

# IIROC NOTICE

## **Rules Notice Guidance Note – UMIR**

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## **NEW PROCEDURES FOR ORDER MARKER CORRECTIONS**

### **Summary**

This Rules Notice provides guidance on the new procedures for the reporting of an order marker correction to the Investment Industry Regulatory Organization of Canada (“IIROC”) by a Participant or Access Person.

Effective June 1, 2008, Market Regulation Services Inc. (“RS”) merged with the Investment Dealers Association of Canada (“IDA”) to form IIROC. IIROC adopted the Universal Market Integrity Rules (“UMIR”) as the rules of IIROC governing trading on marketplaces for which IIROC acts as the regulation services provider and IIROC adopted the guidance on the interpretation of UMIR previously published by RS. As a result of the merger, references to “RS” in the Market Integrity Notices mentioned in this Rules Notice should also include IIROC.

### **General Order Marking Requirement**

Rule 6.2 of UMIR requires that each order entered on a marketplace contain certain designations acceptable to IIROC. In addition to providing an accurate audit trail, the order designations provided for under Rule 6.2 enable IIROC to monitor trading activity on Canadian marketplaces to detect possible violations of UMIR and also allows IIROC to assist securities regulatory authorities by providing initial detection of possible violations of securities legislation (principally related to insider trading).



IIROC has issued guidance dealing with the obligations of a Participant or Access Person with respect to the entry and order marking requirements of orders entered on a marketplace as bundled orders including:

- Market Integrity Notice 2005-025 – *Guidance – Bundling Orders from a Long and Short Position* (July 27, 2005) which set out circumstances in which a sale order from a long position may be bundled with a sale from a short position; and
- Market Integrity Notice 2006-014 – *Guidance – “Insider” and “Significant Shareholder” Markers* (June 16, 2006) which set out the marking requirements dealing with the bundling of “insider” or “significant shareholder” orders together with non-“insider” or non-“significant shareholder” orders.

Reference should be made to these notices for detailed guidance on the circumstances in which orders may be bundled and the order marking requirements for bundled orders.

From the perspective of facilitating an accurate audit trail as required by Rule 10.11 of UMIR, IIROC generally discourages the bundling of orders. Nonetheless, a Participant or Access Person may choose to enter an order on a marketplace as a bundled order, subject to the limitations set out in the above referenced Market Integrity Notices. In the view of IIROC, if a Participant or Access Person enters a bundled order on a marketplace, the entire bundled order must be marked with the most “restrictive” applicable designation. For example, if an order from a long position is bundled with a sale order from a short position, the entire bundled order is to be marked “short” or, if applicable, “short exempt”. Similarly, in the case of an order for an “insider” or “significant shareholder” that is bundled with a non-“insider” or non-“significant shareholder” order, the entire bundled order is to be marked “insider” or “significant shareholder”, as appropriate. In the view of IIROC, the obligation to mark a bundled order with the most restrictive applicable designation ensures that orders are not intentionally bundled to avoid marking an order with the applicable “restrictive” marker.

One of the implications of requiring that a bundled order be marked with the more restrictive applicable designation is the “over-reporting” of trades by certain persons and trade types. For example, an order for a person who is not an insider that is bundled together with an order for an “insider”, will result in the entire order being marked “insider” (when in fact, the “insider” portion of the bundled order represents only a portion of the bundled order). Presently, IIROC provides an informal reporting regime whereby a Participant or Access Person is expected to report:

- in the case of a bundled order, the “corrected” volume of the order that corresponds to the marker that was attached to the order; and
- in the case of an order with an erroneous marker, the correct order designation.



## **Insider Trading Task Force Recommendations/Proposal for Consolidated Short Position Reports**

In September 2002, a task force established by the Ontario, British Columbia and Alberta Securities Commissions, the Commission des valeurs mobilières du Québec, the IDA, the Bourse de Montréal and RS sought to evaluate how best to address illegal insider trading in the Canadian capital markets (“Insider Trading Task Force”). In November 2003, the Insider Trading Task Force released its report outlining a series of recommendations which, among other things, recommended the public disclosure of all trades on a marketplace that are marked “insider” (currently, the insider marker is available for regulatory purposes, but is not disclosed to the public). In September 2006, the Ontario, Alberta and British Columbia Securities Commissions approved orders requiring the Toronto Stock Exchange (“TSX”) and the Toronto Venture Exchange (“TSXV”) to, using reasonable commercial efforts, consolidate on a per security basis, all trades on the TSX and TSXV that are marked for the accounts of insiders of each listed issuer and to publicly disseminate such information in summary form at the end of each trading day (“Insider Trading Reports”). IIROC understands that the TSX and TSXV expect to make these Insider Trading Reports available starting in August of 2008. IIROC also understands that Canadian Trading and Quotation System (“CNQ”) is also developing a form of insider trading summaries for public dissemination.

In Market Integrity Notice 2007-017 – *Request for Comments – Provisions Respecting Short Sales and Failed Trades* (September 7, 2007), IIROC proposed to replace the existing Consolidated Short Position Report with trading summaries from all marketplaces trading the same securities. This proposal is still under review by the applicable securities regulatory authorities. However, the ability to repeal the requirement for Participants to prepare and file Short Position Reports would depend upon the ability of IIROC to update in a timely manner trading information involving short sales in circumstances where a “short” order had been bundled with a “long” order or where the “short” or “short exempt” marker had been inadvertently omitted or incorrectly included on an order entered on a marketplace.

## **Procedures for Providing Order Marking Corrections**

Presently, all order marker corrections (corrected volumes and designations for bundled orders and erroneously marked orders) for orders entered on a marketplace are reported to IIROC market surveillance staff by email, or by other means. In the view of IIROC, the current “informal” reporting mechanism in addition to being “unsecure” (e-mails are not encrypted) is an inefficient method for Participants and Access Persons to report marker corrections. The new procedures will facilitate the preparation of automated updates that will be necessary for the production of the Insider Trading Reports and any summary trading report that may replace the Consolidated Short Position Report.

**Effective August 1, 2008**, each Participant or Access Person reporting an order marker correction will be required to submit an order marker correction report using the newly developed web-based regulatory marker correction form (“Regulatory Marker Correction Report”) that will be available under the “Quick Links” section of the IIROC website at [www.iiroc.ca](http://www.iiroc.ca).



The new web-based “Regulatory Marker Correction Report” will be password protected and will leverage the same access procedures currently in place at IIROC for the on-line Continuing Education and ComSet systems. Each Participant or Access Person must appoint a person within its organization to act as administrator (“Correction Report Administrator”). The Correction Report Administrator will have the authority to add or delete other users within the Participant or Access Person. The Correction Report Administrator may file Regulatory Marker Correction Reports on behalf of the Participant or Access Person or may delegate the responsibility to other users within the Participant or Access Person. The Correction Report Administrator may be the same individual as the “Administrator” for the Continuing Education and ComSet systems or for the filing of gatekeeper reports as described in Market Integrity Notice 2008-011 - *Guidance - New Procedures for Gatekeeper Reports* (May 16, 2008).

***In order to facilitate the introduction of the new procedures, each Participant and Access Person must provide the name and email address of their Correction Report Administrator to Thomas Moppett at [tmoppett@iroc.ca](mailto:tmoppett@iroc.ca) not later than July 31, 2008.***

## **Questions and Answers**

The following is a list of the most frequently asked questions regarding the procedures for submitting a Regulatory Marker Correction Report to IIROC and IIROC’s response to each:

### **1. Is the obligation to notify IIROC of a regulatory order marker correction a new requirement?**

No. Under Rule 6.2 of UMIR, a Participant or Access Person must ensure that each order entered on a marketplace contains the appropriate designations. If a trade has been improperly marked on entry, the Participant or Access Person must notify IIROC in order to correct the audit trail. Similarly, IIROC has permitted the entry of “bundled” orders from more than one account. In these circumstances, IIROC expects that the order will contain the most restrictive of order markers. If the bundled order executes, IIROC expects that the Participant or Access Person will provide accurate information regarding the proper marking of the orders. Insofar as Participants and Access Persons currently provide such marker correction information to IIROC through an informal reporting mechanism, the implementation of the on-line web-based reporting form simply formalizes the pre-existing reporting obligation.

### **2. Does the requirement to file a Regulatory Marker Correction Report apply only to bundled orders?**

No. IIROC expects a Participant or Access Person to submit a Regulatory Marker Correction Report to IIROC in all instances in which an order entered on a marketplace fails to include the appropriate order designation as required by Rule 6.2 and the order has executed at least in part. **A Regulatory Marker Correction Report is not required in respect of an order**



**that has not executed.** In the case of a bundled order, IIROC expects a Participant or Access Person that has entered a bundled order that trades on a marketplace to submit a Regulatory Marker Correction Report with the “corrected” volume of the order(s) that corresponds to each order type that makes up the bundled order.

**3. Does the requirement to submit a Regulatory Marker Correction Report apply to trades that are subsequently cancelled or amended?**

If a Participant or Access Person executes a trade and subsequently cancels or varies a trade (as to volume or price) involving an insider or significant shareholder, IIROC expects the Participant or Access Person to file a Regulatory Marker Correction Report identifying the nature of the change, including the corrected volume and/or price. A Regulatory Marker Correction Report is **not** required for a post-trade cancellation or variation that does not involve an insider or significant shareholder.

**4. What information must be in a Regulatory Marker Correction Report?**

At a minimum, the Regulatory Marker Correction Report must include:

- the identification of the security or securities involved;
- the trading number of the Participant that entered the order on a marketplace;
- the identification of specific orders or trades including:
  - the date and time the order was entered on a marketplace,
  - the trade date,
  - the marketplace on which the trade was executed,
  - the volume, and side (buy/sell) of the order, and
  - for an order involving an “insider” or “significant shareholder”, the price (or average price) and currency;
- the reason for the marker correction (i.e. marking error or bundled order);
- the details of the correction (i.e. corrected volume of a bundled order that is attributable to an “insider” or order was marked non-client instead of client);
- the name, title and contact information of the person filing the Regulatory Marker Correction Report; and
- in the case of an order that was improperly marked, the name of the person responsible for the marking error.



**5. To which order and account types does the requirement to file a Regulatory Marker Correction Report apply?**

The requirement to file a Regulatory Marker Correction Report applies to **all marker corrections** by a Participant or Access Person for a trade executed on a marketplace that is subject to UMIR (and is not limited to the correction of the “insider” or “significant shareholder” markers). Reference should be made to Rule 6.2 of UMIR, for the designations and markers which must be attached to an order on entry to a marketplace.

**6. Can a single Regulatory Marker Correction Report be submitted for an order that is “split” and executed on more than one marketplace?**

No. A separate Regulatory Marker Correction Report is required for each marketplace on which a portion of the original order was executed. If an order entered on a marketplace executes in more than one trade, a single Regulatory Marker Correction Report covering all trades resulting from the entry of the order may be filed.

**7. When is a Regulatory Marker Correction Report due?**

For order marker corrections involving a trade entered as a “bundled order”, a Regulatory Marker Correction Report must be submitted to IIROC on the date of the trade as soon as practicable after the execution of the trade and, in any case, by the later of 5 p.m. and 15 minutes following the close of trading on the marketplace on which the trade was executed.

In all other cases, IIROC expects that a Participant or Access Person will submit a Regulatory Marker Correction Report immediately upon becoming aware that an order had been “mismarked” on its entry on any marketplace, regardless of how the Participant or Access Person became aware of the error.

For trades involving an insider or significant shareholder that are cancelled or varied on a date other than the trade date, a Regulatory Marker Correction Report must be filed immediately upon the cancellation or variation of the trade. For “same day” trade cancellations or variations that have been reported to and accounted for by the marketplace, a Regulatory Marker Correction Report is not required to be submitted.

**8. Does the obligation to submit a Regulatory Marker Correction Report extend to orders entered on a marketplace by a Dealer-Sponsored Access Client (“DSA Client”)?**

Yes. Part 1 of Policy 7.1 under UMIR provides that a Participant has an obligation to supervise orders which are entered on a marketplace directly by a client and routed to a marketplace through the trading system of a Participant. Policy 7.1 further stipulates that compliance procedure must be appropriate for the lines of business conducted by a Participant. To the



extent that orders entered by a DSA Client will be subject to limited supervision prior to entry on a marketplace, the compliance procedures for DSA Clients should, at a minimum, address the procedures for testing orders that have been entered for order markers as required by Rule 6.2 of UMIR. As part of its compliance procedures, a Participant should include guidance on how testing and correction of orders from a DSA Client is to be conducted.