

IIROC Rule 2800

(Previously IDA Policy No. 5)

CODE OF CONDUCT FOR
IIROC-REGULATED FIRMS
TRADING IN WHOLESALE
DOMESTIC DEBT MARKETS

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RULE 2800
CODE OF CONDUCT FOR CORPORATION DEALER MEMBER FIRMS TRADING
IN WHOLESALE DOMESTIC DEBT MARKETS

PREFACE

Purpose

Rule 2800 describes the standards for trading by market participants in wholesale domestic Canadian debt markets. This Corporation policy was developed jointly with the Bank of Canada and Department of Finance to ensure the integrity of Canadian debt securities markets and thereby to encourage liquidity, efficiency and the maintenance of active trading and lending and promote public confidence in such debt markets.

In its application to Corporation Dealer Member Firms, Rule 2800 is supplementary to and explanatory of the Rules of the Corporation. It does not replace or restrict the application of the Rules to the wholesale domestic debt market.

History

In the spring of 1998 the Bank of Canada and Department of Finance introduced several initiatives, in consultation with the Investment Dealers Association (a predecessor organization of the Investment Industry Regulatory Organization of Canada) and other market participants, to maintain a well-functioning market in Government of Canada securities.

These actions were prompted by what was perceived as potential challenges to the liquidity and integrity of debt markets, including such factors as declining benchmark issue size in response to falling government borrowing requirements, the predominance of heavily capitalized market-makers and the emergence of levered market participants¹.

The federal government has defined its jurisdiction over domestic debt markets as the new issue or primary markets for Government of Canada securities. Since the liquidity and integrity of secondary markets are also at risk from reduced issue size, and capitalized and levered market participants, the Investment Dealers Association worked with the Bank of Canada and Department of Finance to develop a formal code of conduct for dealing practices in wholesale (i.e. institutional) domestic debt markets. This code of business conduct is embodied for Corporation Dealer Members in Rule 2800, and is intended by the participants in its development to be applicable in principle to all participants in wholesale domestic markets. It complements the federal government's objective to safeguard the liquidity and integrity of domestic markets.

The Corporation and the Provincial securities regulatory authorities (collectively the Canadian Securities Administrators (CSA)) also have in place specific and general rules that regulate domestic secondary market trading carried out by Corporation member firms. Rule 2800 provides further amplification and, in some cases, broader application of these rules in relation to domestic debt markets.

In 2002 the CSA and Corporation conducted, through an independent consultant, a survey of domestic debt market participants, including Dealer Members, to determine whether they were encountering any problems in the debt market. The survey was followed by reviews of a number of Corporation Dealer

¹ New auction rules (www.bankofcanada.ca/en/auct.htm#rules) were developed to set out the administrative and reporting procedures for Primary Dealers and Government Securities Distributors, and for their clients bidding at auctions for Government of Canada treasury bills and bonds. There were also revisions to the Terms of Participation, which defines the nomenclature for IDA member firms and chartered banks eligible to bid at Government of Canada securities auctions and the rules and responsibilities governing these designated Primary Dealers and Government Securities Distributors.

Members by Corporation Staff to further delineate the issues, one of which was the difficulty of developing operational and supervisory procedures from the general provisions of Rule 2800. In 2004 the Corporation struck a committee to revise Rule 2800. That committee has worked with the Bank of Canada and the Department of Finance to develop this version of Rule 2800.

Application

While Rule 2800 applies directly only to Corporation member firms and their related companies (as defined in Rule 1.1), which play an active and integral role in domestic debt markets, this code of conduct should also guide the actions of all other market participants. Examples of such market participants are chartered banks, which play a role in the marketplace analogous to Corporation member firms, insurance companies, money managers, pension funds, mutual funds and hedge funds. The Bank of Canada and the Department of Finance are joining the Corporation in taking steps to make these institutions aware of the Corporation code of conduct and encourage them to adopt and enforce similar rules. Dealer Members should also promote the standards established in this Rule among their affiliates, customers, and counterparties

Aspects of the Rule require the co-operation of affiliates and customers of Dealer Members, for example in reporting and certain disclosure, and Dealer Members are expected to conduct their business in a way that will encourage compliance with the Rule by affiliates, customers and counterparties to the extent applicable.

Moreover, dealings between Dealer Members, their related companies, affiliates, customers and other counterparties must be on terms which are consistent with this Rule and such dealings shall be deemed to include any terms necessary for a party to implement or comply with this Rule. Dealer Members must not condone or knowingly facilitate conduct by their affiliates, customers or counterparties that deviates from this Rule and its purpose of maintaining and promoting public confidence in the integrity of the Domestic Debt Market. Subject to Applicable Law, the surveillance provisions of this Rule require reporting to the Corporation or appropriate authorities of the failure, or suspected failure, of Dealer Members, their affiliates, customers and counterparties to comply with this Rule.

Dealer Members generally are responsible for the conduct of their partners, directors, officers, registrants and other employees and compliance by such persons with the Rules of the Corporation pursuant to Rule 29.1. In addition, partners, directors, officers, registrants and other employees of Dealer Members and their related companies are expected to comply with the Rules of the Corporation and other regulatory requirements, and this Rule is to be construed as being applicable to related companies and such persons whenever reference is made to a Dealer Member.

Implementation and Compliance Expectations

Rule 2800 sets out specific requirements for dealing with customers and counterparties, including that customer dealings be carried out on a confidential basis, and standards related to market conduct. As with all Rules, the Corporation expects member firms that are involved in wholesale domestic debt markets to have in place written policies and procedures relating to their dealings with customers and trading². Such policies and procedures must address both Rule 2800 and all other Corporation and CSA regulations related to the Dealer Member's whole domestic debt market activities. These policies and procedures must be readily available to relevant employees, who must be properly trained and qualified. Internal controls and operating systems must be in place to support compliance.

The Corporation will audit Dealer Member's sales and trading activities in the Domestic Debt Markets to ensure compliance with this Rule.

The Rule also provides for 'on demand' reporting to the Corporation of large securities positions held by dealers or traded with customers, if market circumstances warrant the need for such information.

² See also IDA Rule 29.27

The terms of the Rule are binding on Dealer Members and all related companies of Dealer Members and failure to comply with the Rule may subject a Dealer Member, a related company or their personnel to sanctions pursuant to the enforcement and disciplinary Rules of the Corporation. The disciplinary Rules of the Corporation provide for a wide range of sanctions, including fines of up to the greater of \$5,000,000 per offence for Dealer Members (\$1,000,000 per offence for Approved Persons) or triple the amount of the benefit from the breach, reprimands, suspension or termination of approval or expulsion. Notice of such sanctions is given to the public and government and other regulatory authorities in accordance with the Rules. In addition, other government or regulatory authorities such as the Bank of Canada, Department of Finance (Canada) or provincial securities regulatory authorities may, in their discretion, impose formal or informal sanctions including, in the case of Government of Canada securities, the suspension or removal by the Bank of Canada of eligible bidder status for auctions of such securities.

The Rule, together with applicable securities legislation, the auction rules and Terms of Participation for Primary Dealers and Government Securities Distributors, will ensure proper conduct of market participants at auctions of Government of Canada securities, in other primary markets and in secondary markets, and will result in the close coordination between federal authorities, the CSA, Corporation member firms and the Corporation in the exchange of detailed market information and the enforcement of proper market conduct.

RULE 2800

TRADING IN WHOLESALE DOMESTIC DEBT MARKETS

TABLE OF CONTENTS

- 1. Definitions**
- 2. Firm Standards and Procedures**
 - 2.1 Policies and Procedures
 - 2.2 Responsibility
 - 2.3 Controls and Compliance
 - 2.4 Confidentiality
 - 2.5 Resources and Systems
- 3. Dealings with Customers and Counterparties**
 - 3.1 Know-Your-Client and Suitability
 - 3.2 Conflicts of Interest
- 4. Market Conduct**
 - 4.1 Duty to Deal Fairly
 - 4.2 Criminal and Regulatory Offences
 - 4.3 Prohibited Practices
 - 4.4 Market Conventions and Clear Communication
- 5. Enforcement**
 - 5.1 Corporation Procedures to Apply
 - 5.2 Surveillance
 - 5.3 Net Position Reports

1. Definitions

The following terms used in this Rule shall have the meanings indicated:

“Applicable Laws” means the common or civil law or any statute or regulation of any jurisdiction in which Dealer Members and their related companies trade in the Domestic Debt Market, or any rule, policy, regulation, directive, order or other requirement of any regulatory authority, exchange or self-regulatory organization applicable to trading in, or having jurisdiction over, the Domestic Debt Market and/or Dealer Members or their related companies.

“Domestic Debt Market” means any Canadian wholesale debt market in which Dealer Members participate as dealers on their own account as principal, as agent for customers, as primary distributors or jobbers as approved by the Bank of Canada or in any other capacity and in respect of any debt or fixed income securities issued by any government in Canada or any Canadian institution, corporation or other entity or any derivative instruments thereon, and includes, without limitation, repo, security lending and other specialty or related debt markets.

“Rules” means the Rules, Rulings and Forms of the Investment Industry Regulatory Organization of Canada, from time to time in effect.

2. Dealer Member Standards and Procedures

2.1 Policies and Procedures

Dealer Members shall have written policies and procedures relating to trading in the Domestic Debt Market and the matters identified in this Rule. Such policies and procedures shall be approved by the board of directors of the Dealer Member or an appropriate level of senior management and by the Corporation. The policies and procedures must be established and implemented by senior management and must be periodically reviewed to ensure that they are appropriate to the size, nature and complexity of the Dealer Member’s business and remain appropriate as such business and market circumstances change.

2.2 Responsibility

Dealer Members shall ensure that all personnel engaged in Members’ trading activities in the Domestic Debt Market are properly qualified and trained, are aware of all Applicable Laws, this Rule and internal policies and procedures relating to Domestic Debt Market Trading and are supervised by appropriate levels of management.

2.3 Controls and Compliance

Dealer Members shall maintain and enforce internal control and compliance procedures as part of the policies and procedures required in paragraph 2.1 above to ensure that trading in Domestic Debt Markets by the Dealer Member is in accordance with Applicable Laws and this Rule.

2.4 Confidentiality

Dealer Members shall ensure that dealings in the Domestic Debt Market with customers and counterparties is on a confidential basis. Except with the express permission of the party concerned or as required by Applicable Law or Rules (including requests for information or reporting by the Corporation or by the Bank of Canada), Dealer Members shall not disclose or discuss, or request that others disclose or discuss, the participation of any customer or counterparty in the Domestic Debt Market or the terms of any trading or anticipated trading by such customer or counterparty. In addition, Dealer Members shall ensure that their own trading activities are kept confidential including information with respect to customers and trading and planning strategies. The policies and procedures

adopted to ensure confidentiality should restrict access to information to the personnel that require it to properly perform their job functions, confine trading to “restricted access” office areas by designated personnel and encourage the use of secure forms of communications and technology (e.g. careful use of cell or speaker phones, secure systems access and close supervision).

2.5 Resources and Systems

Dealer Members must devote adequate human, financial and operational resources to their trading activities in the Domestic Debt Market. Further, Dealer Members must implement operation and technological safeguards to ensure that their trading activities in the Domestic Debt Markets can be fully supported. This requirement contemplates not only that the Dealer Member have sufficient capital, liquidity support and personnel, but also that it have comprehensive operational systems appropriate for Domestic Debt Market trading such as all aspects of risk management (market, credit, legal, etc.), transaction valuation, technology and financial reporting.

3. Dealings with Customers and Counterparties

3.1 Know-Your-Client and Suitability

Dealer Members must learn the essential facts about every customer, order and account accepted and to ensure the suitability of investment recommendations made to a customer. This applies to Dealer Members dealing with all customers that trade in the Domestic Debt Market. Rule 2700 establishes minimum standards of supervision necessary to ensure compliance with Rule 1300.1 in dealings with institutional clients and will be applicable to dealings with customers in the Domestic Debt Market.

3.2 Conflicts of Interest

Good business conduct as well as provisions of the other Rules of the Corporation and Applicable Law require that Dealer Members avoid conflicts of interest in their dealings with customers, counterparties and the public. Such conflicts can arise in many different circumstances but one of the underlying principles is that a fair, efficient and liquid Domestic Debt Market relies in part on open and unbiased dealings by Dealer Members, and fulfillment by Dealer Members of their duties to customers before their own interests or those of their personnel. The policies and procedures of Dealer Members should clearly describe the standards of conduct for Dealer Members and personnel. Examples of some of the matters to be included in the policies and procedures are restrictions and controls for trading in the accounts of Members’ personnel, prohibition of the use of inside information and practices such as front running, fair client priority and allocation standards and prompt and accurate disclosure to customers and counterparties where any apparent but unavoidable conflict of interest arises.

4. Market Conduct

4.1 Duty to Deal Fairly

Dealer Members must observe high standards of ethics and conduct in the transaction of their business and prohibit any business conduct or practice which is unbecoming or detrimental to the public interest. Dealer Members must act fairly, honestly and in good faith when marketing, entering into, executing and administering trades in the Domestic Debt Market.

4.2 Criminal and Regulatory Offences

Dealer Members shall ensure that their trading in the Domestic Debt Market does not contravene any Applicable Law including, without limitation, money laundering, criminal or provincial securities legislation or the directions or requirements of the Bank of Canada or the Department of Finance (Canada) whether or not such directives or requirements are binding or have the force of law.

4.3 Prohibited Practices

Without limiting the generality of the foregoing, no Dealer Member or partner, officer, director, employee or agent of a Dealer Member shall:

- (a) engage in any trading practices in the Domestic Debt Market that are fraudulent, deceptive or manipulative; such as
 - (1) executing trades which are primarily intended to artificially increase trading volumes;
 - (2) executing trades which are primarily intended to artificially increase or decrease trading prices;
 - (3) spreading, or acquiescing or assisting in the spreading, of any rumours or information regarding issuers or the Domestic Debt Market that the Dealer Member or partner, director, officer, employee or agent of the Dealer Member knows or believes, or reasonably ought to know or believe, to be false or misleading;
 - (4) disseminating any information that falsely states or implies governmental approval of any institution or trading; or
 - (5) conspiring or colluding with another market participant to manipulate or unfairly deal in the Domestic Debt Market
- (b) engage in any trading which takes unfair advantage of customers, counterparties or material non-public information, such as:
 - (1) acting on specific knowledge of a new issue or client order in such a way as to unfairly profit from the expected resultant market movement and/or distort market levels;
 - (2) executing proprietary trades ahead of client orders on the same side of the market without first disclosing to the client the intention to do so and obtaining the client's approval;
 - (3) using proprietary information, the release of which could reasonably be expected to affect market prices, to profit unfairly;
 - (4) using material, non public information which may reasonably be expected to affect prices in the Domestic Debt Market, for gain; or
 - (5) abusing market procedures or conventions to obtain an unfair advantage over, or to unfairly prejudice, its counterparties or customers;
 - (6) consummating a trade where the price is clearly outside the context of the prevailing market and has been proposed or agreed as a result of manifest error.
- (c) engage in any trading in derivatives on Domestic Debt Market instruments in contravention of the above prohibitions;

- (d) accept any order from or effect any trade with another Domestic Debt Market participant if the Dealer Member knows or has reasonable grounds to believe that the other participant is, by giving the order or conducting the trade, contravening this Rule 2800 or any Applicable Laws;
- (e) accept or permit any associate to accept, directly or indirectly, any material remuneration, benefit or other consideration from any person other than the Dealer Member or its affiliates or its related companies, in respect of the activities carried out by such partner, officer, director, employee or agent on behalf of the Dealer Member or its affiliates or its related companies in connection with the sale or placement of securities on behalf of any of them;
- (f) give, offer or agree to give or offer, directly or indirectly, to any partner, director, officer, employee, shareholder or agent of a customer, or any associate of such persons, a material advantage, benefit or other consideration in relation to any business of the customer with the Dealer Member, unless the prior written consent of the customer has first been obtained.

4.4 Market Conventions and Clear Communication

Dealer Members shall use clear and unambiguous language in course of their trading activities, particularly when negotiating trades on the Domestic Debt Market. Each kind of trading in the Domestic Debt market has its own unique terminology, definitions and calculations and a Dealer Member shall, prior to engaging in any trading, familiarize itself with the terminology and conventions relevant to that type of trading.

5. Enforcement

5.1 Corporation Procedures to Apply

Compliance by Dealer Members with the terms of this Rule will be enforced in accordance with the general compliance, investigative and disciplinary Rules of the Corporation.

5.2 Surveillance

Careful surveillance of the Domestic Debt Market and the trading activities of market participants is required to ensure that the objectives of this Rule are achieved. Dealer Members and their related companies are responsible for monitoring their trading and the conduct of their employees and agents. Dealer Members have an obligation to report promptly to the Corporation or any other authority having jurisdiction, including the Bank of Canada, breaches of the Rule or suspicious or irregular market conduct. Dealer Members should also encourage their customers or counter-parties who raise concerns about any Domestic Debt Market activity or participants to report such concerns to the relevant authorities.

5.3 Net Position Reports

As part of the surveillance of Domestic Debt markets, the Corporation may require a Dealer Member and its related companies to file the Corporation Net Position Report. Net Position Reports may be requested by either the Bank of Canada (for Government of Canada securities), or by the Corporation. The request for a report, and associated requests for information required to clarify individual Dealer Member's reports, would be undertaken as a preliminary step to identify large holdings of securities that could have allowed a participant to have undue influence or control over the Government of Canada, provincial, municipal or corporate debt markets.

RULE 2800B

RETAIL DEBT MARKET TRADING AND SUPERVISION

Purpose

Rule 2800B describes the standards for trading and supervision by Corporation Dealer Members of retail domestic debt market activity.

Rule 2800B is supplementary to and explanatory of the Rules of the Corporation. It does not replace or restrict the application of the Rules to the retail domestic debt market.

1. Definitions

“**Retail Debt Market Trading**” means trading conducted by Dealer Members, whether as principal or agent, to fill orders received from a retail customer for any debt or fixed income securities or any derivative instruments thereon including, without limitation, repo, security lending and other specialty or related debt markets.

“**Retail Customer**” means a customer of the Dealer Member that is not an institutional client as defined in Rule 2700.

2. Dealer Member Policies and Procedures

Dealer Members shall have written policies and procedures relating to trading in the Retail Debt Market and the matters identified in this Rule. Such policies and procedures shall be approved by the board of directors of the Dealer Member or an appropriate level of senior management and by the Corporation. The policies and procedures must be established and implemented by senior management and must be periodically reviewed to ensure that they are appropriate to the size, nature and complexity of the Dealer Member’s business and remain appropriate as such business and market circumstances change.

3. Commissions and Mark-Ups

Dealer Members must have written procedures or guidelines issued to its registered representatives regarding mark-ups or commissions on debt or fixed income securities sold to the Dealer Member’s retail customers. The Dealer Member must have reasonable monitoring procedures to detect and monitor mark-ups or commissions which exceed those specified in the written procedures or guidelines and ensure that such mark-up or commission is justified in the reasonable judgment of the Dealer Member.

4. Market Conduct

4.1 Duty to Deal Fairly

Dealer Members must observe high standards of ethics and conduct in the transaction of their business and prohibit any business conduct or practice which is unbecoming or detrimental to the public interest. Dealer Members shall act fairly, honestly and in good faith when marketing, entering into, executing and administering trades in the Retail Debt Market.

4.2 Prohibited Practices

Without limiting the generality of the foregoing, no Dealer Member or partner, officer, director, employee or agent of a Dealer Member shall:

- (a) engage in any trading practices in the Retail Debt Market that are fraudulent, deceptive or manipulative; such as

- (1) executing trades which are primarily intended to artificially increase trading volumes;
 - (2) executing trades which are primarily intended to artificially increase or decrease trading prices;
 - (3) spreading, or acquiescing or assisting in the spreading, of any rumours or information regarding issuers that the Dealer Member or partner, director, officer, employee or agent of the Dealer Member knows or believes, or reasonably ought to know or believe, to be false or misleading;
 - (4) disseminating any information that falsely states or implies governmental approval of any institution or trading; or
 - (5) conspiring or colluding with another registrant to manipulate or unfairly deal in the Retail Debt Market.
- (b) engage in any trading which takes unfair advantage of customers, counterparties or material non-public information, such as:
- (1) acting on specific knowledge of a new issue or client order in such a way as to unfairly profit from the expected resultant market movement and/or distort market levels;
 - (2) executing proprietary trades ahead of client orders on the same side of the market without first disclosing to the client the intention to do so and obtaining the client's approval;
 - (3) using proprietary information, the release of which could reasonably be expected to affect market prices, to profit unfairly;
 - (4) using material, non public information which may reasonably be expected to affect prices in the Domestic Debt Market, for gain; or
 - (5) abusing market procedures or conventions to obtain an unfair advantage over, or to unfairly prejudice, its counterparties or customers;
 - (6) consummating a trade where the price is clearly outside the context of the prevailing market and has been proposed or agreed as a result of manifest error.
- (c) engage in any trading in derivatives on debt market instruments in contravention of the above prohibitions.
- (d) accept any order from or effect any trade for a retail customer if the Dealer Member knows or has reasonable grounds to believe that the customer is, by giving the order or conducting the trade, contravening this Rule 2800B or any statute or regulation, or any rule, policy, directive, order or other requirement of any regulatory authority, exchange or self-regulatory organization governing the Dealer Member or the market in which the trade will be effected.