



CIRO • OCRI

Canadian Investment
Regulatory
Organization

Organisme canadien
de réglementation
des investissements

CIRO Bulletin

Rules Bulletin

Request for Comments

IDPC Rules

Rule Connection:

IDPC Rules 1200, 1400, 2200, 2300, 2500, 2600, 2700,
3100, 3200, 3300, 3400, 3500, 3600, 3700, 3800, 3900,
4100, 4200, 4300, 4400, 4700, 4900

23-0092

July 13, 2023

Please distribute internally to:

Credit

Institutional

Internal Audit

Legal and Compliance

Operations

Registration

Regulatory Accounting

Retail

Senior Management

Trading Desk

Training

Comments Due By: August 14, 2023

Contact:

Member Regulation Policy

Email: memberpolicymailbox@iroc.ca

Phil Devault

Director, Member Regulation Policy

Telephone: (514) 392-3412

Email: pdevault@iroc.ca

Re-publication of Proposed Derivatives Rule Modernization, Stage 1

Executive Summary

The Canadian Investment Regulatory Organization (**CIRO**) is publishing for a third comment period proposed amendments to modernize and simplify its derivatives-related requirements.¹

We have made additional revisions to the proposed amendments set out in the previous two publications (the **Revised Proposed Amendments**) to:

- incorporate them in the most recent version of the Investment Dealer and Partially Consolidated Rules (**IDPC Rules**), formerly the IIROC Rules, which came into effect on January 1, 2023, and
- introduce changes to address concerns and suggestions received from commenters and the Canadian Securities Administrators (**CSA**).

¹ For previous publications, see [Rules Notice 19-0200](#), published on November 21, 2019 and [Rules Notice 22-0055](#), published on April 14, 2022.

These revisions are necessary to ensure consistency with the anticipated final version of CSA National Instrument 93-101 *Derivatives: Business Conduct* (**NI 93-101**).

How to Submit Comments

Comments on the Revised Proposed Amendments should be in writing and delivered by August 14, 2023 (30 days from the publication date of this Bulletin) to:

Member Regulation Policy
Canadian Investment Regulatory Organization
Suite 2000
121 King Street West
Toronto, Ontario M5H 3T9
e-mail: memberpolicymailbox@iiroc.ca

A copy should also be delivered to:

Market Regulation
Ontario Securities Commission
Suite 1903, Box 55
20 Queen Street West Toronto, Ontario M5H 3S8
e-mail: marketregulation@osc.gov.on.ca

Commentators should be aware that a copy of their comment letter will be made publicly available on the CIRO website at www.ciro.ca

1. Background

We initially published the Derivatives Rule Modernization, Stage 1 amendments on November 21, 2019.² The 2019 publication set out the objectives of the Derivatives Rule Modernization project, which primarily aims to ensure consistent regulatory treatment between securities-related and derivatives-related activities, where appropriate. Due to the extent and the nature of the amendments, the approach adopted was to publish proposed amendments for public comment in two separate stages as follows:

- Stage 1, includes all amendments we propose to make other than those relating to margin requirements, and
- Stage 2 will include the amendments we propose to make to the margin requirements.

On April 14, 2022 we republished the proposed amendments for a second comment period³ and received five comment letters. A summary of the comments received and our responses to these comments are included under Appendix 7.

To address comments received and incorporate the two previous publications in the IDPC Rules, we have made additional revisions as set out in the Revised Proposed Amendments described below.

2. Summary of Revised Proposed Amendments

2.1. Definition of “derivative” and “security”

To specify more clearly which of the core regulatory obligations apply to securities and derivatives, we previously proposed definitions for “*security*” and “*derivative*”. The intention and objective were not to change the current classification of products under the applicable legislative and regulatory framework.

Considering comments received, to avoid any potential confusion, we propose the following change to the definition of “*derivative*”:

Proposed terms	Proposed definitions
derivative	<p><u>A contract or an instrument classified as:</u></p> <p><u>(i) An option, swap, futures contract, forward contract, futures contract option, contract for difference₂ or</u></p> <p><u>(ii) any other financial or commodity contract or instrument whose market price, value, delivery obligations, payment obligations or settlement obligations are derived from, referenced to or based on an underlying interest, including a value, price, rate, variable, index, event, probability or thing₂.</u></p> <p><u>but does not include a contract or instrument determined by the Corporation to be classified in a category other than a <i>derivative</i>.</u></p>

² See [Rules Notice 19-0200](#).

³ See [Rules Notice 22-0055](#).

This proposed amendment will allow the CIRO to make a determination when the classification of a product is questioned.

2.2 Definition of “hedger”

The previously proposed definition of “hedger” is intended to apply to a client of a member registered as an investment dealer (**Investment Dealer Member**) that seeks to hedge business activities related risks. To qualify under the definition, partial hedging of such risks is acceptable. To address comments received, we are proposing the following changes:

Proposed term	Proposed definition
hedger	<p>A non-<i>individual</i> that:</p> <ul style="list-style-type: none"> (i) is exposed to one or more risks as a necessary part of its business activities, <u>and</u> (ii) seeks to hedge each<u>such</u> risk by engaging in <i>derivatives</i> transactions where: <ul style="list-style-type: none"> (a) the underlying interest for the transactions is the same as or materially related to the underlying interest for the risk, (b) the intended effect of the transactions is to: <ul style="list-style-type: none"> (I) eliminate or reduce the risk related to fluctuations in the <i>market value</i> of the underlying interest or position being hedged, or (II) substitute the risk associated with one currency for the risk associated with another currency, provided the aggregate amount of currency risk to which the hedger is exposed is not increased by the substitution, and (c) there are reasonable grounds to believe that the <i>market value</i> changes in the positions resulting from the transactions will completely or materially offset <i>market value</i> changes in the underlying interest or position being hedged.

We have also made related changes to the proposed guidance note *Applying and interpreting the definitions of “hedger” and “institutional client”* found in Appendix 1 and added more information to assist Investment Dealer Members in their assessment of whether a client qualifies as a hedger.

2.3 Client account statements

We had previously proposed to expand periodic reporting rules to include a daily statement for retail clients who have opened, unexpired or unexercised derivative contract positions in their account.

To address comments received, we are proposing to provide flexibility on the form and way the prescribed information is made available to retail clients. For example, this could include making the information available in clients’ online accounts or through their advisors.

2.4 Other amendments

The Revised Proposed Amendments are incorporated in the most recent version of the IDPC Rules to reflect rule changes made since the last publication.⁴ In line with the objective of the Derivatives Rule Modernization project, we are also proposing to extend the product due diligence and know-your-product requirements⁵ to derivatives-related activities. We believe these changes are required to ensure consistent regulatory treatment between securities-related and derivatives-related activities.

3. Impact of the Revised Proposed Amendments

Overall, the Revised Proposed Amendments remain consistent with the objectives and considerations described in previous publications. We believe the revisions address several suggestions received and alleviate some of the potential negative impacts by:

- adding clarity to some of the proposed requirements and defined terms,
- ensuring consistency with NI 93-101.

As previously concluded, while some of the proposed amendments will introduce incremental costs of compliance to Investment Dealer Members, the proposed amendments will establish relatively consistent regulatory requirements across all securities and derivatives-related business lines. This would avoid significant cost of compliance increases that would otherwise occur if requirements were materially different.

We continue to believe that the proposed Derivatives Rule Modernization, Stage 1 amendments impose costs and restrictions on the activities of market participants that are proportionate to the goals of the regulatory objectives sought to be realized. We have included an updated impact assessment in Appendix 3.

3.1. Impact of other policy projects

The Revised Proposed Amendments overlap with sections considered for amendment as part of the clarifying amendments to registration and proficiency requirements that will be published shortly. The most significant area of overlap is the table in subsection 2602(3). There is also an overlap in paragraph 3816(2)(x)(b)(VI) between the Revised Proposed Amendments and amendments proposed to facilitate the investment industry's move to T+1 settlement published on April 20, 2023 in [Rules Bulletin 23-0054](#). We anticipate the registration and proficiency amendments and T+1 amendments will be finalized prior to the completion of the Derivatives Rule Modernization Project. However, whichever set of amendments is finalized first will be reflected in subsequent amendments to the overlapping sections of the IDPC Rules.

4. Implementation

Subject to the process described in the next section, we intend to implement the Revised Proposed Amendments at the same time as the NI 93-101.

⁴ See [Rules Notice 22-0061](#), [Rules Notice 22-0191](#), [Rules Bulletin 23-0049](#) and [Rules Bulletin 23-0072](#).

⁵ Introduced as part of the client focused reforms. See [Rules Notice 21-0148](#).

5. Policy development process

5.1 Regulatory Purpose

The Revised Proposed Amendments would clarify the scope of application of the IDPC Rules for derivatives-related activities and ensure consistent regulatory treatment between securities-related and derivatives-related activities, where appropriate.

5.2 Regulatory Approval Process

The Board of Directors of CIRO (**Board**) has determined the Revised Proposed Amendments to be in the public interest and approved them for public comment on June 28, 2023.

We took the public interest into account when developing the Proposed Amendments through these consultations.

After considering the comments in response to this request for comments, together with any comments of the CSA, CIRO staff may recommend revisions to the Revised Proposed Amendments. If the revisions and comments received are not material in nature, the Board has authorized the President to approve the revisions on CIRO's behalf and the revisions will be subject to approval by the CSA. If the revisions or comments are material, CIRO staff will submit the revisions to the Board for approval for republication or implementation, as applicable.

6. Appendices

[Appendix 1](#) – Proposed Guidance Note - Applying and interpreting the definitions of “hedger” and “institutional client”

[Appendix 2](#) – Proposed Guidance Note - Derivatives Risk Disclosure Statement

[Appendix 3](#) – Impact Assessment

[Appendix 4](#) – Revised Proposed Amendments to the IDPC Rules (Clean)

[Appendix 5](#) – Revised Proposed Amendments to the IDPC Rules (Blackline)

[Appendix 6](#) – Revised Proposed Amendments compared to 2022 publication

[Appendix 7](#) – Summary of public comments received on 2022 publication