

**OVERSIGHT REVIEW REPORT  
INVESTMENT INDUSTRY REGULATORY  
ORGANIZATION OF CANADA  
QUÉBEC DISTRICT  
2010**

## TABLE OF CONTENTS

<b>A.</b>	<b>BACKGROUND .....</b>	<b>1</b>
<b>B.</b>	<b>REGISTRATION .....</b>	<b>1</b>
	1. Introduction .....	1
	2. Staffing and duties .....	1
	3. Benchmarks .....	2
	4. Tools .....	3
	5. Delegation of powers to the Approval Committee.....	4
<b>C.</b>	<b>MEMBERSHIP .....</b>	<b>5</b>
	1. Introduction .....	5
	2. Procedures .....	6

## **A. BACKGROUND**

The Autorité des marchés financiers (the “AMF”) inspected the registration and membership components of the Québec District of the Investment Industry Regulatory Organization of Canada (“IIROC”) in March and April 2010. The inspection complemented the inspection of other program components (such as Business Conduct Compliance, Financial & Operations Compliance, Complaints, Investigations and Enforcement) conducted in fall 2009 and for which the inspection report was issued on April 1, 2011.

As part of this second phase of the IIROC inspection program, the AMF’s inspection of the registration and membership components was conducted concurrently with the inspection of registration by the Ontario Securities Commission (the membership component was examined during the first phase of IIROC’s inspection) and the British Columbia Securities Commission in their respective Toronto and Vancouver regional offices.

## **B. REGISTRATION**

### **1. Introduction**

Registration is a separate aspect of the inspection program. The purpose of the program is to validate how IIROC, as a recognized self-regulatory organization, carries out its functions and powers and the extent to which it complies with its governing statutes and the decisions rendered by the AMF when determining a person’s skills or suitability for registration. In Order No. 2009-PDG-0100 handed down on August 19, 2009, the AMF delegated to IIROC all functions and powers relating to the registration of individuals.

The registration component covered the period from September 28, 2009 to February 28, 2010, to coincide with the coming into force of the registration reform and to give the inspecting regulators time to evaluate its implementation by IIROC.

The implementation of the registration reform, concomitant with the coming into force of *Regulation 31-103 respecting registration requirements and exemptions* (“Regulation 31-103”) and other related regulations, necessitated corresponding amendments to IIROC’s *Dealer Member Rules*. This entailed substantial activity for the Registration department, and the Montréal office staff was very involved in different initiatives, including the training of IIROC staff, Dealer Members and the various committees of the Québec District Council, as well as the publication of several Notices (including Frequently Asked Questions) designed to provide Dealer Members with guidance on issues involving the transition to the new registration regime.

### **2. Staffing and duties**

During the period covered, Registration staff for IIROC Québec District consisted of eight people — the manager of the Registration department, six Registration officers (four senior officers and two regular officers) and a Registration clerk. During this period, two persons resigned and were temporarily replaced. At the time this report was written, these two positions were vacant. During the three previous years, Registration staff levels remained unchanged.

According to the organizational chart, the Registration manager reports directly to the Director, Member Regulation of IIROC Québec District and consults the Vice-President, Registration and Complaints in Toronto. Her main duties consist in ensuring the continuity and consistency of the review of applications made by firms (as new Dealer Members or in situations where ownership of a Dealer Member changes, for example) and overseeing the work of Registration officers. She also provides the necessary support to develop or change registration procedures and methods and acts as a liaison with other IIROC departments, regional offices and securities regulators.

The senior Registration officers administer the laws and regulations regarding the approval of individuals for registration, paying particular attention to their competency, integrity and solvency. The regular Registration officers ensure that information is filed in the National Registration Database (the “NRD”) according to the appropriate procedure. The Registration clerk provides the necessary administrative support to the Registration department staff by keeping the registration files up-to-date.

### *Findings*

AMF staff is of the opinion that, notwithstanding the resignation of two persons during the period covered, the Montréal office Registration department has sufficient staff, staff is qualified and the department is adequately supervised.

### *AMF recommendations*

No action required.

## **3. Benchmarks**

Registration benchmarks are as follows:

- 80% of all applications received, not including transfer and registration exemption requests, must be approved or processed with the sending of an initial non-compliance letter to the registrant within five business days;
- regarding possible new members, a preliminary non-compliance letter must, where applicable, be filed and sent through the NRD within two weeks of receipt of a person’s registration application after being reviewed for compliance by management (in accordance with IIROC Dealer Member Rule 7 *Dealer Member Directors and Executives*).

In and of itself, registration is a detailed procedure characterized by a high volume of operations. During the period covered, a total of 2,830 applications were processed by the Montréal office Registration department, including 151 new registration applications, 1,060 amendment applications (change or surrender of individual categories) for individuals, 83 amendment applications involving a company (branch), 590 notices of amendment (in particular regarding employment) and 946 termination applications. In addition, 64 reinstatements of registration (also called “transfers of registration”) of individuals were processed; it is no longer necessary to record such operations because they are done automatically in accordance with Regulation 31-103.

According to statistics provided by IIROC, 74% of operations processed by IIROC's Montréal office relating to new registration applications, individual amendments and company amendments met the five business day approval period or, where applicable, processing times established to measure the Registration department's performance.

AMF staff identified and analyzed a sample of 42 files.

### *Findings*

During the first two months after the coming into force of Regulation 31-103, significant delays were observed in the processing of registration applications for individuals. This was considered reasonable in view of the significant changes related to registration reform. Furthermore, the NRD was inactive for two weeks at the time the registration reform was implemented. Applications filed during this period were processed manually. The situation has progressively improved and the performance benchmarks have been met since December 2009. Nonetheless, it is premature to make a judgment based on these benchmarks as the period covered is relatively short.

### *AMF recommendations*

No action required.

## **4. Tools**

The IIROC *Registration Operations Manual* was completely revised and updated in April 2010.

As with all IIROC departments, the tools used by the Registration department have been refined as computer processing is now used throughout the organization. The main computer systems used by the Registration department staff are the following:

- the NRD to file registrations of individuals working for a registered firm, a database in which Registration staff can take various regulatory actions (approve, refuse, withdraw, suspend or reinstate registration, impose or withdraw a condition, terminate an authorization and indicate a regulatory note);
- the ComSet complaints and settlement reporting system to validate information obtained in the case of customer complaints and disciplinary matters;
- the AS400 system to check the background of a registered individual or firm (e.g., regulatory action taken against the individual or firm).

### *Findings*

AMF staff has noticed that the NRD is very strict in terms of managing exemption applications which, in many cases, are related to registration applications. When a registration application must be re-entered in the NRD for some reason, the related exemption application must be cancelled and also re-entered. This problem is caused by the system configuration. AMF staff believes that this entails a loss of time for all NRD users, and in this case for IIROC staff and Dealer Members.

In fact, any point pertaining to the improvement of the NRD is discussed within regular meetings of a working group composed of system users who are representatives of IIROC and the Canadian Securities Administrators. This working group determines the changes required according to pre-established priorities.

*AMF recommendations*

No action required.

**5. Delegation of powers to the Approval Committee**

District Councils have powers relating to registration applications of individuals (approve, refuse, maintain, impose terms and conditions, revoke, suspend, etc.) set forth in IIROC Dealer Member Rule 20.18 *Corporation Hearing Processes* ("Rule 20"). According to subsections (1) to (3) of Rule 20.18, these powers may be delegated to a sub-committee of the District Council or to IIROC staff or, pursuant to subsection (4), to a sub-committee of the District Council.

The District Council of a geographic region may set up permanent sub-committees for different purposes, including a registration sub-committee. In Québec, the Approval Committee, a sub-committee of the Québec District Council, performs functions related to registration applications by individuals.

*Findings*

AMF staff has obtained the resolutions of the Québec District Council regarding the Approval Committee for the years 2007-2008, 2008-2009 and 2009-2010. As they should, these resolutions deal with the appointment of members to the Approval Committee. However, they do not systematically or expressly provide for the delegation of powers to the Approval Committee or IIROC staff which, in reality, performs them. By comparison with the resolution of the Québec District Council, we obtained the resolution respecting the delegation of powers to the registration sub-committee of several other IIROC District Councils for 2009-2010, renewing their previous resolution.

*AMF recommendations*

The Québec District Council resolution respecting the Approval Committee should provide for not only the appointment of members of the Approval Committee but also the delegation of powers in accordance with the related IIROC's *Dealer Member Rules*.

Priority – Medium

*IIROC's response*

The Québec District Council resolution respecting the Approval Committee was updated June 8, 2010 and includes the following two resolutions: (i) provision for the appointment of members of the Approval Committee; and (ii) provision for the delegation of powers related to IIROC's *Dealer Member Rules*.

*AMF comments and follow-up*

AMF staff are satisfied with the response obtained and will follow up this recommendation with IIROC.

*Findings*

District Councils have other powers described in Rule 20.24 respecting proficiency exemptions. However, this section of the Rule reads differently from section 18 of Rule 20 as the powers listed apply to the District Council or a sub-Committee of the District Council which may delegate them to IIROC staff.

In Québec, no powers are delegated to IIROC staff under Rule 20.24 as the Approval Committee grants or denies proficiency exemptions. AMF staff has obtained a draft resolution of the Québec District Council recognizing the Approval Committee as the sub-Committee of the District Council authorized to act pursuant to Rule 20.24.

*AMF recommendations*

The Québec District Council should obtain the resolution duly approved by its members identifying the sub-committee of the District Council authorized to act pursuant to IIROC Dealer Member Rule 20.24 *Corporation Hearing Processes*.

Priority – Low

*IIROC's response*

A resolution was passed on June 8, 2010 by the Québec District Council identifying the Québec Approval Committee as authorized by IIROC Dealer Member Rule 20.24.

*AMF comments and follow-up*

AMF staff are satisfied with the response obtained and will follow up this recommendation with IIROC.

**C. MEMBERSHIP**

**1. Introduction**

Registration as a dealer with a regulatory authority is a prerequisite for membership in IIROC. The permit of an applicant planning to carry on business in Québec is issued by the AMF.

Before a membership application is submitted to IIROC's Board of Directors for approval, it is carefully examined by staff of IIROC's Financial & Operations Compliance, Business Conduct Compliance and Registration departments. This examination includes an analysis of the information and documents filed, discussions with the applicant's technical and management staff, and a site visit to examine the premises and systems. When IIROC staff believes that the application meets the membership requirements, the application is sent to the District Council of the province where the applicant's head

office is located. The District Council then examines the application and, if it issues a favourable recommendation, the application is submitted to the Board of Directors for approval. The applicant is admitted as an IIROC member once administrative issues such as the payment of fees have been settled.

Other than the acceptance of new Dealer Members, the membership component of the inspection of IIROC Québec District includes the resignation, acquisition, change of control or ownership of a Dealer Member and amalgamation of Dealer Members. These changes are set forth in Article 3 *Conditions of Membership* of IIROC General By-Law No. 1 as well as in Rule 5 *Ownership of Dealer Member Securities*, Rule 6 *Dealer Member Holding Companies, Related Companies and Diversification* and Rule 8 *Dealer Member Resignations, Amalgamations, etc.* of IIROC's *Dealer Member Rules*.

The period covered for the inspection of the membership component is September 1, 2006 to February 28, 2010.

## **2. Procedures**

The manual used by IIROC for the membership component is entitled *General Counsel's Office Membership Policies & Procedures*, the most recent version of which is dated September 29, 2009. It describes membership procedures to be followed by staff of the various IIROC departments, IIROC management, the relevant District Councils and the Board of Directors. It gives an approximate schedule for each step of the approval procedure, which depends on several contingencies, including missing information in the supporting documents filed and Board meeting dates. On average, the time spent examining an application filed by a firm is approximately four months.

The computer tools used to store membership information are the SharePoint portal, which is similar to a national on-line library, and UBSS, a file tracking management software system.

Staff at IIROC's Montréal office did not have to deal with new dealer memberships during the period covered. However, it examined several cases of shareholding changes and amalgamations for which it had to make a recommendation to the Québec District Council, which had to deal with about 24 files related to diverse transactions involving one or several Dealer Members during the period covered.

AMF staff examined a sampling of two files: one relating to the amalgamation of two IIROC members and another one involving the acquisition of a significant interest in a Dealer Member. AMF staff's findings further to its examination of these two files are set forth below.

### *Findings*

Although the amalgamation file has a great deal of analyses explaining a complex transaction, supported by several legal documents, it is not complete. AMF staff did not find any information exchanged between the relevant IIROC departments and there is little information about the new Dealer Member resulting from the amalgamation, in particular with regard to its new compliance structure, supervision, insurance coverage and clearing of transactions.



AMF staff did not find any problems with the matter involving the acquisition of a significant interest in a Dealer Member.

*AMF recommendations*

IIROC's Montréal office staff should ensure that it obtains all documents to support its analysis of a transaction involving a Dealer Member.

Priority – Medium

*IIROC's response*

We acknowledge the finding on this particular file. In future, staff leading the review of such files will ensure that all discussions with relevant IIROC departments are documented in the file as well as any required District Council resolutions.

*AMF comments and follow-up*

AMF staff are satisfied with the response obtained and will follow up this recommendation with IIROC.

*Findings*

The procedures contained in the *General Counsel's Office Membership Policies & Procedures* manual concerning amalgamations, reorganizations, consolidations and changes of control among Dealer Members are quite succinct. In addition, the manual does not cover communications between IIROC departments or the types of matters which should be checked by Financial & Operations Compliance and Business Conduct Compliance departments, for example.

*AMF recommendations*

IIROC should set out more detailed procedures in the *General Counsel's Office Membership Policies & Procedures* manual.

Priority – Medium

*IIROC's response*

The *General Counsel's Office Membership Policies and Procedures* manual relates solely to GCO's role in coordinating the substantive review performed by the other departments. The manual does contain complete information about the manner in which materials are to be distributed to those departments and the levels of involvement of those departments (notice, approval, etc.) and other IIROC bodies (such as the District Councils or IIROC Board). It is not GCO's responsibility to perform a substantive review of the transaction, and the manual accurately and comprehensively reflects GCO's responsibilities. The policies and procedures for the substantive review of those transactions are set out in the respective departmental manuals, and there would be little benefit to reproducing those in the GCO manual.

*AMF comments and follow-up*

According to the information available to us at the time of the inspection, IIROC used the September 29, 2009 revised version of the *General Counsel's Office Membership Policies & Procedures* manual for its membership inspection.

We understand that detailed reviews of membership applications are primarily conducted by IIROC's Financial & Operations Compliance, Business Conduct Compliance and Registration departments, in accordance with a process outlined in their respective policies and procedures manuals. We also understand that the *General Counsel's Office Membership Policies & Procedures* manual sets out the procedures to be followed by the GCO to co-ordinate membership issues from all departments concerned.

We believe, however, that as with the registration component, the steps in the membership process should be consolidated into one document which IIROC staff could consult from the time an application is made until its approval by IIROC's Board of Directors, including the recommendation of the District Council. This would ensure that all information from different sources is contained in a single document and that applications are processed consistently.

AMF staff will follow up this recommendation with IIROC.