

August 12, 2024

Submitted via Email

Attention: Member Regulation Policy
Canadian Investment Regulatory Organization
Suite 2600 40 Temperance Street
Toronto, Ontario M5H 0B4
E-mail: memberpolicymailbox@ciro.ca

Dear CIRO,

RE: DERIVATIVES RULE MODERNIZATION PHASE 1; CIRO RULE CONSOLIDATION PHASE 3 AND 4

We are writing to advise of key operational concerns that have arisen during implementation of Derivatives Rule Modernization Phase 1, to advise of their impact and to propose resolutions for your consideration. They are as follows:

i) Pre-approval

Proposed Rule 2246 (3) regarding a Dealer Member's Notice of Changes which also formed part of CIRO's most recent Rule Consolidation Phase 3 consultation provides:

(3) A Dealer Member must notify in writing and receive written approval from the Corporation before:

- (i) offering retail clients any highly leveraged securities or derivatives
- (ii) offering retail clients previously approved highly leveraged securities or derivatives that are to be based on a new underlying interest.

Highly leveraged securities or derivatives are undefined and subject to differing interpretations. We appreciate they may include leveraged and inverse ETFs, but the language remains overly broad.

In addition, the investor protection concerns proposed Rule 2246(3) seeks to address are already addressed in multiple ways by CIRO through rules, guidance, and audits. With non-exhaustive reference to Investment Dealer and Partially Consolidated Rules only, concerns are addressed, for example, through: Options Accounts (3252 – 3256); Futures Contracts and Futures Options Accounts (Rules 3257 – 3261); Discretionary Accounts and Managed Accounts (Rules 3270 – 3281); Supervision of Retail Client Accounts including suitability determinations (Rules 3945 – 3948) and Part B General Internal Control Requirements (Rules 4220 – 4225).

In CIRO Rule Consolidation, Phase 3, we recommended that the above rule be simplified and rephrased in a manner reflective of several pre-existing regulatory obligations as follows:

A Dealer Member *not previously approved for margin accounts* must notify in writing and receive written approval from the Corporation *before offering clients leverage*.

We ask that the proposed revisions above be applied to Derivatives Rule Modernization, Phase 1. Alternatively, should CIRO prefer additional time to consider, we ask that proposed rule 2246(3), which extend beyond derivatives, be excluded from Derivatives Rule Modernization Phase 1, while CIRO continues to review Rule Consolidation.

ii) Cumulative Loss Reporting

The additional provisions at Rule 3252(2) state:

The client's cumulative loss limit under clause 3252(1)(vii)

- (i) Applies to an account where the transactions involve futures contracts, forward contracts, contracts for difference, futures contracts options or similar derivatives or highly leveraged securities or derivatives
- (ii) Applies to an account, other than a hedging account, whether the account is an advisory account, a discretionary account, a managed account, or an order execution only account and
- (iii) Must, notwithstanding obligations under 3400 be determined on
 - a. A lifetime basis and validated with the client on an annual basis
 - b. An annual basis and updated monthly.

Please see prior comments regarding "highly leveraged securities or derivatives."

In addressing implementation for Derivatives Rule Modernization, Phase 1, the operational difficulty posed by proposed cumulative loss limits in additional Rule 3252(2)(i)(ii) and (iii) which include, but extend beyond derivatives, has become evident.

The resulting regulatory and administrative burdens-imposed risks dealers opting not to sell the impacted futures contracts, derivatives, or securities, limiting investor choice for those who satisfy suitability requirements, where applicable, and for order execution only investors.

In light of the above, and as CIRO's Rule Consolidation is ongoing, we ask that the additional provisions of Rule 3252(2) be reconsidered for comment in Phase 4.

Due to current implementation deadline, we ask that you kindly advise by month's end.

Respectfully submitted,

Investment Industry Association of Canada

Per : Laura Paglia, President & CEO

cc. P. Devault