FAIR Canada Canada's Investor Rights Advocate | Promoteur des droits des investisseurs

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Re: Canadian Investment Regulatory Organization (CIRO) Rule Consolidation Project – Phase 5 (the Proposal)

FAIR Canada is pleased to provide comments in response to the above-referenced Proposal.

FAIR Canada is a national, independent, non-profit organization known for balanced and thoughtful commentary on public policy matters. Our work includes advancing the rights of investors and financial consumers in Canada through:

- Informed policy submissions to governments and regulators
- Relevant research focused on retail investors
- Public outreach, collaboration, and education
- Proactive identification of emerging issues.[1]

A. Overview

We generally support the goals of the phase 5 consolidation project, which aims to harmonize rules for investment and mutual fund dealers.

[1] Visit www.faircanada.ca for more information.

However, we are disappointed that CIRO has not prioritized investor protection more within the project's scope. Instead, CIRO's stated objectives are limited to:

- Achieving greater rule harmonization by ensuring that similar dealer activities are regulated similarly and minimizing regulatory arbitrage between investment and mutual fund dealers,
- Adopting more principles-based rules, and
- Improving access to and clarity of the rules.

Some of these objectives may indirectly benefit investors, but they fail to place their interests at the forefront. Given its public interest mandate, it is regrettable that CIRO did not approach this project as an opportunity to raise standards where appropriate, rather than merely an exercise of choosing between two existing sets of rules.

1. The Proposal Fails to Enhance and Harmonize Complaint Handling

CIRO's proposed approach to complaint handling exemplifies the lack of focus on investors. We are disappointed that the Proposal (a) fails to harmonize with established best practices that CIRO previously consulted on,[2] and (b) will create a fragmented complaint-handling system for investors across Canada. This is a significant missed opportunity for CIRO to address a known gap, which should be rectified in the final Dealer Consolidated Rules (DC Rules).

We appreciate that the Proposal introduces some improvements, such as prohibiting the use of misleading terms (e.g., "ombudsman") for a dealer's internal dispute resolution service (IDRS) and mandating plain language in the acknowledgment and response letters. However, these changes fail to address the bigger and more fundamental issues–lengthy timelines, unequal standards and confusing procedural layers that wear clients down.

The Proposal also overlooks a crucial opportunity to create a single, national standard for complaint-handling timelines and processes by harmonizing with the Autorité des marchés financiers' (AMF) new complaint-handling regulation (AMF Regulation).[3] The AMF Regulation raises the bar for investor protection by reducing the timeframe for dealers to respond to client complaints. This timeline includes all internal escalation processes.

The new timelines were introduced to address the problem of clients abandoning their complaints or accepting unsatisfactory outcomes because they are tired of waiting and want to move on. The improvements in the AMF Regulation also mirror new and improved standards for federally regulated financial institutions, which now require banks to provide a substantive response to consumers well below the 90 days in the Proposal.[4]

As a self-regulatory organization with a public interest mandate, CIRO must promote investor protection through, among other things, high standards of conduct among its members. It is,

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[2] The Investment Industry Regulatory Organization of Canada (IIROC), CIRO's predecessor, published a consultation on January 13, 2022 that included complaint-handling requirements. These proposals were withdrawn after CIRO was formed, and their content was to be integrated into the current Phase 5 proposals [IIROC Consultation].
[3] AMF, Regulation Respecting Complaint Processing and Dispute Resolution in The Financial Sector, which comes into force on July 1, 2025.
[4] Bank Act s.627.43(1)(a), Financial Consumer Protection Framework Regulations, s. 14.

therefore, disappointing that CIRO has opted not to align with these well-known best practices and forgo an opportunity to enhance investor protection regarding complaint handling.

Harmonizing would also simplify the complaint process for consumers and dealers by creating consistent standards, regardless of the type of financial product or where the consumer or dealer is located. It would also ease the stress and burden on complainants, who often feel vulnerable and overwhelmed when navigating different processes.

We provide further details on our concerns beginning in Section B below.

2. The Proposal Introduces Unnecessary Complexity and Subjectivity for Complaint Handling

The Proposal introduces unnecessary complexity by creating two new defined terms: "serious misconduct" and "serious client-related misconduct." These definitions are intended to help dealers determine which complaints are subject to the full complaint-handling requirements in sections 3755 to 3759 of the DC Rules and which ones must be reported to CIRO.

However, both terms inject a high degree of subjectivity into the process. Each dealer will have to analyze whether activities not explicitly listed as "serious misconduct" create a material risk of harm. This subjective materiality element opens the door to varying interpretations and inconsistent application among dealers. It also introduces challenges for compliance and oversight. Dealers and CIRO may have difficulty assessing what is material, increasing compliance costs and complicating enforcement efforts.

CIRO could and should avoid this added complexity and ambiguity by:

- Adopting and harmonizing with the approach in the AMF Regulation and Mutual Fund Dealer (MFD) Rules, which exclude complaints that can be resolved informally or within a short period (e.g., 20 days) from the full complaint-handling requirements, and
- Maintaining, with a minor enhancement, the approach in the Investment Dealer and Partially Consolidated (IDPC) Rules that excludes service complaints from the reporting obligations to CIRO.

We elaborate on our recommendations in this area further in Section D below.

3. Uninvested Client Cash and Use of Free Credit Client Cash

We are disappointed that the Proposal does not go further to ensure clients are fully informed about the implications of dealers using free credit client cash (FCCC), including whether dealers will share income generated from FCCC. Moreover, the lack of a requirement for dealers to obtain clients' explicit consent before using FCCC in their business operations may expose clients to risks without their full awareness or understanding. This is contrary to principles adopted by the International Organization of Securities Commissions in its report on protecting client assets (the IOSCO Report).[5]

[5] IOSCO, Recommendations Regarding the Protection of Client Assets - Final Report, January 2014

We recommend that dealers be required to (i) provide clear, plain disclosure about the implications of using FCCC, including information about any interest payments to clients, (ii) obtain their clients' agreement to the dealer using FCCC in its business operations, and (iii) provide clients with prescribed disclosure about FCCC and uninvested cash.

These recommendations are consistent with:

- The client-focused reforms (CFRs), which emphasize putting clients' interests first,
- The duty of care in securities laws for firms to deal fairly, honestly, and in good faith with their clients, and
- CIRO's public interest mandate.

Section J below expands on our concerns and recommendations in this area.

Where we are responding to a specific question in the Proposal, we indicate as such in a footnote. In addition, we comment on other aspects of the proposed DC Rules that are not the subject of specific questions.

B. Time Limit to Provide a Substantive Response Letter[6]

We are disappointed that the Proposal perpetuates the longer 90-day timeline for dealers to resolve complaints, despite dealers in Québec being subject to a shorter 60-day timeline. This approach undermines CIRO's public interest mandate, and is contrary to a key objective of the consolidation project–to achieve rule harmonization by ensuring that similar dealer activities are regulated similarly.

In the banking sector, an in-depth Financial Consumer Agency of Canada (FCAC) review of complaint handling (the FCAC Review) found that lengthy resolution timelines are a key cause of attrition (i.e., consumers abandoning complaints that could have been brought to the Ombudsman for Banking Services and Investments (OBSI)).[7] Data from OBSI supports this assertion. It revealed a 248% increase in OBSI banking cases from 2022 to 2023. OBSI attributed this surge to the Financial Consumer Protection Framework, noting that the changes reduced attrition, leading to more complaints escalating to OBSI.[8]

The FCAC Review also found that delays in resolving complaints hinder fair resolutions. Prolonged complaint-handling processes tend to make it more difficult for the bank to find solutions that satisfy consumers. Moreover, when complaint handling takes too long, consumers may feel compelled to accept partial or unfair resolutions to their detriment.[9]

Delays may also discourage consumers from filing complaints altogether, leading to under-reporting and leaving systemic issues unaddressed. During the complaint-handling process, firms deal with individuals at their most vulnerable. Lengthy resolutions not only risk financial harm but also contribute to undue stress and anxiety, undermining trust in the system.

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[6] This section responds to Question 4 in the Proposal.
[7] FCAC, Industry Review: Bank Complaint Handling Procedures, February 19, 2020, at 22.
[8] OBSI, OBSI 2023 Annual Report Released, March 15, 2024.
[9] FCAC Review, *supra* note 7, at 22.

The FCAC Review also highlighted that the 90-day period is relatively generous by international standards.[10] The Department of Finance underscored that the shorter timeframe was intended to align Canada with global best practices for handling banking complaints.[11] Notably, firms regulated by the UK Financial Conduct Authority (FCA) must address complaints within eight weeks (56 days),[12] while in Australia, firms have 30 days to respond.[13]

The FCAC Review's findings are also reflected in the AMF Regulation. Beginning July 1, all members operating in Québec will be required to respond to complaints within 60 days, except in exceptional circumstances.

Given these developments and IIROC's prior consultation on complaint handling,[14] we would expect the Proposal to adopt the 60-day timeframe. It is indefensible for CIRO to maintain a 90-day response timeframe when a much shorter standard applies in Canada's banking sector and for dealers in Québec. If Québec-based dealers can provide a final decision to clients within these timelines, there is no rationale for their counterparts elsewhere requiring more time. By aligning with this standard, CIRO would fulfill its public interest mandate to protect investors and require its members to follow best practices.

Harmonizing with the AMF Regulation would also create a level playing field and ensure equal treatment of complainants. As one industry comment letter highlighted, inconsistent resolution timeframes across jurisdictions might lead firms to prioritize Québec complaints over others, creating unfairness.[15] Harmonization would make it easier for consumers to navigate complicated, fragmented complaint-handling processes by creating a unified response period. Additionally, it would help reduce attrition by providing more efficient complaint handling, boosting investor trust in financial institutions and the regulatory system.

C. Time Limit for Internal Dispute Resolution Services[16]

FAIR Canada also has serious concerns that the Proposal gives dealers additional time for their IDRS process beyond 90 days.[17] This additional process could result in clients waiting 120 days or more to receive a final and determinative decision. This is more than twice the timeframe in Québec and under the Bank Act. This is because both frameworks' 56- or 60-day timelines include any internal review or escalation processes they may offer their clients.

This issue is further compounded by s. 3756(5)(ii) of the DC Rules, which lacks a clear timeframe for the IDRS to issue its decision. The rule states that where the IDRS received the complaint after the substantive response letter, it has 30 days from the date it received the complaint to provide its final decision. Our concern is that the timing of the final decision is contingent on when the IDRS receives the complaint. However, dealers are not obligated to transfer the complaint to

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[10] Ibid., at 20.
[11] Fasken Martineau DuMoulin LLP, The Wait Is Over: Federal Government Releases Regulations For Financial Consumer Protection Framework, August 25, 2021.
[12] Financial Conduct Authority Handbook, s. DISP 1.6.2.
[13] Australian Securities & Investments Commission, Regulatory Guide 271 – Internal Dispute Resolution, September 2021, RG 271.56.
[14] IIROC Consultation, *supra* note 2.
[15] Fidelity Investments Canada ULC, Comment Letter on AMF Regulation, at 2.
[16] This section responds to Question 5 in the Proposal.
[17] DC Rules, s. 3756(5).

the IDRS within a defined period. This lack of urgency could create undue delays for complainants beyond 120 days, while the time limit for escalating to OBSI continues to run.

We believe CIRO should adopt a similar approach to the AMF Regulation. In short, dealers should only have 60 days to resolve complaints to the client's satisfaction, including any IDRS process offered to the client.

The Proposal is also concerning because the IDRS acts as a parallel second phase that diverts complaints from OBSI. It may confuse clients and obscure the fact that they can go to OBSI within the specified timeline after initiating their complaint.

As far back as 2017, the Canadian Securities Administrators (CSA) flagged issues with this two-stage process in a Staff Notice. Specifically, they noted that:

- Fair and effective complaint handling means avoiding potential client confusion, yet the IDRS risks confusing clients or causing them to conflate the IDRS with OBSI,
- Investors may abandon their claims due to exhaustion from the extended process or accept inadequate settlements they might not have taken had they gone directly to OBSI after receiving the firm's decision,
- The 180-day deadline for escalating complaints to OBSI continues to run during the IDRS process, putting investors at risk of losing access to this option, and
- Similarly, the statutory limitation period for pursuing legal action runs during the IDRS process, further disadvantaging clients.[18]

The complexity of dealer disclosures concerning IDRS and OBSI worsens the problem. FAIR Canada staff reviewed a sample of these disclosures and found that they can be lengthy and unclear, and fail to adequately inform investors of their rights or when they can involve OBSI.

D. Definition of "Serious Misconduct"[19]

1. When do the Full Complaint-Handling Requirements Apply to Verbal Complaints?

Dealers receive a broad spectrum of complaints, ranging from minor grievances to significant issues that may indicate serious problems. The challenge lies in distinguishing and appropriately addressing these complaints to ensure compliance with regulatory standards while protecting client interests.

The Proposal makes it clear that written complaints are subject to the full complaint-handling requirements in sections 3755 to 3759 of the DC Rules. However, when a verbal complaint concerns conduct that is not enumerated in the list under "serious misconduct," dealers will have to assess whether it is material before applying the complaint handling requirements. In short, it introduces a subjective materiality assessment for verbal complaints.

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[18] Joint CSA Staff Notice 31-351, IIROC Notice 17-0229, MFDA Bulletin #0736-M – Complying with Requirements regarding the Ombudsman for Banking Services and Investments, December 7, 2017.

[19] This section responds to Question 2 in the Proposal.

This approach presents significant complexity for determining whether the comprehensive complaint-handling rules apply, as materiality assessments are inherently nuanced and subjective. This increases the risk of inconsistent interpretations across dealers, resulting in unequal treatment of complainants. Moreover, dealers' perspectives could differ markedly from those of clients. This subjectivity may result in some verbal complaints being inappropriately excluded from the full complaint-handling process, jeopardizing the equitable application of the rules. This ambiguity also opens the door to disputes and confusion.

Instead, CIRO should opt for a more straightforward, transparent approach. The AMF Regulation and MFD Rules are instructive, as they offer simpler alternatives which are easier to apply in practice. Under the AMF Regulation, complaints that can be resolved within 20 days are subject to less onerous complaint-handling requirements. Similarly, under the MFD Rules, complaints that can be resolved informally are excluded from the full complaint-handling requirements.

CIRO should create a bright-line test along these lines rather than rely on a subjective materiality assessment. For example, the complaint-handling requirements would not apply to verbal complaints that can be resolved informally within 20 days. We also recommend that CIRO adopt this approach for written complaints. If so, it might alleviate some burden for dealers.

This approach would be consistent with existing frameworks and offer the advantage of greater clarity and ease of implementation. It would also streamline the process and promote consistency and equity in complaint resolution.

2. When does a Dealer Have to Report a Complaint to CIRO?

We are concerned that the subjective materiality threshold in the definition of "serious misconduct" could also narrow the reporting of complaints, complaint outcomes, disciplinary actions, and other important information to CIRO. For example, dealers must report the following to CIRO:

- Complaints involving allegations of: (i) serious misconduct against the dealer, or any current or former approved person, or (ii) serious client-related misconduct against an employee while employed by the dealer,[20]
- The outcomes of client complaints alleging serious misconduct or serious client-related misconduct,[21] and
- The resolution of any disciplinary action against an approved person or employee involving allegations of serious misconduct.[22] This replaces dollar thresholds for reporting internal disciplinary actions in the IDPC Rules.[23]

This subjective materiality assessment opens the door to inconsistent and overly conservative interpretations for situations outside the prescribed list in the "serious misconduct" definition. Dealers may prioritize their reputational interests over transparency, potentially underreporting valid complaints and obscuring patterns of misconduct or systemic issues. For CIRO, it also

[20] DC Rules, s. 3711(2).
[21] DC Rules, s. 3711(3)(iii).
[22] DC Rules, s. 3711(3)(ii).
[23] IDPC Rules, s. 3703(2)(vi)(e).

creates challenges when monitoring compliance and holding dealers accountable for complying with the letter and spirit of the reporting requirements.

To foster greater consistency and transparency, CIRO should retain the more objective reporting framework under the IDPC Rules, which requires dealers to report all client complaints other than service complaints.[24] We recommend, however, that CIRO enhance this framework by adopting the definition of service complaint from the MFD Rules. Specifically: "(i) any complaint by a client which is founded on customer service issues and is not the subject of any securities legislation or regulatory requirements; or (ii) any complaint by a client as a result of a good faith trading error or omission."[25]

E. Complaint Policies & Procedures – Addressing Systemic Issues

The Proposal introduces some revisions to dealers' complaint policies and procedures requirements. Unfortunately, the changes fall short of fully addressing concerns around systemic issues that may come to light through one or more complaints.

For example, the Proposal only requires dealers to include "procedures to monitor the general nature of the complaints."[26] We assume this is intended to require a dealer to monitor all complaints, presumably to identify patterns that may point to systemic issues or more serious problems.

CIRO's approach contrasts sharply with the AMF Regulation, which specifically requires a dealer's complaints policy to include measures to gain a comprehensive view of complaints, and to identify the common causes and address the issues such complaints raise.[27] We believe CIRO should include a similarly clear and specific obligation in the final DC Rules.

Proposed DC Rule 3753(2) also seeks to reinforce the notion that a dealer ought to take action when it determines that the number, frequency or severity of complaints may indicate a serious problem. However, that obligation is limited to: "consider whether it is fair and reasonable for the Dealer Member to undertake proactively a redress or remediation exercise." It does not require dealers to take action, but only to consider whether it would be fair and reasonable to do so.

We believe this provision should be revised to make it clear that:

- A dealer must review complaints to ascertain potential systemic issues, and
- When it determines that more than one client is affected, it must take action to address the issue(s) impacting those clients.

This approach is based on the AMF Regulation.[28] It would address concerns around the subjective nature of whether it is "fair and reasonable." As long as another client is impacted, the dealer would have to take action to address the issue. Finally, harmonizing the rules for dealers operating both inside and outside Quebec would be more consistent with the project's objectives.

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[24] IDPC Rules, s. 3703(2)(i).
[25] MFD Rules, Rule 600 – Information Reporting Requirements, s. 2.
[26] DC Rules, s. 3753(1)(vii).
[27] AMF Regulation, s. 10.
[28] AMF Regulation, s. 13.

This approach is also consistent with the FCAC's Guideline on Complaint-Handling Procedures for Banks and Authorized Foreign Banks. The Guideline makes it clear that banks must have policies in place for identifying and remedying any recurring or systemic problems, and for providing redress and reimbursement to all clients affected by a complaint.[29]

The absence of a clear systemic issues mandate in the DC Rules undermines fairness and accountability. It also creates a lower standard for dealers operating outside Quebec. Without a clear obligation to address such issues, dealers outside Quebec may overlook patterns of harm, leaving many clients without recourse simply because they did not formally raise a complaint. This approach risks eroding trust among investors and detracts from the industry's ability to promote a culture of putting clients' interests first.

We strongly urge CIRO to strengthen the DC Rules by imposing a concrete requirement for dealers to act when they identify systemic issues. This should include addressing the root causes of recurring complaints, implementing corrective measures, and addressing issues for all impacted clients, including any needed redress or reimbursement.

F. Complaint Drafting Assistance

A new provision in the DC Rules requires dealers to provide complaint drafting assistance to any complainant who expresses a need for it.[30]

While this is a positive step, CIRO could strengthen its approach by mirroring the AMF Regulation. The AMF's rule obligates firms to take the necessary actions to understand what clients are communicating to them and to assist with complaint filing when necessary.[31] In contrast, CIRO's approach is reactive; it requires clients to express a need for help before dealers act.

Proactively offering assistance upfront ensures that all clients, not just those who explicitly request help, receive the support they need. This approach would reduce barriers for clients lacking the expertise or confidence to articulate their complaints, thereby fostering trust and fairness. It would help level the playing field between dealers and clients and enhance investor confidence as they navigate the complaint resolution process.

G. Plain Language and Accessibility

Clear and accessible communication is essential for empowering investors, especially during complex complaint-handling processes. We are pleased that the DC Rules introduce new requirements for using plain language in acknowledgement and response letters. In addition, these documents must be in readily accessible and understandable formats.[32]

The requirement for dealers to provide clear, plain-language disclosure of the approved ombudsman service is a positive step toward removing barriers that could discourage clients from seeking OBSI's assistance.[33] As noted above, FAIR Canada staff reviewed some of this disclosure and found that it can be complex and challenging for the average retail investor to

[29] FCAC, Guideline on Complaint-Handling Procedures for Banks and Authorized Foreign Banks, see sections 21 to 24.
[30] DC Rules, s. 3752(5).
[31] AMF Regulation, s. 12.
[32] DC Rules, s. 3755(2) and s. 3756(2).
[33] DC Rules, s. 3759(4)(ii).

grasp. Given the importance of disclosing the approved ombudsman service, CIRO should consider prescribing this disclosure based on behavioural research with retail investors.

Moreover, we recommend that CIRO align with the AMF Regulation and expand its plain language requirements. In addition to requiring complaint-related documents to be clear, readable, specific, and not misleading, the AMF Regulation requires staff to use clear, plain language in *all* complainant interactions.[34] This comprehensive approach would help clients navigate the complaint resolution process more confidently. Clients would feel more supported and empowered, which, in turn, would strengthen their trust in the industry.

Additionally, CIRO should require dealers to make complaint-handling documents easy to locate on their websites, reducing the burden on clients who might otherwise struggle to find critical information.

H. Definition of Complaint[35]

Consistent with the MFD Rules, we believe the definition of complaint should include prospective clients and limit such clients to those who have dealt with a dealer member or approved person.[36]

Recognizing complaints from prospective clients would encourage responsible and professional conduct at the earliest touchpoints with potential clients. It would also ensure that complaint-handling processes address the whole client experience, not just once an account has been opened or a service provided.

Prospective clients may have legitimate concerns, such as misleading disclosures regarding fees, services, or risks; discriminatory or unfair treatment, such as unjustified denial of service; or unauthorized use or sharing of their personal information during the pre-account phase. Incorporating prospective clients into the definition of a complaint would build greater trust in the financial system, allowing individuals to voice concerns even before becoming customers. Moreover, it aligns with CIRO's mandate to protect investors, including potential clients of member firms, and promotes responsible market conduct.

Lastly, our recommendation aligns with the Bank Act and OBSI's Terms of Reference, which both encompass complaints from individuals dissatisfied with the offering or handling of financial services, whether or not they become customers.[37]

I. Confidentiality Restrictions

We support the clarification in the DC Rules that a dealer must not impose confidentiality or similar restrictions on clients through a release or otherwise.[38] Including the phrase "or otherwise" ensures that dealers cannot impose restrictions in contexts beyond formal releases.

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[34] AMF Regulation, s. 11.
[35] This section responds to Question 1 in the Proposal.
[36] MFD Rules, Rule 300 - Complaint Handling, Supervisory Investigations and Internal Discipline, s. 2.
[37] Bank Act, s. 627.01(1); OBSI Terms of Reference, effective June 16, 2022.
[38] DC Rules, s. 3731.

Additionally, we support the new provision in the DC Rules prohibiting dealers from preventing clients, through a release or otherwise, from sharing information with securities regulators or enforcement authorities.[39]

These expanded measures strengthen investor protection and foster trust in the regulatory system by allowing clients to communicate openly with authorities. Furthermore, they help ensure regulators receive complete, unfettered information, which is crucial for effective oversight and public confidence in the financial markets.

J. Uninvested Client Cash and Use of Free Credit Client Cash

Under the MFD Rules, mutual fund dealers must segregate all client cash in a trust account with a financial institution.[40] In contrast, investment dealers can use their clients' uninvested cash up to a certain prescribed limit for business purposes. They must invest any excess above the limit in short-term securities, or segregate it and hold it in trust with an acceptable financial institution.[41]

We are concerned that the proposed requirements regarding uninvested client cash, whether held in trust at a financial institution, invested in short-term securities, or used as FCCC, are insufficient.

1. Disclosure of Interest on Uninvested Cash Held in Trust

CIRO proposes not to carry over MFD Rule 3.3.2(e) to the DC Rules. This provision requires mutual fund dealers to disclose whether clients' uninvested cash held in trust will earn interest, the applicable rate, and to provide at least 60 days' written notice of any rate changes.

While the 60-day prior written notice may have disincentivized competitive rate setting, we do not view this as a sufficient reason to dispense with the disclosure entirely. Dealers should inform clients whether they will be paid interest on any uninvested cash held in trust.

In this regard, client account statements should include information on the interest earned from uninvested cash, specifying the applicable rate during the reporting period. Providing such transparency empowers clients to evaluate their dealer's services and make informed decisions, such as transferring their accounts to firms offering more competitive returns on uninvested cash awaiting future investment.

2. Requirements Regarding Uninvested Cash Used as FCCC

FAIR Canada recommends that dealers using FCCC be required to (i) provide clear, plain disclosure about the implications of using FCCC, including information about any interest payments to clients, (ii) obtain their clients' agreement to use FCCC in their business operations, and (iii) provide clients with prescribed disclosure about FCCC and uninvested cash.

(i) Improve the disclosure regarding the use of FCCC

[39] DC Rules, s. 3731(1)(iv).
[40] MFD Rules, s. 3.3.2.
[41] IDPC Rules, s. 4381, DC Rules, s. 4381.

Under the DC Rules, a dealer that uses FCCC must write the following or an equivalent on all client account statements:

> Any free credit balances represent funds payable on demand which, although properly recorded in our books, may not be segregated and may be used in the conduct of our business.[42]

This statement is problematic, particularly from the perspective of an average client. Many retail investors will not appreciate the implications of their uninvested cash not being segregated and held in trust. Moreover, the statement fails to explain how FCCC is used in the dealer's business, the risks that may flow from that use, or the fact that the dealer can directly profit from using a client's uninvested cash.

We believe these issues should be addressed in a plain-language version of the proposed statement. In addition, the statement should make it clear whether the dealer intends to share any profits it makes and, if so, how much, with its clients. Finally, we recommend that the revised version be tested for comprehension with everyday investors.

Our recommendation is consistent with the principles established in the IOSCO Report. Principle 5 emphasizes the importance of clarity and transparency in disclosing arrangements for protecting client assets and the associated risks. It notes that "[a]ny required disclosure should be in writing and prepared in clear, plain, concise and understandable language. Legal or financial jargon not commonly understood should be avoided."[43]

(ii) Obtain client consent prior to using FCCC

As noted above, CIRO will require members to disclose their use of uninvested client cash in their business operations. However, the Proposal does not require dealers to obtain the client's express consent before doing so. We believe the Proposal should include such a requirement as part of the account opening process (see the proposed disclosure in (iii) below). In addition, the account statements should remind clients that they can consent to the dealer using their uninvested cash as FCCC and opt out at any time.

An existing precedent in the IDPC Rules requires client consent to use their property. IDPC Rule s. 4312 provides that a dealer cannot use securities or precious metals bullion held in segregation for its own purposes without the client's express written approval.

Moreover, Principle 6 of the IOSCO Report reaffirms the importance of clients providing their explicit consent when waiving or modifying protections or opting out of the client asset protection regime.[44] Permitting dealers to exploit FCCC in their business operations appears to be a uniquely Canadian deviation from typical client protection practices in other countries. This underscores the importance of allowing clients to decline dealer use of their FCCC.

[42] DC Rules, s. 4383(1)(ii).
[43] IOSCO Report, *supra* note 5, at 6.
[44] Ibid.

Principle 6 also makes it clear that the client should be provided with clear and understandable disclosure regarding the implications and risks of giving such consent.[45] As noted above, we do not believe those implications or risks are clear in CIRO's proposed disclosure.

(iii) Prescribe disclosure about FCCC and uninvested cash

For dealers that use FCCC, we recommend that CIRO require clear, plain, prominent disclosure in the account opening documents addressing the following points:

- How uninvested cash is handled, including that dealers may use FCCC in their business operations,
- FCCC is not segregated in trust with a financial institution,
- The dealer may be able to use FCCC in its business and earn income from it,
- The dealer's responsibilities and the associated risks of using FCCC,
- Statements that the dealer is not obligated to pay interest on uninvested cash, but if it does, it will disclose the amount and rate,
- Consistent with Principle 6 in the IOSCO Report, the dealer cannot use the investor's FCCC unless the investor agrees.

Below, we provide a sample of how such disclosure could be presented for illustration purposes. However, we recommend that CIRO conduct behavioural research with retail investors to identify the most effective, comprehensible wording to include in account opening documentation.

Sample Disclosure Wording

What Happens to Uninvested Cash in Your Account

When you have uninvested cash in your account, we may:

1. **Hold it in trust**: Uninvested cash may be segregated and held in trust at a financial institution. "Segregated" means the cash is kept separate from our own funds and business operations. We may earn interest on cash held in trust. We are **not obligated to pay you interest** on cash held in trust. However, if we pay interest, we will let you know the amount of interest earned, including the interest rate.

2. **Invest it in short-term securities**: Uninvested cash may be invested in short-term securities with a maturity of one year or less, such as bonds, treasury bills and Canadian bank paper. We may earn interest when your cash is invested in short-term securities. We are **not obligated to pay you interest** on cash invested in short-term securities. However, if we pay interest, we will let you know the amount of interest earned, including the interest rate.

3. **Use it in our business**: Uninvested cash may be classified as a "free credit balance." We may use free credit balances in our business—for example, by lending it to other clients, or using it to fund our day-to-day operations—and may earn income from doing so. Free credit balances are not segregated in trust with a financial institution. We will not use your uninvested cash as a free credit balance in our business operations

[45] Ibid.

unless you agree. We are **not obligated to pay you interest on free credit balances**. However, if we do pay interest, we will let you know the interest rate and notify you if the rate changes.

We have a responsibility to manage uninvested cash carefully, and there are rules we must follow to protect your interests. However, there are still some risks associated with our use of free credit balances. For example, if we face financial difficulties, your access to your free credit balances could be delayed or impaired.

We will provide you with a consent form regarding the use of your uninvested cash as a free credit balance in our business operations. If you give your consent, you may opt out at any time if you change your mind. [*Include instructions about how the client can opt out.*]

The proposed disclosure aligns with the CFRs, which emphasize putting clients' interests first, and the duty of care in securities laws for firms to deal fairly, honestly, and in good faith with their clients.

3. Compliance Review of Uninvested Cash and FCCC Practices

We suggest that CIRO also conduct compliance reviews of dealers' practices regarding the payment of interest on uninvested cash. Such reviews would help ensure that dealers are adhering to the CFRs and fulfilling their duty of care.

The FCA's "Dear CEO" letter[46] highlighting concerns about handling interest on customer cash balances provides valuable insights CIRO could incorporate into its compliance efforts. The FCA raised issues regarding practices such as "double dipping," where firms both retain interest and charge account fees on uninvested cash. Additionally, the FCA flagged the retention of disproportionately high interest percentages, which may indicate a lack of good faith and failure to deliver fair value to clients. The FCA emphasized that firms must ensure their interest retention practices align with the principles of fairness and transparency. Compliance reviews in this critical area would safeguard consumer interests and reinforce accountability among dealers.

4. Allowing Level 3 Mutual Fund Dealers to use FCCC[47]

To ensure investor protection and promote fairness, it is important to address the concerns posed by allowing Level 3 mutual fund dealers to use FCCC under their current, less stringent regulatory framework.

Unlike Level 4 dealers, Level 3 dealers operate under lower minimum capital requirements ($75,000 compared to $200,000) and reduced insurance obligations. This disparity could increase the risk of errors and misuse of FCCC, as Level 3 dealers may lack the sophisticated systems, infrastructure, and controls to manage these funds responsibly. Given these shortcomings, Level 3 dealers should not be allowed to use FCCC. If they wish to do so, they should become Level 4 dealers.

[46] FCA, The Retention of Interest Earned on Customers' Cash Balances, December 12, 2023.
[47] This section responds to Question 7 in the Proposal.

We also support requiring mutual fund dealers that would like to use FCCC to notify CIRO in writing of their intentions and to undergo a thorough review to verify they have the requisite systems, controls, and capital.

K. Recordkeeping and Reporting Requirements in a Digital Age

The Proposal does not address recordkeeping and reporting requirements in today's rapidly evolving digital environment where new communication tools and platforms have transformed how business is conducted. We recommend that CIRO review and consult on its recordkeeping and reporting framework to ensure it keeps pace with innovation and continues to effectively protect investors.

In a recent consultation, the U.S. Financial Industry Regulatory Authority (FINRA) sought input on modernizing its rules to support emerging technologies.[48] It noted that the widespread adoption of digital communication channels, such as instant messaging and online meeting platforms, has introduced benefits but also created challenges around compliance, supervision, and record retention. FINRA also flagged concerns about "off-channel communications" on unauthorized platforms, which bypass recordkeeping systems and have already led to enforcement actions this year.[49]

Additionally, FINRA's consultation explores questions, such as how firms can effectively supervise off-channel communications and what unique challenges AI-generated content presents. These are critical issues for CIRO to address to ensure its framework reflects how businesses operate today and properly protects investors in a rapidly changing world.

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Thank you for considering our comments on this important issue. We welcome any further opportunities to advance efforts that improve outcomes for investors. We intend to post our submission on the FAIR Canada website and have no concerns with the regulators publishing it on their websites. We would be pleased to discuss our submission with you. Please contact Jean-Paul Bureaud, Executive Director, at jp.bureaud@faircanada.ca or Tasmin Waley, Policy Counsel, at tasmin.waley@faircanada.ca.

Sincerely,

Jean-Paul Bureaud
President, CEO and Executive Director
FAIR Canada | Canadian Foundation for Advancement of Investor Rights

[48] FINRA, Regulatory Notice 25-07 - Supporting Modern Member Workplaces, April 14, 2025.
[49] Securities and Exchange Commission Press Release - Twelve Firms to Pay More Than $63 Million Combined to Settle SEC's Charges for Recordkeeping Failures, January 13, 2025.