



Monday, April 15, 2024

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**Re: CIRO Request for Comments 24-0067 issued on February 15, 2024 - Proposed rule amendments — Fully paid securities lending and financing arrangements, and CIRO Proposed Guidance on fully paid securities lending.**

The **Canadian Independent Finance and Innovation Counsel** appreciates the opportunity to provide comments to the Canadian Investment Regulatory Organization (CIRO) on the Proposed Amendments and Draft Fully Paid Securities Lending Guidance.

The Canadian Independent Finance and Innovation Counsel represents national Investment Dealers and their industry's position on securities regulation, public policy, and industry issues. We represent notable CIRO-regulated Investment Dealers in the Canadian securities industry.

### CIRO intention

CIRO published for comment proposed amendments to the Investment Dealer and Partially Consolidated (IDPC) Rules and IDPC Form 1 (Form 1) relating to fully paid securities lending and financing arrangements (Proposed Amendments).

As stated by CIRO, the Proposed Amendments aim to:

enhance the rule framework regarding retail fully paid securities lending, carry out CIRO's commitment to update our rules to address lessons learned from Dealer Members offering fully paid lending programs, and address a few inconsistencies in the existing financing arrangements rules. We are also publishing for comments the revised Guidance on Fully Paid Securities Lending (Draft FPL Guidance), which will replace the existing guidance GN-4600-22-001.

### Revised Guidance on Fully Paid Securities Lending

Investment Dealers have identified a few areas of concern arising from the draft Fully Paid Lending (FPL) Guidance. These issues, detailed below, would be difficult for the Investment Dealers we represent to navigate and create additional burdens, also discussed below.

### Section 2.3 – Securities Loan Agreement – Draft FPL Guidance

The Draft FPL Guidance states:

The client has the right to impose restrictions on the Dealer borrowing in the client's accounts such as:

- securities that they would like to exclude from lending, and
- their maximum risk tolerance limit on the total dollar value of securities they are willing to lend. The Dealer is expected to review their fully paid lending transactions against this criterion daily and terminate loans that exceed the client's risk tolerance limit as soon as possible.

Investment Dealers are particularly concerned with the Guidance as it pertains to clients introducing restrictions on the products Investment Dealers can or cannot lend under the FPL Program. These restrictions, if adopted, would add complexity to the operational processes of Investment Dealers participating in the lending program.

### Additional burden and operational complexities

If the Proposed Amendments detailed above were to be implemented, Investment Dealers would face additional burdens and operational complexities, including, but not limited to the following:

- **Daily Monitoring and Compliance:** Investment Dealers would need to continuously monitor their clients' restrictions regarding securities lending. This would require implementing systems and processes to review fully paid lending transactions against client criteria on a daily basis. Further, it would mean an additional layer of compliance and administrative work for the Investment Dealers.
- **Termination of Loans:** Investment Dealers would be required to terminate loans promptly if they exceeded the client's restrictions. This would necessitate close monitoring of loan positions and immediate action to unwind any positions that breached client-defined limits. Failure to do so could lead to regulatory repercussions and potential legal liabilities.
- **Enhanced Compliance Infrastructure:** To comply with the requirement of daily monitoring and termination of loans exceeding client restrictions, Investment Dealers would need to invest in robust compliance infrastructure. This would include upgrading or implementing new systems capable of real-time monitoring and reporting of lending transactions. Such systems would also need to be equipped with alerts and triggers to prompt immediate action when breaches occur, in order to ensure timely resolution and adherence to regulatory requirements.

In summary, the Proposed Amendments would impose additional monitoring, compliance, and operational constraints on Investment Dealers regarding securities lending activities. They would require Investment Dealers to invest in technology, resources, and processes to ensure adherence to client restrictions and regulatory requirements while managing securities lending transactions effectively.

### Industry recommendations regarding the FPL

Investment Dealers have crafted the following recommendations aimed at optimizing the FPL.

#### **Recommendation #1: Leveraging client borrowing through Introducing Brokers and Portfolio Managers.**

Since Fully Paid Lending has been available to retail clients in Canada for nearly five years, we are advocating for increased clarity and legal assurance from both CRO and the Canadian Securities Administrators (CSA) regarding the inclusion of clients from Introducing Brokers (IBs) or Portfolio Managers (PMs) in CRO-approved FPL programs.

By providing public guidance, regulatory bodies can enhance predictability and legal confidence not only for IBs and PMs but also for Investment Dealers, fostering scalability and streamlining processes, ultimately resulting in a more positive client journey. The current standards lead to potential delays and uncertainty for the industry.

International regulatory bodies overseeing FPL programs in the US, UK, the European Economic Area (EEA), Hong Kong, and Singapore, do not impose similar restrictions as those proposed by the Canadian regulators.

**Recommendation #2: Special Audit Reports through internal audit departments.**

Investment Dealers with established FPL programs (approved and operational for at least four years) should have the flexibility to utilize their internal audit departments to fulfill the requirement when a Special Audit Report is requested.

The reliance on external auditors often entails significant costs, as such auditors may lack the specialized expertise needed to perform these audits and may require additional time and resources from the Investment Dealer's internal operational and compliance teams for data collection, as observed by some Investment Dealers since the launch of FPL services. Having this option would empower Investment Dealers to leverage their internal resources efficiently, ensuring robust oversight while mitigating unnecessary expenses associated with external audits.

**Next Steps**

We are available to discuss the content of this submission further, address any concerns you may have, or provide additional information as needed. Your feedback is invaluable to us, and we are committed to ensuring that we all achieve our objectives effectively and efficiently.

Please feel free to contact me at [annie@cific.co](mailto:annie@cific.co) with any questions, comments, or to schedule a call to discuss any aspects of the letter or explore potential next steps. We look forward to our continued collaboration on this matter.

Sincerely,

*A. Sinigagliese*

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