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Kenmar response to CIRO consultation consolidated rules

<https://www.ciro.ca/newsroom/publications/rule-consolidation-project-proposed-ciro-rules>

Kenmar acknowledge the significant effort CIRO has undertaken to complete this complex rule consolidation project and appreciate the challenges of bringing two proud organizations together, one rules based, the other principles based.

Although virtually none of our prior Phase 5 recommendations are apparent in this consolidation consultation, we will try again to convince CIRO of the core concerns with some of the proposals. We refer CIRO to our earlier response located at <https://www.ocri.ca/media/12886/download?inline> Our main focus at this point in time is complaint handling and corrective action (learning from complaints).

In our earlier response we argued that some of the proposals could harm complainants, undermine OBSI, increase migration to discount brokers and lead to a further decline of financial consumer trust in the financial services industry/regulation. Without amendment, the net result will be an antiquated complaint system, to the detriment of retail investors.

Kenmar Associates is an Ontario-based privately-funded organization focused on investor education via articles hosted at www.canadianfundwatch.com Kenmar also publishes the Fund OBSERVER on a monthly basis discussing consumer protection issues primarily for retail investors. Kenmar is actively engaged with regulatory affairs. An affiliate, Kenmar Portfolio Analytics, assists, on a no-charge basis, abused consumers and/or their counsel in filing investor complaints and restitution

claims.

The general tone of the proposed complaint handling rules is to narrow the definition of complaint, allow extended Dealer cycle times and focus the use of complaint information to the resolution of individual complaints. There is barely a hint of a desire to deliver client satisfaction, eliminate root causes or improve service, policies, practices or products.

We use this consultation to amplify and elaborate on the rationale for our previous comments. These points are:

OBSI and proposed CIRO rules/ definition of a complaint.

Our concern is that the proposed definition of complaint is narrower than the existing OBSI standard. By requiring specific reportable levels or formal recording by the Dealer as a prerequisite, many legitimate investor expressions of dissatisfaction may be filtered out at the Dealer level. This creates an access barrier that will ultimately prevent a significant number of complaints from ever reaching OBSI for independent review, undermining consumer protection. We argue that this is inconsistent with CIRO's Public interest mandate, basic fairness and support for OBSI. A broader definition of complaint is warranted reflecting client focus.

Lengthy response time to complaint resolution

The 90 calendar day cycle time was structured to reign in Dealers who dragged out complaints for months on end. The 90- day cycle time standard was designed to include all internal complaint steps. Adding 30 calendar days on top of the generous 90-days would make the CIRO cycle time the lowest standard in the Western world. It should be noted that the 90- day target was articulated many years ago – the rest of the world now can deliver substantive response letters in 60 or less days including any internal steps. Quebec's AMF has established a 60 calendar day standard, the FCAC standard is 56 calendar days.

If there is objective evidence that a material number of complaint resolutions exceed 90 calendar days, CIRO should be asking serious questions about Dealer processes, resources and tools. If there is no evidence that a material number of complaints require more than 90 days to resolve, CIRO should withdraw the 30 day supplement.

The longer the complaint response time, the greater the chance the complaint will be abandoned or a low-ball offer accepted. There is also the distinct possibility that investors will be deterred from complaining at all. Complaints may be diverted away from OBSI. As a worst case, we recommend that the cycle time should be 90 calendar days, including ALL internal processes.

Reliance on Dealers to identify complaints alleging *serious misconduct*

We continue to have concerns regarding CIRO's reliance on Dealers to identify complaints alleging serious misconduct, which is vulnerable to under-identification for the reasons outlined in OBSI's April 2022 [comment letter to IIROC](#).

The definition of "serious misconduct" is based on a Dealer's assessment of whether an alleged activity "creates a reasonable risk of material harm to a client or the capital markets".

With Dealers able to determine whether a given complaint meets this definition is vulnerable to variable interpretation among Dealers and individuals because it depends on individual Dealer interpretation of complex and often ambiguous consumer complaints. This may lead to under-reporting and introduces the risk that any such interpretation will be viewed through the lens of the Dealer or the individual receiving the complaint, and how it is interpreted will be based at least in part on their own subjective view. Material conflicts-of-interest may influence identification.

Outsourcing of complaint investigation (a securities related activity) to a related party or other external source

CIRO Dealers should not be permitted to outsource client complaint handling to a non-CIRO regulated entity, even an affiliate. If for some reason, an unregulated IDRS is permitted by CIRO/CSA, there should be more transparency and at least a retention period defined for complaint records held by IDRS, client information should be robustly protected against cyber-attacks or privacy breaches and the CIRO Dealer be held accountable for any breaches.

An example of a IDRS is the one provided by the Bank of Nova Scotia (a separate corporation⁰). It goes by the name Customer Complaints Appeals Office (CCAO). Its Terms of Reference (ToR) are 4 pages of fine print. The CCAO calls itself "impartial" but it's staffed and funded by Scotiabank, operates under Scotiabank-drafted terms, and imposes blanket confidentiality and privilege over the entire process before any settlement is even discussed. If a client ultimately accepts an offer, they sign a Full and Final Release with a separate confidentiality clause -so there's a gag order to get in and another gag order to get out. We encourage CIRO staff to analyze the ToR and determine if the provisions are in the best interests of complainants. See CCAO Terms of Reference (ToR) <https://www.scotiabank.com/ca/en/about/contact-us/customer-care/ccao/terms-of-reference.html> In our view, clients should be read their Miranda rights before engaging with a CCAO.

The CSA and CIRO should have the legal right and obligation to audit outsourced complaint handling suppliers for compliance with securities laws, regulations and rules and service quality.

Internal Dispute Resolution Service (IDRS) usage issues

It seems odd to us that the nomenclature *Internal Dispute Resolution Service* contains the word *internal* when in fact the bank-owned Dealers outsource

complaint resolution to an **external** non-regulated affiliate with the blessing of CIRO.

Kenmar do not support IDRS in principle. We feel that a Dealer should make their initial resolution offer, their best offer. Adding more steps in a complaint process induces complainant fatigue and leads to unfavourable outcomes for complainants. In effect, IDRS, as proposed, becomes a direct in-house competitor to OBSI! IDRS is a deliberate attempt to siphon complaints away from OBSI. Once diverted, complainants may not have enough energy left to engage with CSA approved OBSI. Such a process goes against the fundamental principles of the Client Focused Reforms.

If IDRS is offered to a complaint, the complainant will be informed that the IDRS is not independent, usage is not required and limitation period time eroded but not that the IDRS may be unregulated and that any time spent with IDRS will eat into the 180 calendar days permitted to bring a complaint to OBSI. Improving disclosure will reduce the chances of Dealer diversion of complainants from independent OBSI. It's not clear to us why any reasonable complainant would agree to encounter IDRS.

It would be in the best interest of complainants to use a truly independent ombudsman service (OBSI). It should be noted that bank-based IDRS units have masqueraded as ombudsman and made false claims of independence.

The IDRS step, if permitted by CIRO, should be capped at 30 calendar days and not expanded simply because a substantive response letter is provided in less than 90 calendar days. Otherwise, some Dealers could exploit the provision to drag out the process to the detriment of the complainant. If CIRO/CSA approve the proposal as written, then the complainant, if offered IDRS, should be informed that the IDRS step could take more than 30 calendar days. We repeat –*IDRS, if permitted, should be contained within the 90 calendar day envelope and be executed by unconflicted Dealer staff.*

It is ironic that the CSA plan to impose strict oversight over OBSI and CIRO will have zero oversight over CCAO's.

"Service" complaints

The consultation paper states: " *The proposed definition of a service complaint is similar to the definitions currently in the MFD Rules and the IDPC Rules and focuses on complaints that are founded on customer service issues that do not involve regulatory non-compliance. In order to provide additional clarity, we intend to publish guidance that will address examples and factors to consider in determining whether something is a service complaint.*" As an overarching principle, we again ask that a client complaint be considered valid even if it does not directly involve regulatory non-compliance.

Examples include extended account transfer time, use of an unregulated complaint resolution entity, incompetent dealing with estate settlement matters, performing non- registerable activities such as financial or estate planning and providing incorrect income tax advice causing investor harm. "Service" complaints can cause material investor harm.

We strongly recommend the definition of complaint must relate to services and advice provided NOT services *offered*. If the services and advice provided cause investor harm, the complaint should be professionally addressed even if it does not involve regulatory non-compliance and OBSI should be made available, if the client is dissatisfied with the Dealer's substantive response letter.

Identification and Resolution of Systemic Issue(s)

We once again stress the importance of a CIRO-CSA approved protocol for identifying and resolving systemic issues as fundamentally integral to investor protection.

If trailing commissions being paid to discount brokerages had been identified and dealt with early, millions of retail investor dollars would have been saved. Ditto for the infamous double-billing issue.

The proposed CIRO process for dealing with a systemic issue is defined by:

3754 If a *Dealer Member* determines that the number or severity of *complaints*, is significant, or when a *Dealer Member* detects frequent and repetitive *complaints* made with respect to the same or similar matters which may on a cumulative basis indicate a serious problem, the *Dealer Member* must: review its internal procedures and practices, ascertain the scope and severity of client detriment that might have arisen, consider whether it is fair and reasonable for the *Dealer Member* to undertake proactively a redress or remediation exercise, **and ensure recommendations to remedy the problem are submitted to the appropriate management level.**

Kenmar are of the firm conviction that this rule does not adequately address systemic issues in that a submission to the appropriate management level does not provide closure. It merely deposits the systemic issue in the appropriate managers' in-box. In our opinion, without amendment, the rule is unfit for purpose.

We recommend that.

- "Systemic issue" be clearly defined by CIRO and/or the CSA
- Dealer staff promptly inform management (and CIRO) of the systemic issue identified by root cause analysis
- Management decide on affirmative actions to address the issue (a) the steps to eliminate the root cause of the issue; (b) the approach to remediation for all impacted clients ;(c) the timely communication of the issue to impacted clients and (d) Provide redress for impacted clients as applicable

An example of a rule to deal with systemic issues would be UK FCA DISP 1.3.303/01/2018R

<https://handbook.fca.org.uk/handbook/disp1/disp1s3?timeline=true>

CIRO should expect Dealers to have mechanisms, resourcing, capability, and systems in place to detect, assess and report breaches or misconduct swiftly. Delays or omissions in reporting may be viewed as indicative of a broader compliance culture problem. Timely reporting may not grant immunity, but it does demonstrate a degree of transparency and cooperation which can influence regulatory response.

There should also be a specific provision requiring CIRO to react when it is informed by OBSI of a systemic issue.

Disclosure of appeal process

The proposal that the Dealer Member's disclosure of the approved ombudsman service (OBSI) must *be at least equally prominent as the Dealer Member's disclosure of the internal dispute resolution service* is not congruent with the CSA guidance that a registered firm should not make an alternative independent dispute resolution or mediation service available to a client at the same time as it makes OBSI available. The reasoning is simple- to prevent complainant confusion and to ensure reasonable steps are taken to ensure that OBSI is the independent dispute resolution service that is made available to the client. The proposed language should be amended to comply with CSA guidance.

Use of NDA's in dispute resolution

We vigorously oppose the use of NDA's in complaint resolution that harm victims of financial assault and protect wrongdoers. Gag orders have been shown to cause physical and mental health problems. The Canadian Association of Retired Persons (250,000 members) has articulated the issue well. See <https://www.carp.ca/2023/02/26/why-does-canada-allow-gag-orders-on-vulnerable-investors/> In a landmark vote on February 9, 2023 lawyers from across Canada vowed to help stop the use of non-disclosure agreements, or NDA's, to silence victims and whistleblowers.

In a very real sense, NDA's are a form of revictimization.

Complainants considering using IDRS should be informed that they may be required to sign an NDA and possibly a non-disparagement clause before redress / compensation will be provided.

Prospective clients and complaint rights

We concur with CIRO that prospective clients should not be included in the definition of complaint. Dealers should not have to dedicate time and resources

addressing a complaint of a non-client although they may choose to do so if they so wish .If a prospective client has a complaint, say about misleading advertising, she/he can bring that to CISO's attention for action. Under no condition can we see a Dealer having to provide compensation to a prospective client, a client without an account agreement with the Dealer.

Complaint drafting assistance

The Dealer should assist complainants in formulating their complaint as required, not only upon request.

3730. Entering into settlements

We do not concur that a Dealer can avoid accountability for settling a complaint with their client by providing consent to an Approved person or employee to privately settle with the client. The contractual relationship is between the Dealer and the client. Without participation, the Dealer has no way of knowing if the complaint has been settled fairly or if any unfair conditions have been imposed on their client. Also, labour Code/laws should be checked to confirm that Firms can allow employees to provide compensation to a client due to employee errors or negligence.

In the event the Dealer does not consent to the employee settling with a harmed client, will the impacted client be left out in the cold?

Definition of trailing commission

The definition of trailing commission contradicts the definition used by the CSA and language used in CSA approved Fund Facts disclosure. The CRA has determined that trailers are used to provide taxable services: they are not just any payment made by a fund to the Dealer- they are specifically for the services and advice provided by the Dealer to the client. In cases of conflict, the CSA definition should take precedence.

As of June 1, 2022, CISO regulated order-execution-only dealers were finally prohibited from accepting trailing commissions by the CSA precisely because trailing commissions are for service and advice and OEO's are not permitted to provide personalized advice. CISO should use the CSA definition in the final version of the rules.

Access to margin for mutual fund dealer clients

We do not view providing retail mutual fund client access to margin accounts at Mutual Fund Dealers Members as a positive investor protection initiative. The fund industry has a mixed record of providing mutual fund clients advice on borrowing to invest. The beneficiary of allowing access to margin is for Dealers and salespersons via leveraged/ amplified trailing commission cash flows. We believe this proposal is looking for trouble especially given recent CSA/CISO CFR audit findings and the

disturbing results of the bank branch sales practice survey. If the CSA go along with the CIRO proposal, we recommend the robust MFDA rules for leveraging be retained and applied.

Regulation of AI

Artificial intelligence (AI) is becoming increasingly important in enabling Dealers to manage complexity, improve productivity, and strengthen decision-making. CIRO should be more transparent on how its rules are dealing with AI rooted fraud, AI washing, mitigating conflicts-of-interest and Dealer governance over AI deployment. In particular, we would be interested in the rules regarding Dealer use of AI in complaint handling, systemic risk identification and in providing personalized advice to clients. Monitoring Dealer application of AI and international benchmarking is required. See Gen AI complaints handling :E&Y <https://www.ey.com/content/dam/ey-unified-site/ey-com/en-ca/services/ai/documents/> and How AI strengthens compliance in complaints handling <https://regtechanalyst.com/how-ai-strengthens-compliance-in-complaints-handling/> Use of AI in complaint handling can have a major impact on the complaint process by analysis , identification of a systemic issue and trends. It can reduce cycle and improve consistency. The proposed consolidated rules should include baseline requirements regarding the use of AI in complaint handling.

Summary and conclusion

We appreciate that CIRO has taken a number of positive steps to improve complaint handling. However, to really modernize the system, more work is required as suggested in this letter and our earlier comments. We expect regulators will do what's necessary to provide a modern fair, prompt and effective complaint resolution available to Canadian investors. Kenmar view effective complaint handling/resolution as a cornerstone of investor protection and a socio-economic issue.

ISO 10002:2018 (Quality management - Customer satisfaction- *Guidelines for complaints handling in organizations*) is the primary international standard for establishing an internal, customer-focused complaint handling system. It provides a framework for tracking, analyzing, and resolving complaints efficiently to improve customer satisfaction and identify root causes for continual improvement. Implementing this system helps businesses foster customer loyalty and gain a strategic advantage in a competitive environment. This structured framework outlines requirements for establishing policies and designing accountability processes to enhance organizational responsiveness to a complaint. Kenmar encourage CIRO to benchmark its proposals against this standard.

CIRO staff may also want to try out Complaint system self-assessment: Commonwealth Ombudsman [Self-Assessment-Tool-for-Complaint-Handling-Agencies](#) We also provide our own version of a self-assessment checklist for CIRO

use (see APPENDIX). We fully expect CIRO management and Board will feel a need to amend the proposal after completion of these assessments.

Kenmar believes that the complaint handling proposal in the proposed rules does not strike an appropriate balance between clients' best interests and providing adequate time for CIRO Dealers to effectively investigate a complaint given available international benchmarks, AMF regulations and modern technological tools. In our view, there is a material risk of complainant fatigue with accompanying low-ball settlements/refusals if the proposals are approved by CIRO and the CSA.

Given CIRO's Public interest mandate, it is extremely disappointing that CIRO did not approach rule consolidation as a golden opportunity to raise industry conduct/standards, rather than merely an exercise of choosing between two existing sets of rules. Consolidating two obsolete complaint handling rules falls well below the high expectations we had for the new Self Regulating Organization.

No matter what complaint handling rules are ultimately arrived at, unless there is effective compliance oversight matched with timely impactful enforcement, investor protection will not be robust. The lessons learned from the recent bank branch survey suggest CIRO should modify its approach to compliance oversight and expand analysis of client complaint data to drive examinations and enforcement.

Please feel free to contact us if there are any questions concerning this letter.

We would welcome an opportunity to meet directly with CIRO staff to discuss our comments.

Respectfully,

K. Kivenko President
Kenmar Associates

References

Best practices for fair complaint handling: SK Ombudsman

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APPENDIX: Kenmar Modern Complaint system self-assessment checklist

- Is senior management engaged with the system?
- Is the definition of *complaint* clearly understood and aligned with Best practices?
- Is system accountability defined?
- Are complainants proactively assisted in framing their complaint?
- Does the system require the use of Root Cause Analysis?
- Are investigators properly trained and provided the necessary tools/resources?
- Does the system contain provisions for implementing corrective actions (reduce recurrence) based on an analysis of complaint data?
- Is *systemic issue* clearly defined?
- Is there a documented policy dealing with systemic issues and their timely resolution?
- Is the 90-calendar day cycle time competitive with international benchmarks?
- Is the system accessible and easy to navigate for complainants?
- Is a two stage process necessary? (do it right the first time)
- Are senior management/ BOD kept informed of complaint statistics, product issues, and client service level?
- Is there a set of fairness principles to guide decision-making?
- Has a loss calculation methodology been defined and is it compatible with OBSI's Opportunity Cost methodology?
- Does the system provide for non- monetary loss redress?
- Has any component of complaint investigation been outsourced to an unregulated affiliate or other entity?
- Are Gag orders imposed on complainants who accept a settlement offer?
- Is a client complainant satisfaction survey conducted at least annually?
- Are OBSI decisions used in improving the complaint handling system?
- Is complaint information used to improve business processes, productivity, speed and client satisfaction?
- Are individuals permitted to settle complaints on the side with complainants?
- Is AI used to reduce cycle time?

- How often is the system reviewed by compliance?
- Is the system fit for purpose?