating to this announcement.

- the reporting of client account cash balances and margin required in Schedule 4 of Form 1, and
- the calculation of the securities concentration charge in Schedules 11, 11A and 11B of Form 1.

2.1.1.2 Use of client free credit cash

We also announced within the Phase 4 amendments consultation document that we would be proposing to allow mutual fund dealers to use client free credit cash balances within their operations. To codify this option, we have proposed amendments:

- to a number of client free credit cash balance-related rule requirements to include Level 4 mutual fund dealers within scope, and
- that establish the conditions under which a Level 4 mutual fund dealer is permitted to use client free credit cash balances.

The proposed conditions are listed in DC Rule subsection 4382(2) and include required compliance with DC Rule requirements for:

- minimum capital provisioning in sub-clause 4111(3)(i)(f), and
- compliance with client free credit cash usage and segregating excess free credit cash balances in Rule 4300, Part C and Statement F and Schedule 2 of Form 1.

2.1.1.3 Process to be followed to expand services

A mutual fund dealer that chooses to expand their services will be required to notify CIRO in writing before making such material change to its business activities pursuant to DC Rule subsection 2246(2). CIRO will review the request to ensure the dealer has the appropriate systems, controls and capital to offer margin accounts (or use free credits) and meet the associated rule requirements.

As is the case with all other Phase 5 Proposed DC Rules, these proposed expansions to the account services that can be offered by mutual fund dealers are subject to CSA review and approval. Further, should we receive a significant number of material comments on these proposed expansions that suggest that pursuing them will be highly controversial, we may decide to pursue them as separate proposals to not delay the completion of the Rule Consolidation Project.

2.1.2 Account types that cannot be offered by mutual fund dealers

As discussed in the Phase 4 amendment consultation document, it has been determined that CIRO will not proceed with the proposals of allowing mutual fund dealers the ability to offer discretionary accounts, managed accounts or order execution only accounts as part of the Rule Consolidation Project. Any such proposals would be developed in consultation with the CSA as part of a separate

policy project with a separate timeline. To reflect this decision within the proposed Phase 5 Proposed DC Rules, we have added a provision to provide additional clarity on the accounts and services a mutual fund dealer is prohibited from offering. (previously published as part of the proposed Phase 1 amendments). ***(DC Rule subsection 1102(4))***

2.1.3 Financial solvency reporting

One of the material differences in the existing IDPC Rules and MFD Rules is that both sets of rules prescribe the regular completion and submission of different dealer financial solvency reports, both of which are identified as Form 1. Both forms include different sets of calculations designed to determine the Dealer Member's risk adjusted capital.

To ensure consistency and reduce regulatory arbitrage, we propose one consolidated financial solvency report (**DC Form 1**) which applies the same formula for calculating risk adjusted capital to both mutual fund dealers and investment dealers. We maintain some differences within the formula, such as the minimum capital requirements. We also propose separate lines and schedules for reporting requirements that are unique to either investment dealers or mutual fund dealers.

Since we propose adopting the IDPC Form 1 risk adjusted capital formula, this may have a significant impact on certain mutual fund dealers. As a result, we propose a phased implementation approach for those components of the formula expected to have the most significant impact.

We recognize that several statements and schedules may not apply to dealers with limited or simple business activities. Therefore, we plan to customize the regulatory filing system to reduce input fields to those relevant to each dealer's business.

More details on the proposed DC Form 1 are described in section 2.11 of this Bulletin.

2.2 Rule interpretation and definitions of common application throughout the rules *(DC Rules 1100 and 1200)*

In Phase 5 Proposed DC Rules, we propose revisiting DC Rule 1100 and DC Rule subsection 1201 with the scope of adding new definitions or amending several interim definitions proposed in Phase 1.[9]

2.2.1 Mutual fund dealer business structures

We propose to adopt MFD Rule 1.1.1 with regard to certain Approved Persons of mutual fund dealers engaging in securities related business as an employee of a

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[9] In Phase 1 we identified material differences that required further consideration as part of future phases of the Rule Consolidation Project. As such, at that time we proposed interim definitions, where applicable, which may need revisiting once a decision was made on the material differences in future phases. See section 2 of Rules Bulletin 23-0147.

chartered bank or credit union, where permitted by applicable legislation. ***(DC Rule subsection 1102(5))***

2.2.2 "Monthly financial report" definition

We propose introducing a definition for the term "monthly financial report" in the DC Rules. This definition clarifies that the financial report submitted to CIRO on a monthly basis does not include all the statements and schedules in the Form 1 report. The DC Form 1 general notes and definitions specify which statements and schedules must be submitted for the monthly financial report.

2.2.3 Amended terms and definitions

2.2.3.1 Amended terms from previous phases

We propose amending the definitions of "market value" and "introducing broker" that were published in Phase 1, to better reflect subsequent developments in the Rule Consolidation Project and remove any inconsistencies and redundancies. We have not carried forward the market value definition from the IDPC Form 1 to the DC Form 1, since this definition is included in the section 1201 definitions that apply throughout the CIRO requirements.

2.2.3.2 Form 1 terms and definitions

We propose to adopt the IDPC Form 1 approach to measuring financial solvency including assessing custody and credit risk as this approach provides a more rigorous and comprehensive assessment of risks. In Phase 1 we proposed interim terms and definitions in the DC Rules that were relevant in the context of a separate Investment Dealer Form 1 and Mutual Fund Dealer Form 1. Since we are proposing one consolidated Form 1 in Phase 5 Proposed DC Rules, conforming amendments to the following terms are necessary:

- acceptable clearing corporation,
- acceptable counterparty,
- acceptable exchange,
- acceptable institution,
- acceptable securities location,
- designated rating organization,
- early warning excess,
- early warning reserve,
- regulated entity,
- risk adjusted capital, and
- total margin required.

2.2.4 Repealed terms

In Phase 1 we expanded or introduced interim terms and definitions in the DC Rules that were relevant in the context of a separate Investment Dealer Form 1 and Mutual Fund Dealer Form 1 but are no longer relevant in the context of the proposed consolidated Form 1. As such, we propose repealing the following terms from the DC Rules:

- Acceptable entity,
- Investment Dealer Form 1, and
- Mutual Fund Dealer Form 1.

2.3 Acceptable back-office and service arrangements *(DC Rule 2400)*

In this section of the Bulletin, we discuss the proposed requirements relating to:

- Introducing broker/carrying broker arrangements (**IB/CB arrangements**),
- Other outsourcing and back-office arrangements, and
- Service arrangements.

2.3.1 Introducing broker/carrying broker arrangements

We propose adopting the IDPC Rule requirements for the existing Type 1 to 4 IB/CB arrangements. We also propose adopting the majority of the MFD Rule requirements for introducing and carrying arrangements between two mutual fund dealers. Given the complexity of various business models and the potential for diverse arrangements between investment dealers and mutual fund dealers, we propose giving CIRO staff the ability to grant exemptive relief from the requirements pertaining to IB/CB arrangements. Below we discuss each such proposal in more detail.

2.3.1.1 Type 5 IB/CB arrangements

We propose labelling IB/CB arrangements between two mutual fund dealers as Type 5 IB/CB arrangements. ***(DC Rule section 2430)***

The requirements for these Type 5 arrangements are mainly based on the existing IB/CB arrangement requirements in MFD Rule 1.1.6 and are generally similar to the investment dealer Type 2 IB/CB arrangement requirements. Given these general similarities, we are proposing to further align the Type 5 requirements with the Type 2 requirements by:

- adding a requirement to the Type 5 IB/CB arrangements for the introducing broker to report and margin their own principal positions,
- adding a requirement to the Type 5 IB/CB arrangements for the introducing broker to include all accounts introduced to the carrying broker when calculating client net equity for purposes of insurance requirements,

- modifying the existing MFD Rule requirement, whereby the client is to be considered a client of the carrying broker, to the proposed requirement that the client be considered a client of both the introducing and carrying broker, and
- removing the MFD Rule requirement that the carrying broker has responsibility for reporting and sending statements and confirmations.

We expect the impact on mutual fund dealer introducing brokers of reporting and margining their own principal positions will be minimal as this is generally being done in practice, even though it is not prescribed in the MFD Rules.

We expect mutual fund dealers may have to modify their introducing broker/carrying broker agreements to clarify that clients are considered clients of both the introducing and carrying broker. This modification is consistent with the requirement that compliance with CIRO requirements is a joint responsibility between the introducing and carrying brokers.

Under the IDPC Rules for IB/CB arrangements, both the introducing broker and carrying broker are required to include all accounts, introduced to the carrying broker, in the client net equity calculation when determining the amount of insurance coverage required. Under the MFD Rules, only the carrying broker is required to include the introduced accounts when determining the amount of insurance coverage. In harmonizing the insurance requirements for introducing brokers in the DC Rules, for Type 5 IB/CB arrangements we require both the introducing broker and carrying broker to include the accounts introduced to the carrying broker in determining insurance requirements. We expect this requirement to impact Level 3 and 4 mutual fund dealers but not Level 1 or 2 mutual fund dealers as such dealers only introduce accounts where the assets are not held or controlled by the dealer (intermediary accounts). Only assets that are held or controlled by the dealer and owed to the client are included in determining client net equity for insurance requirements.

Client reporting services should be arranged between the two parties to determine which Dealer Member will perform the functions of sending statements and confirmations to clients. While the carrying broker may handle the function of sending a statement or confirmation as part of their client reporting services, both the carrying broker and the introducing brokers are responsible for ensuring the statements and confirmation comply with the rules. This proposal is consistent with CIRO's regulatory principles of outsourcing, including those established by its predecessors.

2.3.1.2 Arrangements that may be executed

In the DC Rules, we propose to clarify the type of IB/CB arrangements that may be executed by a mutual fund dealer. We also clarify the types of

additional arrangements that a mutual fund dealer may enter into, if they have an existing Type 5 IB/CB arrangement. ***(DC Rule sections 2403 and 2407)***

Under the proposal, a mutual fund dealer that is party to a Type 1 or 2 arrangement with an investment dealer, is restricted from entering into any other IB/CB arrangements unless an exemption is obtained. This is consistent with the existing restriction for an investment dealer that is party to a Type 1 or 2 IB/CB arrangement. The carrying broker under a Type 1 or 2 IB/CB arrangement is financially responsible for the obligations of the introducing broker's clients and must look to the introducing broker for repayment of any loss in the event of default by the introducing broker's clients. Allowing the Type 1 or 2 introducing broker to have another IB/CB arrangement, could create additional risk to the existing carrying broker that losses would not be covered.

We are preserving the ability of a mutual fund dealer to engage in multiple Type 5 arrangements, recognizing that a mutual fund dealer introducing broker often collaborates with several mutual fund dealer carrying brokers. Additionally, since mutual fund dealers under these arrangements are prohibited from offering margin or using free credits, there are no significant financing and margining concerns associated with multiple arrangements.

The Type 5 arrangement requirements have been drafted on the basis that the mutual fund dealer introducing broker is not offering margin accounts or using client free credit cash. Should the mutual fund dealer introducing broker decide to offer margin accounts while maintaining a Type 5 arrangement, they will need to request an exemption from the Type 5 arrangement requirements. This exemption would be subject to terms and conditions pertaining to margin requirements.

The proposed restrictions in DC Rule section 2403 and 2407 do not allow a mutual fund dealer to be a carrying broker for an investment dealer because the mutual fund dealer IB/CB arrangement requirements are designed for dealers with simple business models where margin accounts are not offered and products are limited to those investment products that mutual fund dealers can sell. ***(DC Rule section 2409)***

2.3.1.3 Exemptions to IB/CB arrangement requirements

We are introducing a new section that will give CIRO staff the ability to grant exemptions from the IB/CB arrangement requirements and impose terms and conditions on those exemptions. Although Type 1 and 2 introducing brokers are restricted from entering into additional IB/CB arrangements or self-clearing, there may be instances where a second arrangement is justified, such as where the introducing broker seeks a secondary arrangement for their futures contract trading business. The

proposed exemption provision provides us with the flexibility to grant exemptions to other conditions and requirements related to IB/CB arrangements that may be necessary as mutual fund dealers begin using investment dealers as carrying brokers or opt to offer margin accounts to clients.

While the carve-out for futures trading was specified in the IDPC Rules, we recognize that there may be other situations beyond futures trading that justify multiple IB/CB arrangements. Consequently, to ensure adequate rule responsiveness, we have not included the specific carve-out for futures business within the DC Rules. Dealers currently engaged in futures business under a secondary arrangement will be required to obtain an exemption under the new DC Rule requirements. ***(DC Rule section 2408)***

2.3.2 Other outsourcing and back-office arrangements

We propose adopting the IDPC Rule requirements for other permitted outsourcing and back-office arrangements such as:

- arrangements with a foreign affiliate,
- arrangements with a Canadian financial institution affiliate, and
- clearing arrangements with other dealers.

Both investment dealers and mutual fund dealers will be subject to these requirements should they enter into such arrangements. ***(DC Rule 2400 Parts B and C)***

2.3.3 Service arrangements

We propose adopting the requirements for service arrangements that are currently in MFD Rule 1.1.3. We have also clarified that these service arrangement requirements apply regardless of whether the Dealer Member (or Approved Person) is providing or receiving the service. ***(DC Rule section 2490)***

We propose introducing a definition for "service arrangements" to provide more clarity on the difference between a service arrangement and other outsourcing arrangements. ***(DC Rule subsection 2402(1))***

There are no equivalent requirements for service arrangements in the IDPC Rules for investment dealers, but CIRO has published a guidance note on outsourcing arrangements for investment dealers (*Outsourcing arrangements* GN-2300-21-003), which includes similar expectations to the requirements proposed in DC Rule 2400.

2.4 Continuing Education Requirements for Approved Persons *(DC Rule 2700)*

A harmonized approach to the continuing education regime across Dealer Members is currently being pursued in a separate CIRO project published on December 19, 2024 in Rules Bulletin 24-0356. As such, for the purposes of the Phase 5 Proposed DC Rules, we propose to adopt and maintain the existing separate continuing education regimes as an interim measure.

This ensures that the industry will only be required to absorb changes for the purpose of harmonization under one project, thus avoiding a duplicative or redundant regulatory burden on Dealer Members.

2.5 Reporting and handling of complaints, internal investigations and other reportable matters *(DC Rule 3700)*

In this section of the Bulletin, we discuss the proposed requirements relating to:

- reporting requirements set out in DC Rule 3700 Part A (**Reporting Requirements**),
- internal investigation and internal discipline requirements set out in DC Rule 3700 Part B (**Internal Investigation Requirements)**,
- client complaint handling requirements set out in DC Rule 3700 Parts D & E (**Complaint Requirements)**.[10]

In addition to the guiding objectives of the Rule Consolidation Project, the proposed requirements under DC Rule 3700 also aim to:

- make Reporting Requirements, Internal Investigation Requirements, and Complaint Requirements clearer and more consistent with CIRO's expectations by using common triggers,
- reduce duplicative reporting to CIRO by eliminating overlapping Reporting Requirements between those proposed in the DC Rules and those required under the Universal Market Integrity Rules (UMIR), and
- enhance our Complaint Requirements by codifying client complaint handling best practices which will help us to:
    - anticipate client complaints and inquires made to CIRO, and respond to them efficiently,
    - better assess each Dealer Member's risk, to inform the frequency and content of our compliance examinations, and
    - protect capital markets from harmful conduct.

We anticipate the impact of DC Rule 3700 to vary based on Dealer Members' existing complaint practices. For some Dealer Members, these changes may result in an increase in the number of complaints they investigate and respond to. For others, who currently may be reporting and investigating matters more broadly than those specifically included in the existing Rules, these changes may result in a more limited impact on their existing practices.

In the next section of this Bulletin, we summarize the key elements of the proposed requirements.

2.5.1 Definitions (*DC Rule subsection 3702(1)*)

[10] Phase 5 Proposed DC Rule 3700 includes proposed changes to the existing language in IDPC Rule 3700 that were initially proposed in the IIROC Rules Notice and Request for Comment 22-0009 Proposed Amendments respecting Reporting, Internal Investigation and Client Complaint Requirements (Rule Enhancements).

Defined terms provide consistency and clarity throughout this Rule so that reporting, investigations, and complaint handling are handled consistently across Dealer Members and are aligned with CIRO's expectations regarding the types of matters in scope under these proposed requirements.

We propose to adopt the following pre-existing definitions under DC Rule 3700:

- "compensation", from the MFD Rules, and
- "cybersecurity incident", from the IDPC Rules.

We propose to introduce new definitions, or made material changes to the existing definitions, for the following terms:

- "approved ombudsman service",
- "complaint" (which reflects the feedback received pursuant to the Rule Enhancements consultation and includes both verbal and written complaints),
- "internal dispute resolution service", and
- "non-reportable complaint" (which replaces the pre-existing concept of a "service complaint" from the IDPC Rules and MFD Rules).

2.5.1.1 "Serious misconduct" and "serious client-related misconduct"

The existing IDPC Rules and MFD Rules identify a number of specific matters that are directly related to Approved Persons' activities that must be reported to the Dealer and to CIRO. These matters are mostly, but not exactly, consistent between the IDPC Rules and MFD Rules.

We propose to introduce a definition of "serious misconduct" that will apply to both Approved Persons and employees, and contain a non-exhaustive list of reportable matters. The reportable matters include those that were listed in IDPC Rule section 3706 and subsection 3721(2) (now proposed DC Rule section 3720 and section 3751), as well as certain reportable matters contained in the MFD Rule 600 (4)-(6). We believe the matters reflected in the proposed definition of "serious misconduct" are examples of issues that present a reasonable risk of material harm to clients or the capital markets.

We also propose to include a principles-based element of the definition that is intended to capture matters that may not be specifically enumerated within the definition, but may present:

- a reasonable risk of material harm to clients or the capital markets, or
- material non-compliance with CIRO's requirements,[11] securities laws or any other applicable laws.

[11] Under subsection 1201(2), we include UMIR in the definition of "Corporation requirements".

In addition, we propose to introduce a definition of "serious client-related misconduct"**.** This definition is used in situations where CIRO is specifically concerned about serious misconduct that may have an effect on clients.

In Appendix 6 of this Bulletin, we**:**

- list the types of misconduct that are captured under the current Reporting Requirements and Complaint Requirements in the IDPC Rules and the MFD Rules, and
- clarify which types of misconduct have been included in the proposed DC Rules under the definition of "serious misconduct".

2.5.2 Reporting Requirements (*DC Rule Part A – sections 3710-3712)*

The existing IDPC Rules and MFD Rules relating to Reporting Requirements are prescriptive and share similarities but are not completely aligned in terms of which matters are reportable to the applicable regulator.

This has led to inconsistencies and gaps in reporting relating to matters where there may be a risk of material harm to clients or the capital markets, or where there is material non-compliance with CIRO requirements, securities laws, or other applicable laws.

To address these inconsistencies, we have made a number of changes to the Reporting Requirements, which include:

- the introduction of the defined term "serious misconduct", as described above, and the corresponding requirements to report instances and complaints alleging such conduct, and
- extending the Reporting Requirements, which previously applied only to Approved Persons, to now apply to employees of the Dealer Member.

As a result, Dealer Members will be required to establish policies and procedures that require employees to report to the Dealer Member the matters set out in Proposed DC Rule subsection 3710(2), specifically in respect of *such* matters occurring while they were engaging in Dealer Member related activities, while employed by the Dealer Member. Dealer Members will also be required to report such matters to CIRO, as specified in proposed DC Rule clause 3711(1)(v)).

We believe that taking a prescriptive approach, namely by specifying which matters are captured under the Reporting Requirements, will better enable Dealer Members to quickly and consistently identify matters that must be reported to CIRO. This may even decrease the overall amount of reporting by clarifying the types of matters that are not considered reportable.

2.5.2.1 Reporting to the Dealer Member (*DC Rule section 3710*)

In addition to requiring the reporting of serious misconduct, we also propose to adopt the requirements set out in the MFD Rules which state that Approved Persons (and now also employees, given that this requirement has

been extended to employees under section 3711 of the Proposed DC Rules) must report certain matters pertaining to said individual, including:

- cancellation, suspension, or the addition of terms and conditions to a registration or license by any regulatory organization, SRO, professional licensing, credentialling or registration body,
- declaration of bankruptcy, suspension of payments of debts generally or the making of an arrangement with creditors or making an assignment or being deemed insolvent, or
- outstanding garnishments rendered against the individual. ***(DC Rule clauses 3710(1)(v) and 3711(1)(iv))***

2.5.2.2 Reporting by a Dealer Member to the CIRO (*DC Rule section 3711)*

The matters that Dealer Members are required to report to CIRO under proposed DC Rule section 3711 are generally consistent with the changes described above that apply to DC Rule section 3710. Some differences exist, as we took into account that upon investigation, Dealer Members may determine that certain matters reported by the Approved Person or employee, such as complaints, or civil actions, do not meet the threshold of "serious misconduct" and consequently do not require reporting to CIRO.

We also propose a new requirement for Dealer Members to report any substantial compensation paid to a client. We expect Dealer Members will use their professional judgment in determining what substantial compensation means, considering their business practices and the client's circumstances. This new requirement replaces, and takes a less prescriptive approach than, the existing requirements under the MFD Rules and IDPC Rules that set specific dollar amount thresholds for reporting. ***(DC Rule clause 3711(1)(iii))***

We propose to update the reporting requirements to remove the dollar thresholds for reporting internal disciplinary actions, and require Dealer Members report to CIRO, any disciplinary action they take against an Approved Person or employee involving allegations of serious misconduct. *(**DC Rule clause 3711(3)(ii))***

We propose to adopt MFD Rule 600 (7.1) that requires Dealer Members to report the outcomes of client complaints alleging serious misconduct. There is no specific provision in the IDPC Rules requiring Dealer Members to report client complaint outcomes. We believe such reporting provides important information related to investor protection, compliance tracking and governance. ***(DC Rule clause 3711(3)(iii))***

We propose to adopt the existing requirement under the IDPC Rules that Dealer Members report any cybersecurity incident to CIRO. There is no current MFD Rule that deals with cybersecurity reporting. ***(DC Rule subsection 3712(1))***

We propose to add a provision similar to the MFD Rules[12] which require Dealer Members to report any material breach of client information. Given that breaches of personal information can have significant negative consequences for investors, and frequently occur outside the context of a reportable cybersecurity incident, we believe a distinct reporting requirement is necessary to ensure such issues are tracked and addressed. To manage regulatory burden, we propose to only require reporting to CIRO for incidents that are reportable under applicable privacy legislation, in the form and in compliance with the timelines required by such legislation. ***(DC Rule subsection 3712(2))***

2.5.2.3 Supporting documentation and record keeping (*DC Rule section 3804)*

The IDPC Rules require that a Dealer Member must make its records available to the *Corporation* upon request.[13]

MR0162 and IIROC Notice 11-0142 outline the types of supporting documents we may expect Dealer Members to provide CIRO for each reportable event. However, the existing IDPC Rules do not explicitly capture this supporting documentation as part of the general requirements to maintain records. As such, we propose to introduce DC Rule clause 3804(1)(xxi) to clarify that Dealer Members must maintain current records relating to reportable matters under proposed DC Rule subsections 3711-3712, and that these records are now explicitly captured under the requirement to provide such records to CIRO upon request. This requirement is consistent with the existing requirement under the MFD Rules.[14] ***(DC Rule clause 3804(1)(xxi))***

2.5.3 Internal Investigations and Internal Discipline

The current triggers for an internal investigation in the IDPC Rules and MFD Rules are not consistent and do not align with the proposed definition of "serious misconduct." We propose to base the trigger for an internal investigation on the concept of serious misconduct. We also propose to extend this section to the conduct of employees.

2.5.3.1 Requirement to commence an internal investigation (*DC Rule section 3720)*

We propose to adopt the prescriptive approach that is set out in the IDPC Rules, which specifically sets out the triggers for an internal investigation. The proposed approach clarifies that an investigation must be launched when the Dealer Member becomes aware that the Approved Person, former Approved Person or employee appears to have engaged in serious

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12 MFD Rule 600(4.1)(b)(ii) and 600(6.1)(b)(ii).

13 IDPC Rule subsection 3804(4).

14 MFD Rule 300(V) and 300(I)(Complaints)(9)(5).

misconduct. In the case of employees, the serious misconduct or appearance of serious misconduct must have occurred while the employee was in the employ of the Dealer Member and must concern matters that occurred while engaged in Dealer member related activities. ***(DC Rule subsections 3720(1) and (2))***

We have opted not to prescribe how Dealer Members should conduct internal investigations. This is a departure from the current prescriptive approach set out in MFD Rule 300(III) (Supervisory Investigations). We intend to provide guidance regarding how to identify situations that require investigation and recommended investigative processes.

2.5.3.2 Records of internal investigation (*DC Rule section 3721)*

We propose to adopt the existing requirement under the IDPC Rules that Dealer Members must maintain records of an internal investigation, including certain contents that are not currently explicitly required. Such records are not required in the MFD Rules. Given that the trigger for an internal investigation involves serious misconduct, we believe it is important to ensure that the documentation evidencing such investigation forms a complete record for review and compliance purposes. ***(DC Rule subsections 3721(1) and DC Rule clause 3804(1)(xxiii))***

2.5.3.3 Exceptions to reporting requirements (*DC Rule section 3723*)

To prevent duplicative reporting, we propose to introduce a new exception so that the reporting requirements under Rule 3700 do not apply for any matter reported to the CIRO under Universal Market Integrity Rules 10.16, 10.17 and 10.18. ***(DC Rule section 3723)***

2.5.4 Settlements and Confidentiality restrictions – Restrictions/Release

Consistent with MFD Rule 300(I)(Complaints)(10), we will also clarify that a Dealer Member must not impose confidentiality or similar restrictions on a client pursuant to a release entered into between the Dealer Member and client, or otherwise. This is intended to ensure that such restrictions are not imposed even in circumstances that do not involve a release.

We also propose to introduce a provision to prohibit Dealer Members from preventing clients, via a release agreement or otherwise, from communicating or sharing information with securities regulatory authorities or other enforcement authorities. ***(DC Rule section 3731)***

2.5.5 Client complaints – Institutional clients (*DC Rule subsection 3740*)

We acknowledge that the relationship between Dealer Members and institutional clients differs from the relationship between Dealer Members and retail clients. The sophistication, knowledge and balance of power in the former relationship merits a

different standard of engagement with institutional clients when dealing with complaints.

The current MFD Rules do not distinguish between retail clients and institutional clients. As such we propose to adopt the IDPC Rule regime, which sets out different standards for institutional client and retail client complaint handling.

2.5.5.1 Complaint policies and procedures (*DC Rule subsection 3740*)

We propose to adopt the existing IDPC Rule, which outlines the policies and procedures relating to complaints for institutional clients. Consistent with the proposed DC Rules set out above, we also propose to use the proposed term *serious client-related misconduct* as the threshold for requiring a Dealer Member to acknowledge, in writing, a complaint by an institutional client.

We propose that Dealer Members should only be required to acknowledge verbal complaints alleging serious client-related misconduct where a preliminary investigation suggests the allegation may have merit. This differs from the existing requirement, which mandates acknowledgement of all verbal complaints alleging serious client-related misconduct can be handled at the Dealer Member's discretion. Dealer Members are required to investigate to determine if the complaint has merit, and if it does, they must acknowledge the complaint accordingly.

2.5.6 Client complaints – Retail clients (*DC Rule sections 3750- 3759*)

2.5.6.1 Retail client complaints (*DC Rule 3750*)

The existing IDPC Rules require a written response to a written complaint alleging misconduct, and to a verbal complaint which alleges misconduct, and where a preliminary investigation indicates it may have merit. The existing MFD Rules require a written response to all written complaints and all other complaints that are not subject to informal resolution.

The definition of *complaint* under the proposed DC Rules removes the distinction between verbal and written complaints. Therefore, in contrast to the existing regimes, we propose to require that Dealer Members provide a written response to any written retail client complaint, and any retail client complaint alleging serious misconduct. We believe this appropriately addresses the types of complaints that raise regulatory concern, while permitting Dealer Members to manage verbal complaints that do not allege serious misconduct in a more expeditious manner. ***(DC Rule subsection 3750(3))***

2.5.6.2 Complaint policies and procedures (*DC Rule section 3753 and 3740(3)*)

We propose to remove the requirement in the IDPC Rules that Dealer Members must handle complaints in a balanced manner considering the

interests of the client, Dealer Member, Approved Person and employee. We determined that this is inconsistent with the Dealer Member's and Approved Person's obligation to put the client's interests first when managing conflicts of interest. ***(DC Rule sections 3106-3107 described in Phase 4 of the current Rule Consolidation Project)***

2.5.6.3 Response to client complaints *(DC Rule 3756)*

As set out above, the IDPC Rules and the MFD Rules require that Dealer Members provide a substantive response letter to complainants. We propose to introduce a requirement regarding the information Dealer Members must disclose in that letter; specifically, the response must indicate that clients may report suspected serious misconduct to CIRO, and that CIRO will assess whether any disciplinary action is warranted**. *(DC Rule clause 3756(3)(v))***

We propose to adopt the IDPC Rules requirement that Dealer Members provide a substantive response to a client complaint within 90 days. While the MFD Rules do not prescribe a timeline for the substantive response, Companion Policy *Registration Requirement*s, Exemptions *and Ongoing Registrant Obligations,*[15] which applies to securities dealers, recommends that complaints be resolved within 90 days. Therefore, the impact of this change upon Dealer Members should be minimal as the 90-day period is already consistent with best practice and regulatory expectations across the industry.

We note that the Autorité des marchés financiers has adopted a 60-day (+ 30-day flex period) timeline for entities under their jurisdiction to provide a substantive response to a complaint.[16] However, given that the balance of the CSA members recommend a 90-day period as per Companion Policy 31-103, we are proposing to adopt an approach in the proposed DC Rules that is consistent with the general industry practice. In this regard, we have asked a question later in this Bulletin seeking public comment on whether a 90-day time limit to provide a substantive response letter to a complainant is appropriate. We also propose to introduce a limit on a Dealer Member's internal dispute resolution process. The current IDPC Rule does not place a limit on how long a Dealer Member's internal dispute resolution service can take to respond to a client complaint. Effectively, this may allow the complaint resolution process to drag on indefinitely. To ensure that a complaint is resolved within a reasonable time frame, we propose to limit this to a maximum of:

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[15] See section 13.15 of the Companion Policy 31-103 CP *Registration Requirements, Exemptions and Ongoing Registrant Obligations*.

[16] See the *Règlement sur le traitement des plaintes et le règlement des différends dans le secteur financier*.

- 90 days from the date the internal dispute resolution service received the complaint, where no substantive response letter has been issued, provided that no more than 120 days has elapsed from the date the Dealer Member initially received the complaint, or
- 30 days from the date the internal dispute resolution service received the complaint, where the internal dispute resolution service received the complaint after the issuance of the substantive response letter.

Consistent with our proposed complaint handling standards, this will ensure that complaints are resolved more expeditiously. ***(DC Rule subsection 3756(5))***

2.5.6.4 Communication of dispute resolution service options (*DC Rule section 3759*)

We propose to introduce a provision that addresses the concerns articulated in CIRO Guidance Note GN-3700-21-003. This guidance lists acceptable practices for the communication of internal dispute resolution services and OBSI services from Dealer Members to clients. We propose to include certain acceptable practices for communicating internal dispute resolution services and OBSI services into the proposed DC Rules to clarify and standardize disclosure to clients regarding dispute resolution service options.

In addition, consistent with this guidance, we propose prohibiting the use of any misleading terms, including "ombudsman" or similar terms, in referring to a Dealer Member's, or its affiliate's, internal dispute resolution service.

2.6 Recordkeeping and client reporting *(DC Rule 3800)*

In this section of the Bulletin, we discuss significant proposed amendments to rule requirements relating to:

- recordkeeping, and
- client reporting.

Aspects of the recordkeeping and client reporting requirements, in both the IDPC Rules and MFD Rules, are currently being reviewed under a separate project, known as the Total Cost Reporting Enhancements,[17] with proposed amendments expected to take effect before the implementation of the Rule Consolidation project (**TCR Enhancements**). Given their contextual relevance, we show the TCR Enhancements - in their published version - in the proposed draft of DC Rule 3800 (highlighted in grey). The TCR Enhancements are outside of the scope of this Phase 5 consultation, and therefore we are not seeking comments in this Bulletin.

2.6.1 Scope and approach to Rule 3800

[17] The proposed Total Cost Reporting Enhancements have been published via CIRO Rules Bulletin 24-0288.

We are consolidating under DC Rule 3800 the recordkeeping and client reporting requirements, which are currently outlined in IDPC Rule 3800 and MFD Rule 5. While these two rulesets are largely aligned, particularly at a principles level, notable differences in common requirements still exist. Some of these differences are due to the Dealer model, while most are either legacy differences or drafting variations. Maintaining these differences could lead to diverging practices across the Dealer categories.

We propose aligning all the requirements applicable to investment dealers and mutual fund dealers, apart from the areas discussed in sections 2.6.4.2 and 2.6.4.8 of this Bulletin. The outcome is a consolidated DC Rule 3800 setting out common recordkeeping and reporting requirements that are uniform and which applicability to a specific Dealer depends on the service or product they offer, or deal in, rather than their registration category.[18] This is consistent with the project objective of regulating like activities in like manner while maintaining high standards of investor protection.

In terms of impact, the proposed DC Rules generally represent existing expectations about recordkeeping and client reporting as outlined in various sections of the current rules and guidance notes. Where we propose extending existing rule carveouts from one dealer category to another, we anticipate a reduced burden on the affected Dealer category. In limited instances where we propose bringing a Dealer category to the higher standard of another, the affected Dealer category, or a subset thereof, may have to incur the burden of systems upgrades or enhancements in supervision and compliance.

Our proposal also reflects decisions taken in the preceding phases of the Rule Consolidation, and which have been published for comments, such as to:

- clarify within our rules when a regulatory obligation relates to all "investment product" offerings, or offerings of only certain investment products (such as securities or derivatives or precious metals bullion only),[19] and
- offer mutual fund dealers the option of categorizing clients between "institutional client" and "retail client", for the purposes of rule applicability respective of each such client category, in alignment with investment dealers.

2.6.2 Definitions *(DC Rule section 3802)*

[18] DC Rule 3800 requirements are secondary to those in other areas of the rules governing the products and services a Dealer can offer. As such, except when indicated, the proposed DC Rule 3800 requirements are agnostic of whether a Dealer is an investment dealer or mutual fund dealer. Whether a recordkeeping or reporting requirement applies to a Dealer, such as those specific to derivatives products or managed accounts, depends on whether the Dealer is permitted to, and actually engages in, such products or services.

[19] This proposal, including the proposed definition of investment products, has been published for comments via Rules Bulletin 24-0293 Rule Consolidation – Phase 4 (**Phase 4 Bulletin**). Under the new definition, "investment products" means "a product that (i) is a security, (ii) is a derivative, (iii) is a precious metals bullion, or (iv) has been approved by the Board as an investment product".

We propose adopting the common concepts and definitions across the IDPC Rules and MFD Rules that are already materially aligned. In addition, we propose the following:

- *Automatic plan transactions*: We propose defining automatic plan transactions for the purposes of the proposed exemptions from trade confirmations and month-end account statements, discussed later on in this Bulletin,
- *Client's holdings in Dealer control versus "outside holdings"*: The IDPC Rules distinguish between client's holdings under Dealer control and "outside holdings", as defined in these rules, aligning with National Instrument 31-103. In comparison, the MFD Rules use the concepts of nominee accounts and client name assets, which are comparable but not technically equivalent. Allowing these bifurcations to coexist in the DC Rule 3800 would lead to confusion and inconsistent compliance.

As such, we propose to apply the concept of "outside holding" across investment dealers and mutual fund dealers. This means a mutual fund dealer has recordkeeping and reporting obligations for client holdings under their control and outside their control (i.e. book-entry client name assets) where the dealer is listed as the "dealer of record" in the issuer's books or receives compensation. We believe this to be reflective of the current practice in the mutual fund dealer space, regardless of terminology.

2.6.3 Recordkeeping requirements *(DC Rule 3800, Part A)*

Both the IDPC Rules and the MFD Rules set out common requirements around the principles and general standards of recordkeeping, which are substantially aligned. They also set out common requirements around the "minimum mandatory records" and "specific records" that Dealers need to maintain to ensure recordkeeping compliance, although the IDPC Rules are more extensive when compared to the MFD Rules.

We propose to consolidate the common generic recordkeeping requirements into a principles-based approach, in line with our overall approach to the proposed DC Rules. For specific records, we propose incorporating the more prescriptive requirements from both sets of existing rules, as clarity in regulatory expectation is particularly valued in recordkeeping. By doing so, we do not believe to have introduced any material recordkeeping requirement on either Dealer category, which they do not already abide by within their business model.

2.6.3.1 General recordkeeping requirements *(DC Rule 3800, Part A.1.)*

In DC Rule 3800, Part A.1, we propose adopting the general recordkeeping requirements of the IDPC Rules, which are more principles based and aligned with National Instrument 31-103, with common applicability on all Dealers. We propose, however a few changes to the requirements regarding:

- minimum mandatory records ***(DC Rule section 3804)***, and

- internal controls and access to records ***(DC Rule section 3806)***,

to further align and clarify the Dealer recordkeeping responsibilities in conformity with existing rule expectations and industry practices.

2.6.3.2 Specific records requirements *(DC Rule 3800, Part A.2.)*

In DC Rule 3800, Part A.2., we propose harmonizing under the specific (transactional) records requirements of the IDPC Rules. These rules are more inclusive of Dealer models and provide greater prescriptive clarity. We also propose incorporating a few additions from the MFD Rules. More specifically we proposed the following to reconcile the differences between the two rulesets:

- adopt the IDPC Rule provision regarding the general ledger of accounts ***(DC Rule section 3811)***, which better captures substance over form compared to the corresponding MFD rule provision,
- consistent with the MFD Rules and dealer practices, clarify in the DC Rules the Dealer's obligation to keep:
  - records not only for dividends and interest received by the Dealer, but also those owned and paid to clients ***(DC Rule section 3813)***, and
  - evidence of having informed the client of fees and charges, ***(DC Rule section 3816)***
- extend the applicability of the prescriptive provisions of Part A.2, including DC Rule sections 3813, 3814 and 3821, to mutual fund dealers, relative to their business model.

2.6.4 Client reporting requirements *(DC Rule 3800, Part B)*

Both the IDPC Rules and the MFD Rules set out common requirements for Dealers to provide clients with prompt trade confirmations, regular transaction and holding statements, as well as annual reports detailing the client's investments performance and fees and charges paid. These requirements further delineate the reporting triggers, frequency of reporting, content of reporting, the format and delivery of reporting, as well as any reporting exemptions. Both rulesets are largely aligned in this area, due to the Client Relationship Model initiatives that predate this consolidation. However, there are legacy differences and drafting variations in the common requirements of both rulesets, which, if retained, could lead to inconsistent practices.

We propose aligning the client reporting requirements common to both Dealer categories, with the exceptions discussed in section 2.6.4.2 and 2.6.4.8 of this Bulletin. We generally adopt the IDPC Rules requirements, which are more inclusive of the spectrum of Dealer activities and embody a higher client protection standard, with modifications to incorporate elements from the MFD Rules. Where justified, we also extend the rule carve-outs available to one Dealer category to the other, thereby leveling the playing field. We believe our proposed approach achieves

requirements that are uniform, efficient and inclusive of the Dealer models and practices, while maintaining client protection and adherence to securities laws.

2.6.4.1. General information *(DC Rule section 3850)*

We propose introducing a new provision to set out the general information that a Dealer must include in the statements and reports to clients. In this new provision, we incorporated the explicit requirements in the MFD Rule 5.3.2 and existing Dealer practices.

2.6.4.2 Client account statements and outside holding reports *(DC Rule sections 3851 and 3852]*

Both the IDPC and the MFD Rules require a Dealer to provide frequent information to clients of transactions and other activity in the client's account, as well as information on the client's positions (either under Dealer control or outside holdings, such as book entry client name securities). While there is largely rule alignment in this area, there are a few substantive and operational differences to address. We propose reconciling such differences by adopting the IDPC Rule requirements with the following modifications and clarifications:

- **Reporting obligation**: Dealers must provide clients with:
  - an account statement of client account activity and client positions under Dealer control ***(DC Rule section 3851)***, and
  - a report of client's outside holdings. ***(DC Rule section 3852)***

  We clarify that the Dealer has the flexibility to prepare and deliver these statements and reports to clients either:

  - as separate documents, or
  - combined (but not consolidated) in one statement, provided this format does not mislead a reasonable client regarding client positions under Dealer control and outside of Dealer control, their location, and any applicable investor protection coverage, or lack thereof.

  We also reiterate that such statements/reports must be prepared on an account basis. Any consolidation of information for client positions under Dealer control and outside holdings, or for more than one client's account, is only allowed as a supplement to the separate or combined delivery. ***(DC Rule subsection 3857(3))***

  This proposal seeks to address the current differences in the operational rules and practices of our Dealers. At present the IDPC Rules require the account statement and outside holding report to be prepared and

delivered separately,[20] to prevent consolidation practices and mitigate client confusion. In contrast, the MFD Rules allow combining information in one account statement,[21] without any emphasis on the distinction between client holdings or the consolidation prohibition. While the provisions of the former overfocus on form, the provision of the latter may enable misleading consolidation practices.

Our proposal offers operational compliance flexibility in consideration of current Dealer operations without compromising the client's interest. While mutual fund dealers who operate with both nominee and client name holdings still need to review their back-office systems for needed adjustments, we anticipate any needed adjustments will not amount to major system changes.

- **Reporting frequency:** Investment dealers will continue to be subject to the daily, monthly and quarterly reporting requirements, under the DC Rules. Similarly, we propose upholding mutual fund dealers, who offer margin accounts, to the same monthly and quarterly reporting requirements as investment dealers ***(DC Rule subsections 3851(2)***. Similarly, we propose upholding mutual fund dealers, who offer margin accounts, to the same monthly and quarterly reporting requirements as investment dealers. ***(DC Rule subsections 3851(2))***

  In contrast, mutual fund dealers, who do not offer margin accounts, will continue to be subject to the quarterly reporting requirement only **(*DC Rule subsections 3851(3) and subsection 3852(1)***). We determined to maintain the status quo for this dealer category for now, considering the significant system changes needed to switch to monthly reporting and the existing carve-out from the securities laws.[22] Such exemption from the monthly reporting requirement is limited to the current mutual fund dealer business model and does not extend automatically with the expansion of such model in other products and services in the future.

- **Content of reporting:** Dealers must provide clients with:
  - the opening and closing cash balance in the client account **(*DC Rule clause 3851(4)(i)*)**. This is an existing requirement for Investment Dealers, whereas Mutual Fund Dealers will have to ensure they are disclosing the opening in addition to the closing cash balance, if they are not already doing so.
  - transaction information ***(DC Rule clause 3851(4)(ii))***. This is an existing requirement for Mutual Fund Dealers, whereas it may be an

[20] IDPC Rule sections 3808 and 3809. See also CIRO guidance GN-3800-21-004, *Consolidated statements*.
[21] MFD Rule sections 5.3.1 and 5.3.2.
[22] NI 31-103, section 14.14(2.1.)

enhanced requirement for those Investment Dealers who need to adjust their transaction disclosures to conform with the required transaction details.

- the total market value of all cash and investment positions in the client account with the Dealer (i.e. positions in Dealer control), and the total market value of all outside holding positions, at the beginning and the end of the reporting period ***(DC Rule clauses 3851(4)(vi) and 3852(2)(v))***. This is an existing requirement for Mutual Fund Dealers, whereas Investment Dealers will have to ensure they are disclosing the total values at the start in addition to the end of reporting period, if they are not already doing so.
- the *position cost* for each product position presented "on an average cost per unit, or share basis, or on an aggregate basis" **(*DC Rule paragraph 3851(4)(v)(a)(I)* and *subclause 3852(2)(iii)(a))***. We propose to adopt the MFD Rule which is clearer than the corresponding language in the IDPC Rules and more aligned with National Instrument 31-103.
- the applicable Investor Protection Fund coverage, or any other investor protection coverage approved or recognized under securities laws, and where applicable, the lack of such coverage with regards to client holdings ***(DC Rule clause 3851(4)(viii) and subsection 3852(4))***. While both Dealer categories already report the IPF coverage, they need to assess whether enhancements to their current disclosures are needed to conform with the proposal (e.g. whether they are already disclosing any other applicable investor protection coverage beyond the IPF, or whether they are adequately disclosing the applicable coverage (or lack of) in connection to the eligible accounts/assets and the coverage policy).

We also propose removing the requirement, currently unique to the IDPC Rules, for a Dealer to report non-arm's length transactions in the account statements to clients, therefore aligning with the MFD Rules and National Instrument 31-103. [23] This conflict of interest provision predates the Client Focused Reforms, which enhanced the Dealer responsibility of not only disclosing any material conflicts of interests to the client in a timely manner, but also addressing such a conflict in the client's best interest. [24] Furthermore, a Dealer continues to be subject to the existing requirement for disclosing any non-arm's length transactions in both the relationship

[23] IDPC Rule subsection 3808(9). In contrast, there is no such a disclosure requirement for account statements in the MFD Rules and NI 31-103.

[24] IDPC Rule 3100, Part B and MFD Rule section 2.1.4., which we bring forward into DC Rule 3100, Part B.

disclosure package[25] and the trade confirmation.[26] We believe that the enhanced conflicts of interest requirements combined with the Dealer responsibility for disclosing the conflicts of interest in a timely manner, including at account opening and transaction execution, offers a more balanced, yet impactful, approach for addressing conflicts of interest.

- **Reporting carve-outs:** We propose extending to mutual fund dealers the institutional client reporting carve-outs currently available to investment dealers, whereby a dealer is required to provide only the retail client with the following:
  - quarterly position cost information ***(DC Rule clauses 3851(4)(v) and 3851(4)(vii))***, and
  - an outside holding report. ***(DC Rule subsection 3852(1))***

  We also propose codifying the exemption from the requirement to provide a client with a monthly account statement, which would otherwise be triggered by automatic plan transaction(s) ***(DC Rule clause 3851(2)(ii))***,[27] consistent with National Instrument 31-103.[28]

2.6.4.3 Performance report *(DC Rule section 3853)*

Both the IDPC Rules and the MFD Rules require a Dealer to provide clients with an annual report of their investment performance on an account basis. The two rulesets similarly outline the data elements of the performance reports, and their delivery format (including when to combine or consolidate performance information), with a few exceptions. We propose reconciling these differences between the rules by adopting the IDPC Rule requirements, with the following modifications and clarifications:

- **Reporting obligation**: Under MFD Rule 5.3.4, Dealers can send the first performance report within 24 months after the first client trade or transfer, whereas under the IDPC Rules, Dealers must send the first performance report within 24 months from when the client account is open. We propose adopting the MFD Rule requirement, which is equivalent to the corresponding requirement under National Instrument 31-103 and has minimal impact on Dealers.
- **Content of reporting:** In *DC Rule subclause 3853(2)(iv)(a)* we propose adopting the IDPC Rules formula to calculate the "total market value change since account opening", because it offers a simpler approach when compared to the two formulas under the MFD Rules. Mutual fund

[25] DC Rule section 3216.
[26] DC Rule subsection 3855(2)(viii).
[27] See the proposed definition of "automatic plan transactions" in DC Rule section 3802.
[28] NI 31-103, section. 14.14(2).

dealers must evaluate whether system changes are needed to conform with this proposal.

We also propose adding a provision clarifying that where a Dealer provides clients with a performance report for a period shorter than 12 months, the disclosed information must not be calculated on an annualized basis ***(DC Rule subsection 3853(11))***. This requirement is currently stipulated in the MFD Rules and National Instrument 31-103, but not the IDPC Rules. Apart from enhancing rule clarity and preventing misleading disclosures, we believe this proposal does not introduce any new requirement for Investment Dealers.

- **Reporting carve-outs:** We propose extending to mutual fund dealers the institutional client reporting carve-out currently available to investment dealers, whereby a dealer is required to provide a performance report to retail clients only. **(*DC Rule subsection 3853(1))***

2.6.4.4. Report on fees/charges *(DC Rule section 3854)*

Both the IDPC Rules and the MFD Rules require Dealers to provide clients with an annual report detailing the fees and charges paid by the client, either directly or indirectly, on an account basis. The fee and charge reporting requirements of both rulesets are already largely aligned, including with regards to combining or consolidating the fee information. Similarly, the recent proposed changes to both rules under the parallel Total Cost Reporting Enhancements are significantly aligned. These proposals are shown in our rule proposal (in grey boxes) for context only, as we are consulting on those changes separately.

We propose reconciling the few existing differences between the rules by adopting the IDPC Rule requirements, with the following modifications and clarifications:

- **Reporting obligation:** We propose to clarify that Dealers may exclude the required fees and charges information from the report only if reliable data cannot be obtained ***(DC Rule subsection 3854(14))***. This is a change from the corresponding MFD Rule provision, whereby a Mutual Fund Dealer has the option of excluding from the report payments for investments other than securities.[29] We believe the MFD Rule approach can lead to arbitrary practices and even misleading reports, especially when information on such products is included in the performance report but excluded in the fee charge report. Because the MFDA has interpreted the concept of "securities" broadly, we anticipate the impact of this proposed provision on Mutual Fund Dealers to be limited.

[29] MFD Rule 5.3.3(5).

- **Reporting carve-outs:** We propose extending to mutual fund dealers the institutional client reporting carve-out currently available to investment dealers, whereby a dealer is required to provide a fee/charge report to retail clients only. **(*DC Rule subsection 3854(1)*)**

2.6.4.5. Transaction confirmations *(DC Rule 3855)*

Both the IDPC Rules and MFD Rules require a Dealer to send prompt trade confirmation to clients; they also outline the information that must be included in the confirmation, its delivery and any applicable exemptions. While such requirements are largely similar, there are a few differences in common requirements which we propose to harmonize. We propose adopting the IDPC Rule with the following modifications and clarifications:

- **Confirmation obligation *(DC Rule subsection 3855(1))*:** Dealers must provide clients with a written confirmation of transactions in "investment products" and other property for the client's account. We adopt a principles-based language, to better capture the broad spectrum of Dealer activities for which a confirmation must be issued.
- **Confirmation content *(DC Rule subsection 3855(2))*:** We propose reconciling the current differences in both rulesets with regards to the content of the trade confirmation, by:
  - clarifying the minimum information that a Dealer must include in the trade confirmation, ***(DC Rule clause 3855(2)(i))***
  - adopting the IDPC requirements for various product-specific confirmation requirements which are more inclusive of the broader spectrum of Dealer products. ***(DC Rule clauses 3855(2)(ii) to (vii))***

  A common requirement of both rulebooks is for the Dealer to disclose in the confirmation whether it is acting as a principal or agent in the transaction. However, there are diverging interpretations in practice between the two rulesets. Under the IDPC Rules, a dealer is acting as a principal when transacting with the client from its own inventory, whereas under the MFD Rules this concept is applied to capture the dealer acting as the "principal distributor" of mutual funds.[30] We propose not maintaining the current differences in interpretation, as it would lead to confusion and inconsistent outcomes. For the purposes of the disclosure under *DC Rule* subclause *3855(2)(i)(c)*, we interpret the term "principal" to capture situations where the Dealer is transacting with the client from its own inventory. In contrast when a Dealer is transacting as a "principal distributor" with the client, we interpret this as acting in an agency capacity. Mutual fund dealers that transact as "principal

[30] Such concept is defined in National Instrument 81-102 *Investment Funds.*

distributors" will need to evaluate their systems for necessary adjustments to ensure that this capacity is disclosed in the trade confirmation as "principal distributor" or "agent" but not as "principal".

- **Confirmation carve-outs *(DC Rule subsections 3855(3) and 3855(4))*:** We propose adopting the exiting confirmation carve-outs of both rulesets and align - where applicable - for both investment dealers and mutual fund dealers so as to level the playing field, including but not limited to the exemption from providing:
  - a trade confirmation for transactions in a security of a mutual fund where the confirmation is sent by the manager of the mutual fund,
  - a trade confirmation for automatic plan transactions, except for the confirmation for the initial transaction,
  - the required information regarding non-arm's length transactions in investment products of an issuer, whose name is sufficiently similar to that of a Dealer to indicate a related or affiliated relationship. In addition to harmonizing this exemption, we also propose applying it not only for mutual fund securities (current application), but also for other investment products on the same grounds.

2.6.4.6. Option of earlier date *(DC Rule section 3856)*

We propose adopting the IDPC Rule provision, which emphasizes that the option for using earlier data must be exercised for all clients equally, consistent with the fair dealing standards of both rules.

2.6.4.7 Delivery of documents to clients *(DC Rule section 3857)*

Both the IDPC Rules and the MFD Rules set out requirements for how a Dealer must deliver the required confirmations, reports and other documents to clients. However, there are some variations between the two rulesets, which we propose reconciling by aligning with the IDPC Rule provisions, with the following changes for added operational flexibility and clarity. Under the proposed DC Rules, a Dealer has the option of delivering to clients:

- the outside holdings report separately or combined with the account statement, to the extent it does not result in misleading reports for the client. We also clarify that consolidation is only permitted as a supplement of the separate or combined reports (***DC Rule subsections 3857(2)* and *3857(3)***), and
- the performance and fee/charge report either separately from the account statement for the monthly or quarterly period ending on the same date, however within a 10-day period, or combined with such statement (***DC Rule subsection 3857(4)***). This enhanced clarification is

consistent with current Dealer practices, as well as National Instrument 31-103, and does not introduce any new requirement.

In addition to the above, we also propose introducing the requirement for dealers to prepare and deliver the documents required under Rule 3800 to clients in electronic format (e-delivery), in accordance with applicable laws, unless the client requests to receive such document in paper format (***DC Rule subsections 3857(1)***). In essence, the proposed change makes e-delivery the default format of communications with clients, with the client having the right to opt for paper delivery. It reflects the growing prominence of electronic communication in the financial and other sectors in Canada, which was accelerated by the COVID-19 pandemic, and aims to align CIRO rules with evolving global practices, regulatory standards and technological advancements. We anticipate such a change to have an overall positive impact in the long term, although in the short-term a subset of dealers may incur costs associated with the transition to the default e-delivery format.

2.6.4.8 Exempt Market Dealers and Scholarship Plan Dealers *(DC Rule section 3860)*

Mutual fund dealers, also registered as either exempt market dealers or scholarship plan dealers, are subject to some of the reporting requirements of National Instrument 31-103 in addition to CIRO requirements. As such we propose to adopt MFD Rule 5.3.6 which sets out the additional reporting responsibility for those mutual fund dealers.

2.7 General dealer member financial standards – minimum capital, early warning, financial reports and auditors *(DC Rule 4100)*

In this section of the Bulletin, we discuss the proposed amendments to requirements relating to:

- minimum capital levels and related requirements,
- early warning tests and related requirements,
- regulatory financial report filing requirements,
- appointment of auditors and audit requirements, and
- Form 1 and capital formula,

that may represent a significant format or substantive change to either the IDPC Rules or the MFD Rules.

The IDPC Rules in these areas impose requirements and actions to be taken by the CFO or UDP, whereas in the MFD Rules these requirements were drafted as actions to be taken by the Dealer Member or senior management. We have adopted the IDPC Rule drafting to impose actions to be taken by the CFO or UDP to align with the proposed Phase 4 DC Rules that require mutual fund dealers to have a qualified CFO and UDP.

2.7.1 Minimum capital levels and related requirements

Both the IDPC Rules and the MFD Rules require a dealer to maintain a minimum amount of capital in the calculation of risk adjusted capital (**RAC**). The minimum amount for a mutual fund dealer is based on the Dealer's level. The Dealer's level is defined based on whether they hold client cash or securities. We recognize that mutual fund dealers that do not hold client cash or securities have inherently lower risk than dealers that hold client assets. We propose to maintain both the IDPC and MFD minimum capital requirements. We bring forward the mutual fund dealer levels and associated minimum capital requirements in the proposed DC rules and Form 1. The IDPC minimum capital requirements are currently only prescribed in the notes and instructions to Statement B of Form 1. For consistency, these requirements will also be included in the proposed DC Rules in addition to Form 1. ***(DC Rule section 4111)***

IDPC Rules require investment dealers to notify CIRO if RAC falls below zero or if any of the early warning tests are triggered. MFD Rules only require notification to CIRO if RAC is below zero. We propose aligning the requirements to apply for both Dealer types by adopting the IDPC Rule requirements in the proposed consolidated rules. ***(DC Rules section 4113)***

Under the existing IDPC Rules, investment dealers are required to calculate their RAC and complete the early warning tests on a weekly basis at a minimum. Under the existing MFD Rules, mutual fund dealers are required to calculate RAC on a monthly basis at a minimum. As explained in section 2.7.2 of this Bulletin, we propose that Level 4 mutual fund dealers be subject to the same early warning tests as investment dealers. To align with the early warning requirements, we also propose that Level 4 mutual fund dealers calculate RAC and complete the early warning tests on the same frequency as investment dealers. We are also proposing to increase the frequency of the RAC calculations for Level 1 to 3 mutual fund dealers from monthly to twice monthly and we propose that early warning tests be completed on the same frequency. The requirement to complete the early warning tests in addition to the RAC calculation will be a new requirement for mutual fund dealers. We recognize the business activity of a Level 1 to 3 mutual fund dealer does not generate significant changes in profits and capital from week to week to justify weekly financial solvency calculations, however neither are monthly calculations sufficient to identify any potential risk adjusted capital deficiencies sufficiently in advance of their occurrence. ***(DC Rules section 4115)***

We propose adopting the following IDPC Rule provisions, in the absence of equivalent provisions in the MFD Rules, with applicability on both mutual fund dealers and investment dealers:

- option for well capitalized Dealer Members to apply more stringent capital calculations, ***(DC Rule section 4119)***
- requirement that guarantees be a fixed or determinable value. ***(DC Rule section 4120)***

2.7.2 Early warning tests and related requirements

The early warning tests and levels differ significantly between the MFD and IDPC Rules. The IDPC Rules provide for several early warning tests and two early warning levels, whereas the MFD rules provide for fewer and simpler early warning tests and one early warning level. We propose adopting a hybrid approach given the difference in risks associated with dealers that hold or control nominee name client assets and those that only engage in book-based client name transactions.

We propose to:

- harmonize the early warning tests and requirements for investment dealers and level 4 mutual fund dealers,
- maintain the existing MFD early warning tests and introduce an additional profitability test for Level 1 to 3 mutual fund dealers, and
- extend the ability for mutual fund dealers to request a hearing panel review for early warning test violation-related restrictions imposed by CIRO.

2.7.2.1 Early warning tests and levels

We propose to retain the IDPC Form 1 early warning framework for investment dealers and bring Level 4 mutual fund dealers to the same standards. We propose aligning the early warning tests, early warning levels and sanctions for both these dealer types since they hold client securities in nominee name which results in a similar risk to clients in the event of insolvency. ***(DC Rule subsection 4132(1))***

As a result of this higher standard for Level 4 mutual fund dealers, they will be subject to additional early warning tests and implications if an early warning level 2 designation is triggered. These additional implications include required actions such as filing weekly capital reports and early filing of the monthly financial report.

We propose to retain the MFD Form 1 early warning framework for Level 1-3 mutual fund dealers, since they have a simpler business and do not hold or control client securities. We also propose to enhance the framework by adding a 6-month profitability test for these mutual fund dealers ***(DC Rule subsection 4132(2))***. The existing three-month profitability test identifies mutual fund dealers that may be close to triggering a RAC deficiency, but such a test alone does not identify longer term losses that may be steadily eroding RAC. The additional 6-month profitability test would enable CIRO to identify profitability concerns and allow early warning sanctions to be imposed for those Level 1 to 3 mutual fund dealers with a longer and steady history of losses. Other than the new 6-month profitability test and the increased frequency of calculating early warning tests, there are no other new requirements or implications for Level 1-3 mutual fund dealers related to early warning.

Since we are proposing a different early warning testing framework for Level 1 to 3 mutual fund dealers versus other dealer types, we have proposed to include separate early warning schedules in the Form 1 as described in section 2.11.4.3 of this Bulletin.

2.7.2.2 Early warning related requirements

Under existing IDPC and MFD Rules, early warning implications for the dealer and the actions the dealer must take are generally similar for both investment dealers in early warning level 1 and mutual fund dealers in early warning. We are proposing alignment, whereby level 1 to 3 mutual fund dealer early warning tests will be categorized as early warning level 1.

Under the IDPC Rules there are additional actions an investment dealer must take if they have triggered early warning level 2 such as additional filings and a meeting with CIRO. We are not proposing to impose these additional required actions on Level 1-3 mutual fund dealers if they trigger early warning. Rather, we are proposing to adopt these IDPC requirements only for investment dealers and Level 4 mutual fund dealers, in line with the adopted approach for the early warning tests.

2.7.2.3 Reimbursing CIRO for costs

The IDPC Rules allow CIRO to charge a Dealer for costs associated with the administration of early warning situations. The MFD Rules on the other hand are broader and allow CIRO to impose an assessment if the Dealer's financial condition or business issues demanded excessive regulatory attention. We are proposing to adopt the IDPC Rule approach. ***(DC Rule subsection 4133(1) – Reimbursing the Corporation for costs)***

2.7.2.4 Additional restrictions and hearing panel review

Under both rules CIRO can impose sanctions on Dealers, such as prohibitions or restrictions for new branches, hiring or account opening. However, investment dealers, unlike mutual fund dealers, may request a hearing panel review of these CIRO-imposed sanctions. We propose bringing forward CIRO's authority to impose sanctions and the Dealer's right to request a review of such sanctions, with applicability for both investment dealers and mutual fund dealers alike. By offering mutual fund dealers the right for review, we enhance process fairness and level the playing field. ***(DC Rule section 4135 and 4136)***

2.7.3 Regulatory financial report filing requirements

We propose to maintain the existing due dates for financial filings for mutual fund dealers and investment fund dealers, except where a mutual fund dealer chooses to offer margin lending. The deadline for filing the annual audited Form 1 for investment dealers is 7 weeks after year-end whereas the deadline for mutual fund dealers is 90 days after year-end. We have aligned the filing deadline for mutual

fund dealers that choose to offer margin lending with the existing 7 week due date for investment dealers. We are not proposing to shorten the 90 day due date for mutual fund dealers that do not choose to offer margin lending, because smaller dealers, such as Level 1-3 dealers may have challenges obtaining audit services. This approach is consistent with other jurisdictions that allow longer filing periods for members with simple business models. We also propose bringing forward the deadline for filing the monthly financial reports and the Dealer ability to request an extension, subject to a late fee, which are similar between both rules. ***(DC Rule sections 4151, 4152 and 4153)***

2.7.4 Appointment of auditors and audit requirements

The most significant difference in audit requirements between the IDPC Rules and MFD Rules is the criteria for qualifying as an auditor to perform the audit of the Dealer Member's year-end regulatory financial report. Under the IDPC Rules, the auditor must be on the approved list of panel auditors. The criteria for this list are not prescriptively outlined in the IDPC Rules but the criteria is set by CIRO and published on our website. The existing IDPC criteria for qualification of a panel auditor is more stringent than the existing MFD criteria. For example, the MFD Rules require that the audit partner acknowledge they have familiarity with the MFD rules whereas the IDPC criteria requires the audit partner to have five years experience and attend the in-depth brokers and investment dealers course at CPA Canada. Given that we are proposing one Form 1, we believe all auditors performing an audit of the Form 1 should have the same educational standards and meet the same approval criteria. We propose to adopt the IDPC Rule requirements and related auditor criteria which will continue to allow CIRO to have the flexibility to update the criteria for approving auditors for both mutual fund and investment dealers. ***(DC Rule section 4171)***

By adopting the IDPC criteria for auditors of all Dealer Members, the mutual fund dealer auditors may need to enhance their knowledge or mutual fund dealers may need to switch to an auditor that meets the required criteria. Based on our analysis there are approximately 24 auditors of mutual fund dealers that are not currently on the IDPC panel auditor list and therefore will need to seek panel auditor approval. The majority of these auditors perform audits solely for level 1 to 3 mutual fund dealers. In the questions section we have requested commenters to provide feedback on whether a transitionary period is needed for mutual fund dealer auditors to upgrade their education and proficiencies.

We propose to further harmonize the requirements for auditors by:

- adopting the MFD Rule requirement for informing CIRO of any changes in auditors or audit partners ***(DC Rule subsection 4172(2))***,
- aligning the prescribed audit procedures for confirmation, reconciliations and other tests ***(DC Rule sections 4173 to 4192)***,

- adopting existing filing requirements for the agreed-upon procedures report and clarifying the applicable report for mutual fund dealers that offer margin lending ***(DC Rule section 4190)***, and
- aligning the audit workpaper record retention requirements with the general Dealer Member record retention requirements. ***(DC Rule section 4191)***

As a result of these harmonizations to the audit requirements, investment dealers will be subject to a new requirement to notify CIRO of any changes in their auditor. Also, the investment dealer's auditor will be required to retain workpapers for 7 years instead of 6 years. The mutual fund dealer's auditors will benefit from more flexibility in the audit confirmation procedures, which provide the auditor with an option, rather than a mandatory requirement, to send second requests for confirmations.

2.8 General dealer member financial standards - disclosure, internal controls, calculations of prices and professional opinions (*DC Rule 4200*)

In this section of the Bulletin, we discuss the proposed amendments to requirements relating to general dealer member financial standards that may present a significant format or substantive change to either the IDPC Rules or the MFD Rules.

2.8.1 Financial disclosure to clients (*DC Rule 4202-4209*)

Under the IDPC Rules, an investment dealer must provide a summary statement of its financial position and a list of current Executives and Directors, to a client upon request. Dealers are also required to notify clients through client disclosures that this information is available upon request. There are no equivalent requirements in the MFD Rules for mutual fund dealers to provide this information to clients.

We propose to adopt these requirements for both investment dealers and mutual fund dealers. We believe that these disclosures are important for clients who wish to perform this due diligence on their Dealer Member.

To align with the separate financial report filing deadlines for investment dealers and mutual fund dealers, as described in section 2.7.3 of this Bulletin, we propose mutual fund dealers prepare the summary statement of financial position within 120 days of their fiscal year-end while we maintain the 75 day requirement for investment dealers. The summary statement can be generated within the electronic regulatory filing system using the Form 1 filing information, which may reduce the burden of this new requirement for mutual fund dealers.

2.8.2 Pricing internal control requirements (*DC Rule 4240-4244*)

We propose to adopt the IDPC rules for pricing internal control requirements. This includes requirements to ensure consistent and accurate pricing of investment products and verification of the Dealer Member's pricing sources against independent sources.

The pricing internal control requirements will be new requirements for mutual fund dealers as there are no corresponding requirements under the MFD Rules. Mutual

fund dealers may need to enhance their policies and procedures related to pricing to support these new requirements.

2.9 Client asset use and custody (*DC Rule 4300, 4400*)

In this section of the Bulletin, we discuss the proposed amendments to requirements relating to:

- segregation and related internal controls
- custody and related internal controls
- client free credit balances
- safekeeping, safeguarding and related internal controls
- insurance

that may present a significant format or substantive change to either the IDPC Rules or the MFD Rules.

2.9.1 Segregation and related internal controls

The segregation and related internal controls for both dealer types are generally similar. However, the IDPC Rule segregation requirements are more prescriptive than the MFD Rule requirements given the additional activities undertaken by an investment dealer, including margin lending.

We propose to adopt a modified version of the IDPC Rule segregation requirements that integrates and maintains the core requirements applicable to the investment dealer margin lending model and the mutual fund dealer full segregation model. References to "Mutual Fund Dealer Members" are inserted where the segregation requirements are specific to the mutual fund dealer business model that does not permit margin lending.

For mutual fund dealers that do not offer margin accounts and margin lending to clients, we preserve the core MFD Rule segregation requirements regarding:

- the frequency and review of the bulk segregation calculation (ensure all client investment products are segregated) ***(DC Rule subsection 4319(3))***,
- the report of items requiring segregation (minimum monthly) ***(DC Rule subsection 4329(2))***, and
- the supervisory review of the segregation report (monthly). ***(DC Rule subsection 4332(2))***

We codified under DC Rule subsection 4319(3) that the determination of the investment products required to be segregated is done daily, which we believe is the current practice.

These changes are meant to integrate the investment dealer and mutual fund dealer segregation models into the DC Rules and are not intended to introduce new requirements for the respective business models in their current form.

2.9.1.1 Investment products requiring segregation

The protection of assets extends to investment products with similar properties that require segregation, custody, safekeeping and safeguarding. The current IDPC and MFD Rules specifically reference segregation requirements for securities, precious metals bullion and other property. We propose to introduce the term "investment product" into the segregation requirements by qualifying that the types of investment products requiring segregation are securities, precious metals bullion and other like assets. Derivatives would not typically be considered a "like asset" requiring segregation.

This does not represent a change from current practice, but clarifies that the scope of the segregation requirements extends beyond securities and precious metals bullion. Following this approach, we would not need to amend the rules in every instance where a new product, similar to a security or commodity, may be recognized by the CIRO Board as an investment product.

2.9.2 Custody and related internal controls

The custody and related internal controls for both dealer types are generally similar, including equivalent acceptable securities location qualification requirements for mutual funds.

We propose to adopt the IDPC Rules' custody and related internal controls, as discussed in section 2.11.3.2 of this Bulletin, which describe potential impacts on mutual fund dealers resulting from acceptable securities location net worth qualification requirements and other custody related requirements that, in the latter case, may positively impact risk adjusted capital.

Another potential impact to mutual fund dealers may result from differences in the requirements for custody agreements since the IDPC Rules require the inclusion of an indemnification clause within the agreement. This requirement is not in the MFD Rules, but the standard custodial agreement prescribed by the MFDA includes an indemnity clause. We expect adopting this requirement will not result in re-papering existing custody agreements, where a standard custodial agreement was used.

By adopting the IDPC requirements for the custody agreements, the mutual funds dealers would also be subject to the requirements for global and foreign locations if they have any foreign locations.

In summary, to the extent there is any net impact to mutual fund dealers, we expect it to be positive. In particular, mutual fund dealers may benefit from reduced margin requirements in scenarios where:

- investment products are custodied at an acceptable securities location without a custodial agreement ***(DC Rule section 4366)***, and
- mutual funds or evidences of deposit, subject to certain conditions, are not reconciled monthly against the custodian's records. ***(DC Rule section 4367)***

2.9.3 Client free credit balances

We propose to adopt a modified version of the IDPC Rules' client free credit balance requirements that integrates and maintains the core requirements applicable to the IDPC allowable use model and the MFD full cash segregation model. We also propose to allow a Level 4 mutual fund dealer to use client free credit balances in its business, subject to meeting the same client free credit balance and financial solvency requirements as an investment dealer, including:

- $250,000 minimum capital requirement ***(DC Rule clause 4382(2)(i))***, and
- client free credit balance usage limits and excess free credit balance segregation requirements ***(DC Rule clause 4382(2)(ii))***

Both the MFD Rules and IDPC Rules require client cash to be held in an acceptable institution. Under the MFD Rules, an acceptable institution has no minimum net worth threshold requirements and is limited to Canadian financial institutions. Although not explicitly stated in the IDPC Rules, investment dealers that segregate client cash in trust for registered accounts or free credit cash segregation are expected to hold such cash at a Canadian financial institution. This requirement is implied in the IDPC Form 1 Statement A Notes and Instructions that require trust accounts to qualify for Canadian Deposit Insurance Corporation (CDIC) coverage. We propose to adopt the IDPC acceptable institution definition as described in section 2.11.3.1 of this Bulletin, and to codify for all Dealers that client cash held in trust must be held at a Canadian financial institution meeting the acceptable institution definition.

Under the MFD Rules, client cash must be segregated in a trust account at a financial institution and cannot be invested in securities. The IDPC Rules allow the cash that must be segregated to be invested in short term securities with maturity of one year or less such as bonds, T-bills and Canadian bank paper. We propose to maintain the MFD Rule requirement for mutual fund dealers that do not use client free credit balances within their business, who will be required to hold the segregated cash in trust bank accounts.

An investment dealer that uses the free credit client cash in their operations must disclose this fact on the client statement under IDPC Rules which we propose to adopt, but there are no obligations for the dealer to pay interest or provide notice before changing the interest rate. We propose to harmonize the requirements regarding the payment of interest on client cash by withdrawing MFD Rule 3.3.2(e), which requires disclosure whether interest will be paid, the rate, and 60 days written notice prior to any rate revision. While this proposed harmonization will eliminate a required client disclosure, the 60 day prior written notice requirement may have disincentivized competitive rate setting and provides challenges where rates vary based on rates set by Bank of Canada. Investment dealers do not have such a requirement and may set interest rate payments, earning a spread, in response to

market conditions in a timely manner. We believe any negative client impacts will be mitigated by allowing timelier rate setting in response to market conditions.

New requirements that may impact Investment Dealers are detailed below and relate to:

- client free credit segregation deficiencies, and
- notice to financial institutions regarding designated trust accounts.

2.9.3.1 Client free credit segregation deficiency capital charge

The IDPC Rules do not require capital charges for client free credit segregation deficiencies and allow investment dealers up to five business days to correct any deficiency. MFD Rule 3.3.2(c) requires immediate action to correct a cash segregation deficiency and requires a capital charge for any unresolved deficiency amount.

For all Dealers, we propose to adopt a capital charge for any client free credit segregation deficiency that exists for more than one business day ***(DC Rule subsection 4386(3))***. We added a reporting line on Statement B of the DC Form 1 for dealers to report this charge in the risk adjusted capital calculation.

2.9.3.2 Notice to institution – designated trust account

For all Dealers, we propose to adopt the written designated trust notification requirements set out in MFD Rule 3.3.2. ***(DC Rule section 4387)***

2.9.4 Safekeeping, safeguarding and related internal controls

We propose to adopt the IDPC Rule safekeeping requirements. We extended the scope of the applicable investment products held for safekeeping to also include "other like assets". The MFD Rules do not include prescriptive safekeeping requirements.

The safeguarding requirements for both dealer types are generally similar with the scope of provisions differing according to business models. We propose to adopt a modified version of the IDPC Rule provisions relating to safeguarding assets. Where the current requirements reference securities and precious metals bullion, we extended the scope to include "other like assets".

In the case of access restrictions for the physical handing of assets ***(DC Rule section 4423)***, the current IDPC provisions only reference securities. We believe it is appropriate to extend these requirements to bearer assets such as precious metals bullion and other like assets.

These changes clarify the safeguarding requirements for assets other than cash. We do not anticipate that these changes will impose a burden on dealers according to their current scope of operations.

2.9.4.1 Safeguarding cash

We propose to adopt the MFD Rule provisions regarding the safeguarding of cash. MFD Rule 400, ICRS 4 includes safeguarding cash requirements not covered in the IDPC Rules, regarding

- general cash requirements (safeguarding of blank cheques ***(DC Rule subsection 4433(7))*** and limits on the number of authorized employees permitted to withdraw funds from bank accounts. ***(DC Rule subsection 4433 (11))***, and
- trust accounts for client funds. ***(DC Rule section 4434)***

We propose to adopt the general cash requirements for all dealers. For mutual fund dealers that do not use client free credit balances within their business only, we propose to adopt the MFD Rule trust account provisions regarding:

- recording and depositing of client cheques ***(DC Rule subsection 4434(1))***
- daily balancing of deposits ***(DC Rule subsection 4434(2))***, and
- segregation of interest received payable to clients. ***(DC Rule subsection 4434(3))***

We propose the MFD Rule trust account provision requiring a dealer that pays interest to clients to maintain adequate records of amounts owing and paid to each client (MFD Rule 400 - ICRS 4, Trust Account for Client Funds, 4) to be a general records requirement that should apply to all dealers. Accordingly, we have included the requirement to maintain records of interest owing and paid to the client. ***(DC Rule clause 3810(1)(ii)***

2.9.5 Insurance requirements

Under both MFD Rules and IDPC Rules, Dealer Members are required to have a minimum amount of insurance coverage against prescribed types of losses. The majority of the insurance requirements such as requirements for qualified insurance carriers, prescribed types of losses, policy riders, notifications to CIRO and global policies are the same or substantially similar between IDPC and MFD Rules. For these requirements, we propose to adopt the IDPC Rules which are drafted in plain language. ***(DC Rule sections 4452-4456, 4459-4468)***

Although the majority of the insurance requirements are the same there are differences between the rulesets for coverage requirements for certain dealer types and reporting requirements on claims and mail insurance.

2.9.5.1 Coverage requirements

The calculation for determining the minimum amount of insurance coverage differs between the MFD Rules and IDPC Rules. We are proposing to align portions of the calculation that are similar and blend or maintain other portions of the calculation to continue requiring that dealers holding client assets have more insurance coverage than those that do not hold client assets.

The base amount is a component of the calculation of the insurance coverage requirement. The definition of the base amount is similar under the MFD Rules and IDPC Rules and is determined as the greater of (i) the aggregate net equity of client assets held by the Dealer and (ii) the Dealer's total allowable assets. We clarified the language that describes how client net equity held by the Dealer is determined so both investment dealers and mutual fund dealers will continue to determine the client net assets in a similar manner to their existing process. ***(DC Rule section 4451)***

Level 1, 2 and 3 mutual fund dealers do not hold or control client securities. Type 1 and 2 investment dealer introducing brokers are not responsible for reporting client accounts or any associated individual position or concentration margin as the carrying broker takes responsibility for segregating and reporting client assets. As a result, these dealer types are subject to a modified insurance coverage calculation under both MFD Rules and IDPC Rules. We are proposing to maintain a modified insurance coverage calculation requirement for these dealer types, but we have proposed slight modifications to the components of the calculation to simplify and align the calculations. These proposed coverage calculations are also included in the insurance schedule of Form 1 where there are separate sections within the schedule for different dealer types.

For Level 1, 2 and 3 mutual fund dealers, we propose to remove the $50,000 per approved person portion of the calculation and set the minimum coverage amount at $200,000. There are approximately 3 mutual fund dealers that maintain insurance less than $200,000 which may need to update their insurance for this new requirement. We also propose to lower the base amount percentage from 1% to ½% to align with the base percentage applicable to Type 1 and 2 investment dealer introducing brokers. Although this approach raises the minimum coverage required, the amount of insurance coverage required for these dealers beyond $200,000 is expected to be minimal due to the change in base amount percentage and the minimal assets held by these dealers. For Type 1 and 2 investment dealer introducing brokers, we plan to keep the existing requirement for minimum insurance coverage at $200,000 for a Type 1 and $500,000 for a Type 2. ***(DC Rule section 4458)***

The insurance coverage requirements for Level 4 mutual fund dealers, Type 3 and 4 investment dealer introducing brokers and self-clearing investment dealers are generally the same under both rulesets and we propose to adopt the existing requirements for these dealer types. ***(DC Rule section 4457)***

The notes and instructions to Schedule 12 of the Form 1 also describe how the Dealer is expected to determine the net equity for each client and the

net value of assets where assets include cash, securities, precious metals bullion and other investment products.

2.9.5.2 Claim notification

We propose to adopt the IDPC Rule that requires claims be reported to CIRO within 2 business days. This is a new requirement for mutual fund dealers as there is no equivalent reporting requirement in the MFD Rules. ***(DC Rule section 4465)***

2.9.5.3 Mail Insurance

The IDPC Rules require an investment dealer to request an exemption from mail insurance if it does not use mail and wishes to exclude mail insurance from its insurance coverage. Under the MFD Rules, a mutual fund dealer is not required to request this exemption or inform CIRO. We propose a hybrid approach where the dealer is not required to maintain mail insurance, if it provides written notice to CIRO that it does not use mail. This approach will reduce the administrative burden of exemption requests for dealers and CIRO. ***(DC Rule section 4455)***

Although providing a notice to CIRO will be a new requirement for mutual fund dealers, we do not expect a significant additional burden. Approximately 7% of mutual fund dealers report not having mail insurance.

2.10 Financing arrangements (*DC Rule 4500, 4600*)

In this section of the Bulletin, we discuss the proposed amendments to requirements relating to:

- repurchase and reverse repurchase market trading practices
- cash and securities loan, repurchase and reverse repurchase agreement transactions

2.10.1 Repurchase and reverse repurchase market trading practices

IDPC Rule 4500 sets out a standard set of trading practices for repurchase agreements and reverse repurchase agreements. There are no corresponding provisions in the MFD Rules, because mutual fund dealers do not typically participate in repurchase or reverse repurchase market trading. We are proposing to adopt IDPC Rule 4500 into the DC Rules without any modifications.

We did not limit DC Rule 4500 to investment dealers only because we believe these requirements should apply to any Dealer Member that may engage in repurchase or reverse repurchase trading. ***(DC Rule 4500)***

2.10.2 Cash and securities loan, repurchase and reverse repurchase agreement transactions

IDPC Rule 4600 sets out requirements for Investment Dealers that engage in securities loans, repurchase and reverse repurchase transactions. There are no corresponding provisions in the MFD Rules. IDPC Rule 4600 is currently under review

as part of a separate project entitled proposed amendments regarding fully paid securities lending and financing arrangements (**FPL Amendments**, published via Bulletin 24-0067). We are proposing to adopt the current IDPC Rule 4600 into DC Rule 4600 without the FPL Amendments but we have shown the FPL Amendments in grey boxes for reference in Appendices 1-4. The FPL Amendments, once approved, will be integrated into the IDPC Rules as well as the DC Rules (depending on the stage of the Rulebook Consolidation project).

Similar to DC Rule 4500, we did not limit DC Rule 4600 to investment dealers because we believe these requirements should apply to any Dealer Member that may engage in financing transactions. Level 4 mutual fund dealers that offer margin lending may engage in financing activities such as securities lending to finance the margin loans. However, we are not considering allowing mutual fund dealers to engage in fully paid lending at this time. This will be considered at a later date when the FPL amendments are closer to approval. As a result, we have included fully paid lending activities as one of the mutual fund dealer restrictions in DC Rule section 1102. ***(DC Rule 4600)***

2.11 Regulatory financial report (*DC Form 1*)

Both the IDPC Rules and MFD Rules require dealers to file a regulatory financial report on a monthly and annual basis. The regulatory filing report required for mutual fund dealers (**MFD Form 1**) includes special purpose financial statements and six supporting schedules. The regulatory filing report required for investment dealers (**IDPC Form 1**) includes special purpose financial statements, thirteen supporting schedules and nine supplemental schedules. The MFD Form 1 has less schedules due to the mutual fund dealers' simple business activities and limited product offerings.

We propose to adopt one Form 1 (**DC Form 1**) that:

- introduces separate schedules for requirements that are unique to investment dealers or mutual fund dealers
- blends and harmonizes the financial statements and similar schedules,
- customizes certain schedules to dealer type, and
- adopts the IDPC schedules where there is no corresponding MFD schedule.

We believe one Form 1 creates more efficiencies while allowing customization of reporting requirements that may be unique to investment dealers or mutual fund dealers. This approach was the preference expressed by public commenters and we believe it is most appropriate to reduce regulatory arbitrage and regulate like activities in a like manner. A copy of the clean version of the DC Form 1 is included in Appendix 3 and the blackline of the DC Form 1 to the IDPC Form 1 is included in Appendix 4.

There are significant differences between the MFD Form 1 and IDPC Form 1 related to the capital formula calculation and the measurement of certain risks. The IDPC Rules' formula measures the financial health of the Dealer to ensure there are sufficient assets in the event

of a wind-down of the dealer by considering non-current liabilities and additional risk measures that are not considered in the MFD formula.

As described in the subsequent sections of this Bulletin, we propose to adopt the IDPC Form 1 requirements for the capital formula calculation of:

- risk adjusted capital including:
  - net allowable assets, and
  - margin required for risk exposures (e.g. counterparty risk, custody risk, etc.),
- early warning excess and early warning reserve.

2.11.1 Net allowable assets

We propose to adopt the IDPC capital formula which is based on net allowable assets calculated with financial statement capital as the initial capital. ***(DC Form 1, Statement B)*** The financial statement capital based formula deducts the Dealer's total liabilities from the total assets to determine the initial capital. The mutual fund dealer risk adjusted capital formula is based on working capital which only considers current liabilities and is not reduced for liabilities such as provisions, deferred tax liabilities, and other non-current liabilities. The RAC formula under the MFD Form 1 requires a 10% adjustment for non-current liabilities which results in 90% of the non-current liabilities being included in RAC. Mutual fund dealers regulated under National Instrument 31-103 are subject to the calculation of excess working capital in National Instrument 31-103F1 which does not include this adjustment. Currently, these dealers are able to include 100% of their non-current liabilities in their adjusted working capital. We anticipate the RAC for approximately 13% of mutual fund dealers will be negatively impacted, with a decrease of at least 5%, by switching from the MFD to the IDPC capital formula. These are mainly Level 4 mutual fund dealers as the Level 1-3 mutual dealers tend to have less complex financial statements and minimal non-current liabilities. By adopting the IDPC formula, we realize there will be a significant impact to certain mutual fund dealers that have these non-current liabilities, so we are proposing a phase in approach to the component of the capital formula related to the exclusion of non-current liabilities from RAC. Under this phase in approach a portion of these liabilities will continue to be included in RAC for the first few years after implementation of the DC Form 1. We expect the mutual fund dealers to take action to adjust their business arrangements to reduce these liabilities that significantly impact their RAC.

We propose that for mutual fund dealers that reported non-current liabilities on their final MFD Form 1, before implementation of the DC Form 1 (**Pre-DC Form 1 non-current liabilities**), may add back a portion of these non-current liabilities when determining the net allowable assets during a five year transitionary period following the effective date of the DC Rules. We have included a transitionary line on Statement B where mutual fund dealers may add back a portion of their non-current liabilities based on the following transitionary percentages:

Period following implementation of DC Rules	Percentage of Pre-DC Form 1 non-current liabilities that may be added back to RAC
1st year	90%
2nd and 3rd year	80%
4th and 5th year	50%
6th year and onward	0%

We propose a five year transitionary period based on feedback from impacted dealers indicating it may take up to five years to eliminate existing non-current liabilities due to the nature of the liabilities. We determined the percentage amounts based on analysis of how existing non-current liabilities will impact mutual fund dealers' RAC and early warning tests under the proposed DC Form 1 and the challenges dealers will face in reducing these liabilities in the first few years after implementation of the DC Rules. As a result, the percentage of non-current liabilities that may be added back to RAC is significantly higher in the first three years following implementation. While the last two years, we expect the liabilities to decrease more significantly as the business strategies creating these liabilities are wound down.

2.11.2 Early warning excess and early warning reserve

Early warning excess **(EWE)** measures short-term liquidity and is used as part of the early warning test framework that provides advance warning of short-term liquidity issues that could lead to a Dealer financial insolvency if not resolved. Both the IDPC and MFD Form 1 include a calculation for early warning excess, although the MFD Form 1 calculation is simpler due to the working capital formula. The IDPC Form 1 includes an early warning reserve **(EWR)** calculation which is an added capital cushion adjustment based on the dealers total margin required.

We propose to adopt the IDPC EWE and EWR calculations with slight modifications to align with the risk adjusted capital approach. Although this will subject mutual fund dealers to the additional EWR calculation, the Level 1 to 3 mutual fund dealers will not be impacted because the early warning tests proposed for Level 1 to 3 mutual fund dealers do not consider EWR. The EWR calculation will be a new requirement for Level 4 mutual fund dealers since we propose to adopt and apply the IDPC early warning tests to Level 4 mutual fund dealers (as explained in section 2.7.2 of this Bulletin). The EWR is considered in determining if early warning level 1 has been triggered for level 4 mutual fund dealers and investment dealers. ***(DC Form 1, Statement C)***

In the proposed DC Form 1, we also modified the early warning excess and reserve calculation on Statement C by:

- Adding a line to adjust for the mutual fund dealers' non-current liabilities during the proposed phased implementation period, and
- Adding a line to adjust for provider of capital charges related to other allowable assets.

2.11.2.1 Adjustment for phase in approach related to non-current liabilities

Since the early warning excess is measuring the dealer's liquidity, the non-current liabilities are added to risk adjusted capital to determine the early warning excess. Since we are proposing a phase in approach for the exclusion of non-current liabilities in RAC, the EWE calculation also needs to be adjusted for the phase in approach to eliminate "double counting" of the phase in adjustment. We have added a reporting line to Statement C of the DC Form 1 for mutual fund dealers to adjust the non-current liabilities during the transitionary implementation period. ***(DC Form 1, Statement C Line 7b)***

2.11.2.2 Adjustment for provider of capital charge related to other allowable assets

In the calculation of early warning reserve, we propose to introduce a new adjustment for other allowable assets that result in a provider of capital charge. There is the possibility of "double counting" capital reductions in the determination of a Dealer Member's early warning reserve when the Dealer Member has a provider of capital charge related to other allowable assets. Since it was never the intent of the provider of capital calculation that "double counting" would occur in the determination of the early warning reserve, an amendment to Statement C is necessary. This issue was identified in an IDPC member regulation notice (MR-0024) but the amendment was not made at the time the provider of capital calculation was introduced and has created unintended early warning consequences for Dealer Members. Since all Dealer Members including mutual fund dealers will be subject to provider of capital concentration requirements, this adjustment to Statement C is required to prevent unintended early warning consequences to those Dealers with a provider of capital charge. ***(DC Form 1, Statement C Line 10)***

2.11.3 Margin required for risk exposures

There are significant differences in the consideration and measurement of certain risks within the risk adjusted capital calculations, between the existing mutual fund dealer Form 1 and the investment dealer Form 1, such as:

- Counterparty credit risk,
- External custody risk,
- Securities concentration risk,
- Foreign currency exposure risk,
- Provider of capital exposure risk.

In developing the DC Form 1, our approach was to ensure common risks have the same regulatory treatment regardless of the dealer type that is taking on that risk. For example, a mutual fund dealer holding foreign currency has the same foreign currency risk as an investment dealer holding the same foreign currency. Under our

proposed approach mutual fund dealers and investment dealers are subject to the same margin requirements for these common risks. In addition to margin requirements, for counterparty and custody risk we propose to adopt the IDPC Form 1 classification criteria for counterparties and custodians (such as acceptable institutions, acceptable counterparties, acceptable securities locations). The IDPC Form 1 classifications are more stringent than the MFD Form 1 as certain counterparties must meet minimum net worth standards to be considered more credit worthy under the IDPC Rules. While we are proposing to adopt additional margin requirements and more stringent counterparty standards for mutual fund dealers, we do not anticipate that these additional risk measures will create material changes to the mutual fund dealers' RAC. We anticipate the provider of capital exposure risk may cause material impacts to the mutual fund dealers RAC and a transitionary period for implementation is proposed.

2.11.3.1 Counterparty credit risk

Under the IDPC Form 1, the counterparty credit risk is addressed by:

- Classifying counterparties based on their creditworthiness ***(DC Form 1 General Notes and Instructions)***
- Reporting non-transactional receivables from certain counterparties as non-allowable assets ***(DC Form 1 Statement A)***
- Requiring margin for trading-related exposures to certain counterparties ***(DC Form 1 Statement B)***

Under the MFD Form 1, counterparty credit risk is also addressed through counterparty classification and reporting of allowable and non-allowable assets, but the classification categories and criteria are different from the IDPC requirements for certain counterparties. Also the MFD capital formula does not consider margin for trading-related exposures.

We also propose to introduce a credit risk framework for the treatment of mutual fund dealers' client debit balances. We propose to allow the option for mutual fund dealers to continue to apply the existing MFD Rule capital requirements to all client debit balances, if they choose to.

(i) Counterparty classification

The current counterparty definitions under the IDPC Form 1 and MFD Form 1 are as follows:

- Acceptable institution **(AI)** *(both MFD Form 1 and IDPC Form 1)*
- Acceptable clearing corporation **(ACC)** *(IDPC Form 1 only)*
- Acceptable counterparty **(AC)** *(IDPC Form 1 only)*
- Acceptable entity **(AE)** *(MFD Form 1 only)*
- Regulated entity **(RE)** *(both MFD Form 1 and IDPC Form 1)*

While the counterparty terms may be the same in certain cases under both rulesets, the definitions of these terms are different. The counterparty definitions under the existing IDPC Form 1 prescribe minimum net worth requirements and a more expansive list of counterparty types than the MFD Form 1 definitions. The counterparty definitions are also applied within the IDPC Rules to classify counterparties that qualify as institutional clients. Institutional clients are exempt from certain standards such as suitability, relationship disclosure, performance and fee reporting. We propose to adopt the IDPC definitions within the proposed DC Form 1 to align with the proposed DC Rules from previous phases where we have adopted the institutional client exemptions. As a result, the IDPC counterparty definitions for acceptable institution, acceptable clearing corporation, acceptable counterparty and regulated entity are brought forward to the DC Form 1.

"Acceptable Institution"

We propose to adopt the IDPC Form 1 definition of AI which includes a more expansive list of entities and more stringent net worth criteria. Under the MFD Form 1, the acceptable institution definition is limited to entities that are Canadian banks, trust companies and credit unions. Under the IDPC Form 1, the acceptable institution definition includes a more expansive list of entities such as governments, Canadian and foreign banks and trust companies, Canadian and foreign pension plans, Canadian insurance companies and credit unions. The IDPC Form 1 definition of AI also requires these entities to meet minimum net worth criteria to qualify as an AI. An AI under MFD Rules has no minimum net worth threshold requirements. By adopting the IDPC definition, counterparties categorized as acceptable institution or acceptable entity under the MFD Form 1 may not qualify as an acceptable institution under the proposed DC Form 1. Mutual fund dealers may have potential capital implications for these types of counterparties where the entity does not meet the net worth requirements. Based on our analysis, we anticipate the impact to be minimal as a significant majority of the financial institutions that mutual fund dealers deal with will meet the net worth requirements to qualify as an acceptable institution.

"Acceptable clearing corporation"

We propose to adopt the IDPC Form 1 definition of acceptable clearing corporation within the DC Form 1. The MFD Form 1 does not have a definition of acceptable clearing corporation as mutual fund dealers are not usually direct participants of clearing corporations due to the nature of the products they offer.

"Acceptable counterparty"

We propose to adopt the IDPC acceptable counterparty definition. Under the IDPC Rules, counterparties that qualify as acceptable counterparties are

considered to be less creditworthy than acceptable institutions but sufficiently creditworthy for dealers to deal with these counterparties on a value for value basis. The acceptable counterparty definition includes many of the similar entities as the acceptable institution definition except the minimum net worth threshold requirement is lower for an AC than an AI. In addition to financial institutions, the AC definition includes additional entities such as mutual funds and corporations which are also subject to a minimum net worth requirement. Corporations are classified as acceptable entities under the MFD Form 1, but will fall in the category of AC in the proposed DC Form 1. Mutual fund companies are not included in the acceptable entity or acceptable institution definition of MFD Form 1 so this will be a new entity categorization for mutual fund dealers.

"Acceptable entity"

We do not propose to adopt the definition of acceptable entity that exists in the MFD Form 1 as it is considered redundant since it includes categories such as acceptable institution and regulated entity within the definition itself. Also other existing categories of counterparties within this definition are captured within the AI and AC definitions.

"Regulated entity"

We propose to adopt the IDPC definition of regulated entity. The definition of regulated entity under the MFD Form 1 is based on the IDPC definition so the entities that qualify under this definition are similar, except for the qualification of mutual fund dealers. Under the MFD Form 1, mutual fund dealers are classified as acceptable entities and under the DC Form 1 a mutual fund dealer may be classified as an acceptable counterparty if the minimum net worth requirements are met. Under the proposed DC Form 1 definition a mutual fund dealer will be classified as a regulated entity since they are a Dealer Member of CIRO under the DC Rules.

(ii) Reporting non-transactional receivables

We propose to adopt the IDPC Form 1 approach to other allowable assets which would limit the other allowable assets to receivables from AIs *(**DC Form 1 Statement A**)*. Under both the MFD Form 1 and the IDPC Form 1, non-transactional receivables from certain entities are classified as other allowable assets on Statement A. The MFD Form 1 and IDPC Form 1 differ in the qualification requirements of these entities. Under the MFD Form 1 other allowable assets include receivables from acceptable entities whereas under the IDPC Form 1 other allowable assets include receivables from acceptable institutions.

For mutual fund dealers, non-transactional receivables with certain counterparties may no longer be considered other allowable assets under the proposed DC Form 1, resulting in a deduction to risk adjusted capital.

For example, non-transactional receivables from regulated entities (other than receivables for IB/CB arrangements or margin deposits), corporations, provincial capital cities, and municipalities no longer qualify as other allowable assets. The other allowable non-transactional receivables reported by mutual fund dealers mainly consists of commission receivables (related to GICs) from financial institutions such as banks, trust companies and insurance companies which will continue to qualify as other allowable assets. We anticipate a minor impact to mutual fund dealers that have interest or dividend receivables from corporations since these receivables are classified as non-allowable assets on the proposed DC Form 1.

(iii) ***Reporting trading-related balances and margin requirements***

To harmonize the counterparty and client reporting and the treatment of client debit balances, while establishing customized and more simplified reporting for mutual fund dealers we propose:

- maintaining separate Form 1 schedules for mutual fund dealers and investment dealers for reporting client trading balances but expanding the mutual fund dealer schedule to include additional counterparties (AI and AC), credit balances and margin reporting ***(DC Form 1 Schedule 3)***
- introducing a credit risk framework for mutual fund dealer client debit balances, ***(DC Form 1 Schedule 3)***
- codifying a harmonized margin treatment for debit balances in registered accounts ***(DC Form 1 Notes and instructions to Schedule 3 and 4)***
- introducing a broker trading balance schedule for mutual fund dealers ***(DC Form 1 Schedule 6)***
- adopting the IDPC equity deficiency margin treatment for trading balances with ACs and REs ***(DC Form 1 Notes and instructions to Schedule 3 and 6)***
- adopting the IDPC Form 1 schedule for reporting the ten largest settlement date trading balances with AIs and ACs ***(DC Form 1 Schedule 5)***

Mutual fund dealers may have clients that qualify as an AI, AC or RE in which case the dealer may benefit from reduced capital requirements under the proposed credit risk framework for these clients. Under the MFD Rules, there are no capital implications for trading balances, with an AI, AC or RE, that arise from trading activity such as the purchase or sale of investment products for the mutual fund dealers' clients. The proposed margin requirements for balances with an AC or an RE may increase capital implications for these trading balances but we believe its important to reduce regulatory arbitrage since the counterparty risk is the same regardless of which dealer type is engaging with the counterparty. We do not anticipate significant capital implications to mutual fund dealers, but we may consider a phased-in implementation approach for mutual fund

dealers to have time to put the proper systems and policies and procedures in place to monitor and calculate margin implications of these counterparties. In the questions section we have requested commenters to provide feedback on this potential approach.

Separate Form 1 schedules for reporting client trading balances

We propose separate client account reporting schedules in the DC Form 1 for mutual fund dealers and investment dealers, but we have harmonized these schedules to align with the IDPC Form 1 reporting approach. The purpose of the separate schedules is to allow the mutual fund dealers with simpler business models (not offering margin accounts) to complete a customized schedule that is more applicable to their business. We have harmonized the mutual fund dealer client account reporting schedule to the IDPC reporting approach by:

- adding reporting lines for client credit balances, in addition to the existing debit balance reporting
- introducing reporting lines for trading balances with AIs and ACs, and
- adding reporting lines for margin required on the credit risk exposures with clients.

We have preserved the reporting of advance redemption proceeds by mutual fund dealers for those dealers that advance funds to clients in connection with the redemption of mutual fund securities. ***(DC Form 1 Schedule 3)***

We propose to adopt the IDPC Form 1 Schedule 4 to apply to investment dealers with no changes to the reporting requirements. ***(DC Form 1 Schedule 4)***

We are requesting feedback in the questions section of the Bulletin on whether the separate schedule approach is necessary or whether a combined schedule for both mutual fund and investment dealers is more effective.

Credit risk framework for mutual fund dealer client debit balances

We propose to introduce a credit risk framework for client debit balances that allows mutual fund dealers to apply a margin calculation methodology based on the credit risk exposure to the client.

Where the client qualifies as an AI or AC, we propose margin be determined based on the same methodology as the IDPC Rule margin requirements.

Where the client does not qualify under a specific counterparty category, we propose margin be determined as the equity deficiency in the client account for balances overdue less than 6 business days past regular settlement date. This equity deficiency approach is similar to the margin approach under the IDPC Form 1 for cash accounts. To encourage mutual fund dealers

to resolve these debit balances on a timely basis, we propose that if the debit balance is not resolved within 6 business days, 100% of the debit must be deducted from risk adjusted capital.

Alternatively, to maintain operational simplicity, mutual fund dealers may choose to margin client debit balances, including clients categorized as acceptable institutions and acceptable counterparties, at 100% of the balance, as currently required under MFD Rules.

Approximately 25% of mutual fund dealers report client debits on the MFD Form 1 and may be impacted if they adopt the new margining approach. Mutual fund dealers that apply the new credit risk framework may need to update their policies, procedures and systems but would benefit from reduced regulatory capital requirements. Also, if the mutual fund dealer applies the equity deficiency margin approach the client account related securities concentration requirements must also be considered. In the notes and instructions to DC Form 1 Schedule 3, we have clarified the requirement to consider concentration when applying the equity deficiency margin approach. ***(DC Form 1 Schedule 3 and 4 Notes and Instructions)***

Margin treatment of debit balances in registered accounts

We published guidance for investment dealers on how to treat client debit balances if they arise in a registered account (GN-FORM1-22-001). We propose to codify this guidance in the proposed DC Form 1 and extend this treatment to apply to both investment dealers and mutual fund dealers. ***(DC Form 1 Schedule 3 and 4 Notes and Instructions)***

Schedule for mutual fund dealers to report broker trading balances

We have introduced a simpler version of the IDPC broker trading balance schedule in DC Form 1 to apply specifically to mutual fund dealers reporting broker and dealer trading balances. ***(DC Form 1 Schedule 6)*** This schedule includes not only balances with regulated entities but also trading balances with mutual fund companies for redemptions and purchase transactions. We do not propose to include a reporting line on this schedule for balances with acceptable clearing corporations since mutual fund dealers are typically not participants of clearing corporations. We expect most mutual fund dealers clear trades with mutual fund companies (for mutual fund securities transactions), financial institutions (for GIC and segregated fund transactions) or regulated entities (for exchange-traded fund transactions). We are seeking feedback on this approach in the questions section of the Bulletin.

We propose to adopt the IDPC Form 1 schedule for reporting broker trading balances to apply to investment dealers with no changes to the reporting or margin requirements. ***(DC Form 1 Schedule 7)***

Equity deficiency margin treatment for trading balances with AC and RE

Under MFD Form 1 there are no margin implications for trading balances arising from purchases and sales of client or dealer securities or investments. Under IDPC Form 1 where a trading balance arises with an acceptable counterparty or regulated entity, a credit risk exposure margin calculation is required equal to the equity deficiency. We propose to harmonize the treatment of this credit risk exposure by adopting the IDPC margin approach for AC and RE which will align both mutual fund dealers and investment dealers to the same margin implications for trading with these entities. ***(DC Form 1 Notes and instructions to Schedule 3 and 6)***

Reporting significant trading balances with AIs and ACs

We propose to extend the requirement to report significant settlement date balances with AIs and ACs to mutual fund dealers. This reporting is provided on an annual basis and is limited to the 10 largest settlement date balances that exceed $250,000 or 20% of risk adjusted capital. Although this is a new reporting requirement for mutual fund dealers, we do not anticipate a significant impact as we expect most settlement date balances with these entities are below the reporting thresholds. ***(DC Form 1 Schedule 5)***

2.11.3.2 External Custody risk

We propose to adopt the IDPC custody risk requirements within the IDPC Form 1 for both investment dealers and mutual fund dealers which includes:

- qualification requirements for custodians to meet the acceptable securities location definition, and
- margin implications for unreconciled positions or securities held at non-acceptable locations.

The custodian qualification requirements are generally similar under both rule sets but where there is a difference we propose to adopt the IDPC qualifications which are more stringent. We also bring forward the IDPC margin requirements which have more flexibility to address situations with different risks such as when the external location is acceptable, but the agreement or reconciliation requirements are not met.

(i) Acceptable securities location

The acceptable securities location definition under the existing rules includes various counterparties that are considered acceptable to hold client and dealer securities. Both IDPC and MFD rules consider depositories, mutual funds, regulated entities and federal and provincial governments to be qualifying acceptable securities locations. Our proposal to adopt the IDPC definition would not impact dealers holding securities at these locations.

The main difference in the acceptable securities location definition between the IDPC rules and the MFD rules is the qualification of financial institutions such as banks, credit unions and trust companies. The IDPC Rules require a minimum net worth threshold to be met for qualification of these counterparties, but the MFD Rules do not have an equivalent net worth requirement. We anticipate the current financial institution custodians used by mutual fund dealers, for holding mutual fund products and exchange-traded funds, will qualify as acceptable securities location under the proposed definition. The net worth requirements may impact mutual fund dealers that hold guarantee investment certificates or other similar assets at low-capitalized credit unions or other financial institutions.

There are additional securities locations under the IDPC acceptable securities location definition that are not included in the current MFD acceptable securities location definition such as foreign locations and the London Bullion Market Association (for holding gold and silver bars). By adopting the IDPC definition these custodians would be newly acceptable securities locations for mutual fund dealers if the dealer holds securities or eligible precious metals bullion at such custodians. ***(DC Form 1 General notes and definitions)***

(ii) Margin requirements for custody risk

Under both the IDPC and MFD rules, margin requirements are imposed when securities are held at a non-acceptable securities location and when unresolved differences arise from reconciliations with the custodian's records. Where there are differences in the requirements, we propose to adopt the IDPC requirements in the proposed DC Form 1 which may result in reduced margin implications for mutual fund dealers.

Under both the IDPC and MFD acceptable securities location requirements, an external custodian must meet the counterparty qualification criteria and must sign a written custody agreement that includes specified terms, otherwise margin requirements may apply. Where the external custodian does not meet the counterparty qualification criteria the margin required under both rulesets is equal to 100% of the market value of the securities held at the custodian. The margin requirements under the IDPC and MFD Rules differ in the situation where the external custodian meets the counterparty qualification criteria for an acceptable securities location, but the written custody agreement is not acceptable. The IDPC Rules recognize that an inadequate custody agreement does not pose a risk to 100% of the securities when held at a qualifying securities location. Under this situation the IDPC Rules impose a penalty of 10% of market value of the securities on the early warning excess as explained in the notes and instructions to Statement B and C of the Form 1. By adopting of IDPC requirements, mutual

fund dealers will benefit from the reduced margin implications if this situation arises. ***(DC Form 1 Statement B Line 21 and Statement C Line 4)***

For unresolved differences associated with reconciling to mutual fund custodians, IDPC Rules recognize that these custodians may provide statements or records on a quarterly instead of monthly basis which creates challenges for dealers to perform monthly reconciliations to identify differences. The IDPC Rules allow reduced margin implications where mutual fund positions are not reconciled on a monthly basis if certain conditions are met. By adopting the IDPC Rules for unresolved differences, this reduced margin approach for mutual fund position reconciliations will also be available to mutual fund dealers where the conditions are met to apply it. ***(DC Form 1, Statement B Line 24)***

2.11.3.3 Securities concentration risk

We propose to adopt the IDPC securities concentration risk requirements for both investment dealers and mutual fund dealers as any dealers investing in securities or providing client margin on securities are exposed to this risk. We propose to introduce simplified concentration schedules in the DC Form 1 which will be applicable to mutual fund dealers that invest their excess cash in securities or hold inventory positions that may pose a concentration risk.

The concentration schedules are based on the IDPC concentration risk requirements for inventory positions in the existing IDPC Form 1 Schedules 9, 9A and 9B. We have excluded the client concentration risk requirements from the simplified concentration schedules because mutual fund dealers do not currently offer margin to clients, and we expect most mutual fund dealers will continue to maintain this approach. ***(DC Form 1 Schedules 10, 10A and 10B***)

As described in other sections of this Bulletin, we are proposing to allow mutual fund dealers to offer margin to clients or calculate margin using the cash account margining approach under certain conditions. Mutual fund dealers that choose to offer margin to clients or use the cash account margining approach would be required to consider the client concentration risk and complete the concentration schedules that include both inventory and client positions. ***(DC Form 1 Schedules 11, 11A and 11B)***

We have also introduced the term “diversified investment product” to expand the option for dealers to “look through” certain investment products to the underlying securities, when determining the concentration exposure. Under the IDPC Form 1 requirements, the dealer may calculate their concentration risk exposures for broad based index positions by looking through to the underlying securities in the basket and calculating the exposure on the individual securities in the basket. We recognize that

certain investment products, such as mutual funds that have a diversified basket of underlying investment products, pose significantly less concentration risk than individual securities. We propose to broaden the "look through" approach beyond index products to include other investment products with a diversified basket of underlying investment products (excluding derivatives). We are also seeking feedback on whether we should go further and exclude certain diversified investment products from the concentration exposure calculation completely.

Although calculating securities concentration risk exposures will be a new requirement for mutual fund dealers, we do not anticipate any material impacts to their RAC. Mutual fund dealers with simple business models such as Level 1-3 mutual fund dealers typically invest their excess cash in money market products or government issued products that are excluded from the concentration risk calculation. For those mutual fund dealers that have invest their excess funds in products such as mutual funds, securities, debt or other products that are subject to the concentration calculation, we do not expect the loan value amounts compared to RAC to be significant enough to trigger concentration charges.

2.11.3.4 Foreign currency exposure risk

We are proposing to adopt the IDPC foreign currency exposure risk requirements for both investment dealers and mutual fund dealers as any dealers with foreign currency assets, liabilities and contracts are exposed to this risk. This means adopting the current IDPC Form 1 unhedged foreign currency calculation schedule (Schedule 11) into the DC Form 1 as a schedule (proposed Schedule 13) applicable to both mutual fund dealers and investment dealers. ***(DC Form 1 Schedule 13)***

Although calculating unhedged foreign currency risk exposure will be a new requirement for mutual fund dealers, we do not anticipate any material impacts to their RAC. We expect the calculation will not be applicable for most Level 1 to 3 mutual fund dealers that have a simple business with no foreign currency assets and liabilities. For those mutual fund dealers that have foreign currency exposures, we anticipate the exposures will be generally limited to US dollar cash deposits and this exposure is likely hedged against the US dollar client liabilities resulting in minimal unhedged exposure. We also do not anticipate mutual fund dealers to engage in foreign currency trading or futures contracts. As a result, we propose to introduce a separate simplified version of the IDPC Form 1 detail foreign currency margin calculation schedule into the DC Form 1. This simplified schedule excludes the foreign exchange contract exposure calculations that are not expected to apply to mutual fund dealers and would allow mutual fund dealers to calculate and report the details of the unhedged foreign

exchange exposure related to monetary assets and liabilities. ***(DC Form 1, Schedule 13A)***

2.11.3.5 Provider of capital exposure risk

We are proposing to adopt the IDPC provider of capital exposure risk requirements for both investment dealers and mutual fund dealers as any dealers with substantial cash deposits, loans and investments with their provider of capital are exposed to this risk. This means adopting the current IDPC Form 1 provider of capital concentration charge schedule into the DC Form 1 as a schedule applicable to both mutual fund dealers and investment dealers. ***(DC Form 1 Schedule 14)***

We anticipate approximately 13% of mutual fund dealers will have a potentially significant provider of capital charge because they hold a significant portion of cash at a parent bank or financial institution that would trigger a provider of capital charge. In order to give these dealers the appropriate time to reorganize their business to reduce the provider of capital exposures, we are proposing a phase in approach for the provider of capital exposure.

We propose that mutual fund dealers may reduce the provider of capital charge when determining RAC during a five year transitionary period after implementation of the DC Rules and DC Form 1. The full amount of the provider of capital charge will be required to be included in RAC in the sixth year following implementation. This transition period and the phase in percentages are consistent with the proposed phase in approach for the portion of the capital formula related to non-current liabilities. We believe a common phase in approach is more efficient and will prevent errors and confusion that may arise from multiple different transition periods. The proposed reduction percentages to phase in the provider of capital charge are as follows:

Period following DC Rule Implementation	Provider of capital charge phase in reduction percentage
1st year	90%
2nd and 3rd year	80%
4th and 5th year	50%
6th year	0%

2.11.4 Organization of Form 1 Statements and Schedules

Although we are proposing to adopt the IDPC Form 1 capital formula and general structure, we have reorganized and renamed certain statements and schedules to accommodate the additional mutual fund dealer schedules and provide a more logical and sequential order for similar schedules.

2.11.4.1 Blended statements and schedules

We have blended the following statements and schedule to include reporting lines from both the MFD Form 1 statements and the IDPC Form 1 statements to ensure the existing regulatory financial information for each dealer type continues to be reported:

- Statement of financial position ***(DC Form 1 Statement A)***,
- Statement of risk adjusted capital (and supplemental details of unresolved differences) ***(DC Form 1 Statement B and Statement B supplemental)***,
- Statement of early warning excess and reserve ***(DC Form 1 Statement C)***,
- Statement of income and comprehensive income ***(DC Form 1 Statement D)***,
- Statement of changes in capital and retained earnings ***(DC Form 1 Statement E)***,
- Securities owned and sold short ***(DC Form 1 Schedule 2)***,
- Current income tax ***(DC Form 1 Schedule 8)***,
- Insurance ***(DC Form 1 Schedule 12)***, and
- Other supplementary information. ***(DC Form 1 Schedule 18)***

The changes in the reporting lines of these statements and schedules due to blending can be identified in the table of concordance (Appendix 5) and blackline to the IDPC Form 1 (Appendix 4).

2.11.4.2 IDPC schedules adopted where no equivalent MFD schedule

We propose to adopt into the DC Form 1 the following IDPC schedules applicable to investment dealers where there is currently no equivalent MFD Schedule:

- Statement of free credit segregation ***(DC Form 1 Statement F)***,
- Analysis of loans, securities borrowed/loaned and resale/repurchase agreements ***(DC Form 1 Schedules 1 and 9)***,
- Cash and securities borrowing and lending arrangements concentration charge ***(DC Form 1 Schedule 9A)***,
- Margin for concentration in underwriting commitments ***(DC Form 1 Schedule 2A)***,
- Underwriting issues margined at less than the normal margin rates ***(DC Form 1 Schedule 2B)***,
- List of ten largest settlement date trading balances with acceptable institutions and acceptable counterparties ***(DC Form 1 Schedule 5)***,
- Tax recoveries ***(DC Form 1 Schedule 8A)***,
- Provider of capital concentration charge ***(DC Form 1 Schedule 14)***, and
- Margin on futures concentration and deposit, ***(DC Form 1 Schedules 15)***

As explained in section 2.11.3.5 of this Bulletin, mutual fund dealers are expected to be impacted by the provider of capital concentration charge if they hold cash at an associated financial institution.

The tax recoveries schedule gives recognition to the tax effect of revenue-related receivables and margin by calculating applicable tax recoveries that may be added back to risk adjusted capital or early warning excess. The tax recoveries schedule will be a new schedule for mutual fund dealers resulting in a potential benefit of increased risk adjusted capital for those dealers with significant tax expenses.

The remaining schedules generally apply to investment dealers' activities, but if a mutual fund dealer is engaging in any activity that would be reported or margined on these schedules they will be impacted by the adoption of these schedules. For example, if a mutual fund dealer engages in financing activities, they would be required to report the related balances on Schedule 1 and 9 or if they opt to use client free credits, they would need to complete DC Form 1 Statement F.

2.11.4.3 Schedules customized to MFDs

We propose separate schedules specific to mutual fund dealers and investment dealers for the following:

- Certificate of UDP and CFO,
- Client trading balances ***(DC Form 1 Schedules 3 and 4)***,
- Broker dealer trading balances ***(DC Form 1 Schedules 6 and 7)***,
- Securities concentration ***(DC Form 1 Schedules 10, 10A, 10B and 11, 11A, 11B)***,
- Foreign exchange margin requirements ***(DC Form 1 Schedules 13, 13A and 13B)***, and
- Early warning tests. ***(DC Form 1 Schedules 16 and 17, 17A)***

As explained in other sections of this Bulletin we are proposing simplified versions of the schedules for broker dealer trading balances, securities concentration and foreign exchange margin which will be applicable to mutual fund dealers with simple business activities. We are proposing different approaches for certain mutual fund dealers and investment dealers for client margining and early warning tests so we have proposed appropriate separate schedules in the DC Form 1. Although the questions on the Certificate of UDP and CFO are generally the same for mutual fund dealers and investment dealers, there are differences related to cash segregation, reconciliation of trust accounts and other mutual fund dealer specific requirements. We have proposed separate Certificates of UDP and CFO for mutual fund dealers and investment dealers due to these differences. Where a mutual fund dealer chooses to offer margin or use free credits, the CFO and UDP must sign the certificate designed for investment

dealers that includes questions related to free credit segregation and concentration of securities as explained in the notes and instructions to the certificate.

2.11.4.4 New schedule related to assets under administration

We are also proposing to introduce an additional schedule to collect supplementary information on the assets under administration at Dealers. This schedule expands the information currently reported by mutual fund dealers in the mutual fund dealer Form 1 to divide the data between client and nominee name and between assets including Quebec and excluding Quebec. The schedule also requires investment dealers to provide assets under administration information for outside holdings and client assets introduced by a mutual fund dealer. Dual registered dealers are also required to provide assets under administration information on this schedule. The assets under administration schedule was added to assist CIRO in determining fees and assessments. ***(DC Form 1 Schedule 19)***

2.11.4.5 Audit reports and agreed-upon procedures

(i) Audit reports

Under both the MFD and IDPC Form 1, two independent audit reports are required to be filed by the auditor with the annual Form 1. The auditor provides an opinion on whether the financial statements fairly present the financial position of the dealer and the results of its operations. The auditor provides a second opinion on whether the additional statements are prepared in accordance with the Notes and Instructions to Form 1. This second audit report differs between the MFD and IDPC Form 1 because the IDPC Form 1 includes an additional statement for the free credit segregation amount which is not part of the MFD Form 1.

We propose to maintain the standard audit report for the financial statements ***(DC Form 1 Statements A, D and E)*** applicable to both mutual fund dealers and investment dealers. We propose to adopt both audit reports for the opinion on additional statements for mutual fund dealers and investment dealers as separate reports in DC Form 1. The audit report applicable to mutual fund dealers should be used by auditors for mutual fund dealers that continue to segregate all client cash in trust. This audit report does not include the statement of free credit segregation amount in the opinion. Where the mutual fund dealer chooses to use free credits in their business, the auditor will be required to complete the audit report that includes an opinion on the statement of free credit segregation amount.

(ii) Agreed-upon procedures report

Under both the MFD and IDPC Form 1, the auditor is required to perform a set of agreed-upon procedures and include a report of the findings in the

Form 1. There are additional procedures required in the IDPC Form 1 for guarantee/guarantor arrangements. The segregation procedures also differ between the IDPC Form 1 and MFD Form 1 due to the investment dealers ability to offer margin.

We propose to adopt both the agreed-upon procedures report from the MFD Form 1 and the IDPC Form 1 as separate reports in the DC Form 1. This will allow auditors to apply the agreed-upon procedures for mutual fund dealers that continue to have a simple business. Where the mutual fund dealer chooses to offer margin to clients, the auditor would be required to complete the agreed-upon procedures report that includes the segregation procedures related to a dealer that offers margin.

2.11.5 Other Form 1 proposals

2.11.5.1 Reporting and filing

One of the reporting differences between the MFD and IDPC Form 1 is that mutual fund dealers report their figures in dollars and investment dealers report figures to the nearest thousand. Amounts less than a thousand are generally immaterial so we are proposing all amounts be reported to the nearest thousand in the DC Form 1.

We recognize the number of statements and schedules may seem overwhelming for those dealers with limited or simple business activities where most of the schedules would not apply. Our approach to help dealers complete the relevant parts of the DC Form 1 is to create more customization in the regulatory filing system. We plan to create a questionnaire type component to the regulatory filing system where Dealers will answer questions about their business that will then show relevant schedules or lines for input and hide the non-relevant schedules.

On a monthly basis, dealers will only be required to file a subset of schedules from the Form 1. This approach is consistent with the current IDPC monthly filing report requirements. The schedules to be filed by each dealer type are outlined in the DC Form 1 general notes and definitions. Mutual fund dealers will benefit from reduced monthly reporting of certain schedules. For example, the “Analysis of clients trading accounts” schedule ***(DC Form 1 Schedule 3)*** is only required to be submitted on an annual basis. As discussed in section 2.2.2 of this Bulletin we propose a new definition, “monthly financial report” to represent the Form 1 subset that is filed on a monthly basis.

2.11.5.2 Mutual fund dealers structured as not-for-profit

We have modified certain statements and corresponding notes and instructions to accommodate fund balance reporting for those dealers that are structured as a not-for-profit organization. Dealers that are structured

as a not-for-profit organization do not have share capital. The base capital for these dealers is the fund balances they receive in donations. We have included the fund balances as capital in the risk adjusted capital calculation but we have proposed an adjustment to deduct any fund balances that are restricted by an external party other than CIRO. If the fund balances have been restricted by an external party, we do not consider these funds as available capital for the dealer. Statements A, B, D and E and the corresponding notes and instructions were amended to consider fund balance reporting for not-for-profit organizations.

2.11.5.3 Proposed Form 1 compared to the MFD Form 1

The table of concordance in Appendix 5 includes a comparison of the MFD Form 1, IDPC Form 1 and DC Form 1 to assist mutual fund dealers in identifying and assessing the Form 1 changes and potential impacts. We have adopted or blended all of the MFD Form 1 statements and schedules into the proposed DC Form 1, except for the statement of changes in subordinated loans (currently Statement F of the MFD Form 1). We are proposing to repeal the statement of changes in subordinated loans in its entirety. This statement is no longer needed as CIRO obtains all necessary details of the subordinated loans outstanding at each Dealer Member at the time CIRO approves changes to such loans. This statement was repealed from the investment dealer Form 1 in 2011 for similar reasons.

2.11.5.4 Proposed Form 1 compared to the IDPC Form 1

In addition to the table of concordance in Appendix 5, we have provided a blackline of the proposed DC Form 1 to the IDPC Form 1 in Appendix 4.

3. Impacts of the Proposed DC Rules

3.1 Impact assessment approach

As the Rule Consolidation Project is being pursued in five phases, and the combined impact of the project can only be assessed once development of all five phases, including consultations on each phase, has been completed, it would be misleading for us to assess the impact of each phase in isolation from the other phases or to make an assessment of the combined impact of the five project phases until all phases have been developed.

To provide you with some impact information in the interim, we will identify the impacts specific to each project phase as each project phase is published for public comment. We will provide an overall Rule Consolidation Project impact assessment once all 5 phases have been completed.

3.2 Specific impacts of Phase 5 Proposed DC Rules

We have assessed the impact of the changes being introduced as part of the Phase 5 Proposed DC Rules as having a neutral to positive impact overall.

We believe Phase 5 Proposed DC Rules would have strong positive impacts on clients and CIRO Staff.

While there may be some negative impacts to mutual fund dealers, and in more limited instances to investment dealers, many of these impacts are short-term, as they relate to requirements to develop new policies, procedures and internal systems. Once developed, the existence of harmonized industry infrastructure and regulatory expectations will be positive for the industry as a whole.

The changes to the capital formula for mutual fund dealers may be significant for some dealers, which offsets the strong positive impacts to other stakeholders. As such our overall assessment of the impact of the Phase 5 Proposed DC Rules is neutral to positive.

A complete impact analysis of the Phase 5 Proposed DC Rules is attached as Appendix 8.

3.3 Regional and specific stakeholder group impacts

Mutual fund dealers registered in Quebec may have more significant impacts than mutual fund dealers registered in other provinces due to the differences between their current regulatory financial reports and the proposed Form 1.

4. Alternatives to rule consolidation considered

We did not consider any alternatives to rule consolidation, such as maintaining separate rules for investment dealers and mutual fund dealers as, based on the feedback provided in response to CSA Position Paper 25-404, *New Self Regulatory Organization Framework*, we determined that there is general cross-stakeholder support for rule consolidation.

We considered maintaining separate financial solvency reports for mutual fund dealers and investment dealers as an alternative to a consolidated Form 1. We chose to propose a consolidated financial report to ensure consistency in measuring and monitoring the financial solvency of dealers, while maintain flexibility to introduce customized schedules and reporting lines for each dealer type. Based on feedback from public commenters and advisory committees, stakeholders generally support our approach.

5. Questions

While comment is requested on all aspects of the Phase 5 Proposed DC Rules, comment is also specifically requested on the following questions:

Question #1 - Definition of "complaint"
The proposed definition of "complaint" includes current and former clients. Should "prospective clients" also be included, as they are in the current MFD Rules? Do "prospective clients" generate a significant number of substantive complaints that present a material regulatory concern, rather than just service issue?

Question #2 - Definition of "serious misconduct"

Does the proposed definition of "serious misconduct" cover the appropriate elements that should be reported, investigated, and dealt with in respect of complaints?

Note that the proposed definition does not specifically include harm to the Dealer. Should it encompass conduct that harms the Dealer, even where that harm ***does not*** pose a reasonable risk of material harm to clients or the capital markets, nor result in material non-compliance with applicable laws?

Question #3 - Definition of "non-reportable complaints"

Is the definition of "non-reportable complaints" appropriate to minimize reporting where there is no material risk of harm to clients or the capital markets, or instances of non-compliance, while still ensuring that material complaints are addressed?

Question #4 - Time limit to provide a substantive response letter

Is the 90-day time limit to provide a substantive response letter to a complainant appropriate, given that the Autorité des marchés financiers has moved to a 60-day period (with a 30-day flex period), while the other CSA members recommend a 90-day period (per Companion Policy 31-103 *Registration Requirement*s, Exemptions *and Ongoing Registrant Obligations*)?

Question #5 - Time limit applicable to internal dispute resolution

Is the proposed time limit for internal dispute resolution processes reasonable, considering the need to balance an expedient resolution for clients while still allowing an appropriate amount of time for Dealers to determine an effective and fair resolution?

Question #6 - Client reporting

Do you agree with our assessment of the areas where the proposed harmonization is consistent with current requirements and Dealer practices and therefore no significant negative impact has been introduced for Dealers and clients as a result? If not, please explain.

Do you agree with our assessment of those areas where the proposed harmonization may impact some Dealers, but that the benefits of such harmonization outweigh the costs to the affected Dealer? If not, please explain.

Question #7 - Use of free credit client cash

Is it appropriate to extend the ability to use free credit client cash to level 3 mutual fund dealers in addition to level 4 mutual fund dealers?

Question #8 - Transition period for Form 1 capital formula and provider of capital charge
Is the phased approach we propose, for mutual fund dealers to adopt the new DC Rules Form 1 capital formula and the provider of capital concentration charge, an appropriate approach and transition period?

Question #9 - Transition period for mutual fund dealers' auditor approval
Should the proposed requirements for approval of mutual fund dealers' auditors as panel auditors be subject to an extended transition period beyond the general effective date for the DC Rules, and if so, what is an appropriate extended transition period?

Question #10 - Form 1 schedules
Where we have proposed separate schedules for mutual fund dealers and investment dealers in the new DC Rules Form 1 (e.g. client trading accounts, broker trading accounts, FX margin, concentration etc.), are these separate schedules appropriate or should we consider one combined schedule for both mutual fund dealers and investment dealers?

Question #11 – Concentration for diversified investment products
The current concentration schedule allows Dealers to look through to underlying securities where the concentrated product is a broad based index. Does the proposed change allowing this approach on a broader basis to diversified investment products such as mutual funds that have a basket of underlying investment products (not including derivatives) provide sufficient operational flexibility to Dealers in managing potential concentration exposures? Or, should we consider excluding these types of fund products from concentration testing based on their risk profile?

Question #12 - Transition period for counterparty margin
To what extent is it appropriate to apply a phase-in approach for mutual dealers to adopt the counterparty margin requirements for acceptable counterparties and regulated entities? What is an appropriate extended transition period?

Question #13 – Rule consolidation project
Considering all the phases of this project, are the proposed DC Rules aligned with the objectives of the project? To what extent have the proposed DC Rules introduced excessive regulatory burden?

6. Policy Development Process

6.1 Regulatory purpose

We took the public interest into consideration when developing the Phase 5 Proposed DC Rules and we believe the proposals achieve their intended objective of ensuring that like

dealer activities will be regulated in a like manner while minimizing regulatory arbitrage between investment dealers and mutual fund dealers.

We also believe the Phase 5 Proposed DC Rules will foster public confidence in capital markets by ensuring all CIRO Dealer Members will be held to standards of conduct that foster fair, equitable and ethical business standards and practices.

6.2 Regulatory process

The Board of Directors of CIRO (**Board**) has determined the Phase 5 Proposed DC Rules to be in the public interest and on March 19, 2025, approved them for public comment.

We consulted with the following CIRO advisory committees on this matter:

- Investor Advisory Panel (IAP),
- Conduct, Compliance and Legal Advisory Section (CCLS),
- Financial and Operations Advisory Section (FOAS),
- Panel Auditor's Committee,
- Form 1 Consultation Group including mutual fund dealer and investment dealer representatives,
- Regional Councils,

as well as a targeted ad-hoc committee comprised of mutual fund dealers.

After considering the comments received in response to this Request for Comments together with any comments of the CSA, CIRO staff may recommend revisions to the Phase 5 Proposed DC Rules. Such revisions will be submitted to the Board for approval for republication together with revisions to other Proposed DC Rules published in previous phases.

6.3 CIRO advisory committee feedback

We have received overall positive feedback regarding the Phase 5 Proposed DC Rules from our advisory committees except for our proposals:

- to extend use of free credit client cash to Level 4 mutual fund dealers as the IAP expressed concerns that this could increase risk to clients, and mutual fund dealers might not compensate clients for this additional risk. We believe that the requirements for mutual fund dealers to comply with the free credit client cash segregation limit and to provide disclosures to clients about the use of their cash are sufficient to mitigate these risks. These requirements were established for investment dealers that use free credit client cash in their operations, and no adverse consequences to clients have been noted from this practice,
- to allow different standards for mutual fund dealers that choose not to offer margin or use free credit client cash. The FOAS capital subcommittee suggested that financial standards should be harmonized across all dealers. They argued that requiring some mutual fund dealers to comply with different standards would create too much complexity and confusion about which rules apply. We chose to give mutual fund dealers the option of offering margin accounts or using free credit client cash, provided they

comply with higher standards. We believe this approach avoids unnecessary regulatory burden on mutual fund dealers that prefer to maintain a simple business model without offering margin or using free credits. We believe the provisions introduced in DC Rule subsections 4382(2) and 5112(2) along with the descriptions in the notes and instructions to the statements and schedules in DC Rule Form 1, provide sufficient clarify for mutual fund dealers to identify the applicable requirements if they choose to offer margin accounts or use free credit client cash,

- to remove the requirement for Dealers to disclose non-arms length transactions in the account statements to clients. (see the proposal in section 2.6.4.2 of this Bulletin). The IAP raised concerns that simply relying on such disclosure in the relationship disclosure and trade confirmations alone, can come with net loss for investors The account statement disclosure requirement is currently unique to investment dealers, and it is not required under the MFD Rules nor National Instrument 31-103. We considered different alternatives under the consolidated rules, including keeping the status quo. Adopting common conflicts of interest requirements with double standards is not advisable, since we are striving for a level playing field. Between the alternative of aligning under the IDPC Rules approach or the MFD Rule/National Instrument 31-103 approach, we believe the second alternative offers a more balanced and impactful solution because such an approach:
    - would also align CIRO's Dealer Members' practices with those of securities registrants that adhere to the National Instrument 31-103 reporting requirements (e.g. Quebec mutual fund dealers, portfolio managers, investment fund managers);
    - does not require mutual fund dealers to change their systems and incur costs associated with modifying their accounts statements to conform with the more onerous disclosure standard; in comparison investment dealers can and may choose to maintain their status quo; and
    - does not necessarily come with a net loss for the investor, in view of the enhanced Dealer obligation, post Client Focused Reforms, to address conflicts of interest in the client's best interest (beyond disclosure) following empirical data suggesting that disclosure alone, or over disclosure, is not always effective.
- to retain a 90-day timeline for Dealer Members to provide a substantive response to a complaint as per Companion Policy 31-103. The IAP expressed a desire to have a shortened complaint handling timeline. We have asked a question in the present Bulletin seeking public comment on whether a 90-day time limit to provide a substantive response letter to a complainant is appropriate.

7. Appendices

Appendix 1 – Phase 5 Proposed DC Rules (clean)

Appendix 2 – Phase 5 Proposed DC Rules (blackline)

Appendix 3 – Phase 5 Proposed DC Form 1 (clean)

Appendix 4 – Phase 5 Proposed DC Form 1 (blackline)

Appendix 5 – Table of Concordance

Appendix 6 – Proposed Serious Misconduct Definition Comparison Table

Appendix 7 – Impact Analysis of the Phase 5 Proposed DC Rules

Proposed "serious misconduct" definition Comparison Table *(DC Rule section 3702(1))*

Activity listed under the definition of "serious misconduct"	**Current Requirements**				**Proposed DC Rule 3700**
	Required to be investigated and reported under the **current IDPC Requirements**?	Required to be reported under the **current MFD Requirements**?	Included in the "misconduct" term under the **current IDPC Complaint Requirements**?	Included as matters to be dealt with in the **current MFD Complaint Requirements?**	Included in the definition of "serious misconduct" under proposed **DC Rule 3700**?
material breach of client personal information under the Dealer Member's control	No	Yes	Yes	Yes	No[31]
theft	Yes	Yes	Yes	Yes	Yes
fraud	Yes	Yes	Yes	Yes	Yes
misappropriation or misuse of funds or securities	Yes	Yes	Yes	Yes	Yes
forgery	Yes	Yes	Yes	Yes	Yes
money laundering	Yes	Yes	No	Yes	Yes
insider trading	Yes	Yes	No	Yes	Yes
misrepresentations	Yes	Yes	Yes	Yes	Yes
unauthorized trading, including discretionary trading contrary to sub-section 3221(1)	Yes	Yes	Yes	Yes	Yes
excessive improper trading	No	No	No	No	Yes

[31] Material breaches of client information will be reportable outside of the definition of serious misconduct, similar to cybersecurity incidents.

engaging in Dealer Member related activities outside the Dealer Member	No	Yes	Yes	Yes	Yes
engaging in activities outside the Dealer Member contrary to section 2554	No	Yes	No	Yes	Yes
addressing conflicts of interest in a manner that is contrary to section 3111 or section 3112	No	No	No	No	Yes
engaging in personal financial dealings contrary to section 3115	No	Yes	Yes[32]	Yes	Yes
materially violating the suitability determination obligation in Rule 3400	No	No	Yes[33]	Yes	Yes
breach of client confidentiality	No	Yes	No	Yes	Yes
Any other instance of material non-compliance with CIRO requirements, securities laws or any applicable laws	No	No	No	No	Yes

[32] Referred to as "inappropriate financial dealings" under the IDPC Complaint Requirements.
[33] Referred to as "unsuitable investments" under the IDPC Complaint Requirements.