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IIROC Proposes Significant Change to Regulation of Investment Industry

The Investment Industry Regulatory Organization of Canada (“IIROC”) has proposed a major change to the regulatory structure of the investment industry.

In response to an announcement by the Canadian Securities Administrators (“CSA”) that it will undertake a review of the regulatory framework for industry self-regulatory organizations (“SRO’s”) later this year, IIROC has proposed to merge with the Mutual Fund Dealers Association (“MFDA”) to form a new SRO, which would regulate the majority of financial advisors in Canada.

Currently, most financial advisors in Canada (outside of Quebec) operate through dealer firms that are governed by either IIROC or the MFDA. IIROC was formed in 2008 through the merger of the Investment Dealers Association of Canada and Market Regulation Services Inc. and regulates investment dealers and trading activity on virtually all debt and equity markets except insurance. The MFDA was formed in 1998 and regulates dealers of mutual funds and certain exchange traded funds and exempt fixed income products.

As IIROC notes in its proposal, the piecemeal and duplicative regulatory structure currently in place reflects a bygone and simpler era in which one could more easily draw rigid divides between financial products and services available to consumers. The investment industry has changed dramatically in the last decade as a result of technology, a change which has only been exacerbated by COVID-19. As a result, according to IIROC, many firms are “increasingly focused on delivering a more comprehensive advice and service experience to their clients, across a broader range of products and services, and are forced to spend valuable resources to work around the requirements imposed by the existing fragmented self-regulatory regime.”

According to IIROC, merging with the MFDA will have numerous benefits including:

- Freeing up resources that investment firms currently spend trying to comply with duplicative and overlapping

regulations that can then be invested in innovation;

- Creating economies of scale that will result in more effective and consistent regulation across the industry;
- Improving customer experience, including the availability of ‘one stop shopping’, since investment firms will be able to create and offer products in compliance with a single regulatory standard; and
- Increasing investors’ understanding of and confidence in the regulatory process, since one SRO would be responsible for regulating the majority of investment advisors.

IIROC argues that the consolidation can be accomplished within three months of the CSA’s approval and without disrupting the existing rule framework, business models, or regulatory fee structures.

Though seismic, IIROC’s proposal is not novel, and follows a similar recommendation by the C.D. Howe Institute from last year.

While the MFDA agrees with the need to revamp the current regulatory structure, it has publicly opposed such a merger, and proposes instead the creation of an even broader SRO that would also include oversight of Exempt Market Dealers (EMDs), Portfolio Managers (PMs) and Scholarship Plan Dealers (SPDs), which goes beyond both IIROC and the MFDA’s present mandates (currently, EMDs, PMs, and SPDs are regulated directly by provincial and territorial securities commissions).

IIROC argues in response that “going back to the drawing board” in the manner proposed by the MFDA would take years to accomplish and effectively freeze the status quo for the foreseeable future, whereas its proposed merger with the MFDA could be accomplished quickly, since provincial and territorial securities commissions already recognize IIROC and the MFDA. Following the merger, IIROC proposes that the new SRO would assist the CSA in reviewing other registration categories like EMDs, PMs, and SPDs.

Both IIROC and the MFDA agree that significant changes are necessary and support greater consolidation. They differ (to a lesser extent) on the extent of those changes, and (to a greater extent) on the process (the MFDA proposes a broader consolidation of existing SROs and regulatory participants notwithstanding that that process will take some time to accomplish, while IIROC seeks the immediate consolidation of the two largest SROs in the industry, with the potential for further consolidation with other regulatory participants in years

to come). While it remains to be seen which approach the CSA will prefer, it is clear that there are major changes on the horizon for the regulatory structure of the Canadian investment industry.