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The future of Canadian SROs

For Canadian self-regulatory organizations (SROs), change is inevitable

The existence of the Investment Industry Regulatory Organization of Canada (IIROC) and the Mutual Fund Dealers Association of Canada (MFDA) as two separate entities has been called into question, and the Canadian Securities Administrators (CSA) is now requesting a new framework.

What could a modernized SRO structure look like?
Adjustments must be made to create a more innovative, streamlined, and progressive SRO framework for investment and mutual fund dealers that will enhance the client experience by becoming a 'one stop shop' for advice-based products and services.

IIROC

175 Members[1]

Existing: IIROC oversees all investment dealers and trading activity on debt and equity marketplaces.

MFDA

91 Members[2]

Existing: MFDA is the national SRO for the distribution side of the mutual fund industry.

25 dual-platform dealers[3]

At a glance

- IIROC and MFDA have both suggested alternatives for the future:
  - **IIROC:** Merge the two entities into one organization, having the members adhere to a combined set of regulatory rules.
  - **MFDA:** A new investor-focused SRO to replace both existing organizations.
- Regulatory compliance topped the Thomson Reuters list of compliance challenges of 2020, highlighting the need for a new SRO.[4]
- The COVID-19 crisis has triggered an increase in the industry's technological capacity and transition to cloud. We need an SRO framework that addresses securities in a digital, flexible, post-pandemic environment.

It's time to get ahead of the inevitable changes and think about what SRO reform will look like for Canada.

Timeline for SRO reform

June 25, 2020
CSA releases consultation paper on the SRO framework

October 23, 2020
Deadline for responses; various bodies submit them for CSA review

Summer 2021
CSA publishes results of review outlining future of SRO framework in Canada

Scenario 1:
Merge IIROC and MFDA into one SRO

Scenario 2:
The potential for a net-new entity

This is just the beginning for Canadian SRO reform
As more information becomes available, it's imperative that organizations understand what the implications and future requirements of this change could be.

Global insights on SRO reform

SRO reform provides an avenue to innovation in the financial industry because it addresses evolving issues and their impact on the regulatory framework. Practical examples of reform that have modernized services and positioned markets to respond to extenuating circumstances include:

United Kingdom 1997

Financial services were reformed to address a fragmented system with overlapping regulatory responsibilities, resulting in the Financial Services Authority. Due to criticism in the 2008 financial crisis, further restructuring took place, culminating in the creation of two statutory regulators in 2013—the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA).

The FCA was tasked with monitoring conduct for financial services firms and the PRA became the prudential regulator for larger firms, removing a previously overburdened system and responding to the evolving needs of industry.

United States 2007

Financial Industry Regulatory Authority (FINRA) was established to help streamline the broker/dealer regulatory system, combine technologies, and create a single set of rules to govern membership matters. Previously, the multiple bodies risked fragmenting the market and ineffectively enforcing the existing regulations.

In response to evolving needs, FINRA further streamlined the market as a single regulatory body able to effectively act in the public interest and enforce rules.

What impact would a consolidated SRO framework have?

Over the long term, a consolidated SRO framework would affect MFDA/IIROC members across several business and operating model dimensions. The changes for different membership levels would be as follows:

Impact for dual-platform members

- **Operating costs**
  We estimated the net present value (NPV) savings of dual-platform firms over 10 years could be $380 to $490 million due to savings in systems and technology, staffing costs, and corporate costs[5]. A new framework would eliminate duplication of processes, improve ease of access to products and advice, and ensure an equitable environment for investors.
- **Process**
  Interactions with regulators would be streamlined across areas such as registration/licensing and regulatory reporting.

Impact for MFDA members

- **Advisor experience**
  Some advisors would have increased flexibility to grow and expand to serve the evolving financial objectives and goals of their clients. It would remove some obstacles for MFDA advisors to progress from a restricted licence to respond to client needs.

Impact regardless of current membership

- **Customer experience**
  Customer experience would be enhanced by the ability to be a one-stop-shop for products and services; 86% of current investors and 68% of aspiring investors believe it is important they can access a range of financial products and services without going to different providers or opening new accounts.[6]
- **Process**
  Potential to streamline the registration and regulatory reporting processes to create a more efficient environment for dealers.

In the near term, IIROC and MFDA members should consider these 4 steps:

1. **Understand and assess potential impact**
   Review the CSA and member response publications (both the initial CSA consultation paper and member responses, and the CSA's proposal to be released in summer 2021) and assess the preliminary impact to your organization.
2. **Connect with internal stakeholders**
   Bring awareness to and communicate the impact of a potential merger or re-structuring to key stakeholders across your organization.
3. **Prepare for client conversations**
   Train and educate client-facing personnel to prepare for communications with clients on this potential change.
4. **Establish a response plan**
   If a consolidation is recommended by the CSA, the timeline for completion could be short. Plan ahead and set aside resources to quickly respond and prepare.

Endnotes

1. Statistic as of 2020 – Link 1: IIROC Membership: Annual Report 2019/20 (iiroc.ca)
2. Statistic as of 2020 – MFDA Annual Report 2020
3. Stat as of November 23, 2020 – https://www.investmentexecutive.com/newspaper_/news-newspaper/sro-merger-too-simple/
4. "Moreover, the submission from the Ontario Securities Commission's (OSC) Investor Advisory Panel (IAP) questions how meaningful those cost savings will be. A study commissioned by IIROC estimated that merging with the MFDA could save $500 million in compliance costs over 10 years. However, the IAP's submission notes most benefits would flow to the 25 dual-platform dealers. And the savings would be marginal in the context of the revenue generated by those firms over that 10-year period."
5. Cost of Compliance in 2020 by Thomson Reuters
6. Deloitte – An Assessment of Benefits and Costs of SRO Consolidation – https://www.iiroc.ca/industry/sro-proposal/Documents/Deloitte_Assessment_of_Benefits_and_Costs_of_SRO_Consolidation_Final_EN.pdf#search=Assessment%20of%20the%20Benefits%20and%20Costs%20of%20Consolidation

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