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Paige Ward
General Counsel and Vice-President, Policy
Mutual Fund Dealers Association of Canada
121 King St. West, Suite 1000
Toronto, Ontario
M5H 3T9
email: pward@mfda.ca

Re: Proposed Amendments to MFDA Staff Notice MSN-0069 (Suitability)

We are writing in response to the MFDA's request for comments on the proposed amendments to MFDA Staff Notice MSN-0069 (Suitability) (the "**Proposed Amendments**"), as published on June 21, 2021.

About the Responsible Investment Association

We are a Canadian investment industry association composed of more than 130 institutional members and over 350 individual members who practice and support responsible investing ("**RI**") – defined as investments that incorporate environmental, social and governance ("**ESG**") issues. Our institutional members represent more than C$20 trillion in assets under management. A list of our members is available online at www.riacanada.ca.

RI has grown rapidly in recent years, driven largely by the growing business case for considering a portfolio's exposure to material ESG risks and opportunities. Executive compensation, board diversity, climate change, cybersecurity, and human rights are just a few examples of ESG issues that are increasingly shaping investment decisions as they can have serious financial implications for companies and portfolios. Many investors are also interested in aligning their investments with their values, for example, by avoiding companies that manufacture tobacco or weapons.

Our Comments

We submit that the proposed subsection 1.B. (d) in the Proposed Amendments should be revised, such that the final text of the first paragraph of this subsection will read as follows:

> A client's investment objectives are the results they want to achieve when investing, such as capital preservation, income generated by invested capital, and capital growth. **A client's investment objectives may also include investing in accordance with environmental, social and governance (ESG) criteria or other personal preferences.** The discussion between the Approved Person and the client to ascertain the client's investment needs and objectives should include consideration of any liquidity needs the client may have. The discussion should also provide an opportunity for the client to express their investment needs and objectives in non-technical terms that are meaningful to them, such as saving for retirement to maintain a certain lifestyle, increasing wealth by a certain percentage in a specific number of years, investing for the purchase of a home, ~~or~~ investing for the post-secondary education of their children**, or investing in accordance with their personal values.**

Supporting Evidence and Rationale

Canadian investors are particularly interested in responsible investing and ESG issues. Highlighting this, a 2020 survey of 1,000 Canadian retail investors conducted by Ipsos indicated that 72% of respondents were interested in responsible investments that aligned with their values.[1] In other words, there is a significant appetite for ESG-focused investment opportunities, and many investors are indicating that investing in such products is an end-goal in itself, or part of an objective to achieve outcomes pertaining to their values or sustainability preferences. Accordingly, investor sentiment suggests that RI and ESG-focused investing are more appropriately considered investment objectives, rather than investment strategies.

Investor demand for responsible investment has never been higher, and there is no shortage of new RI or ESG-focused investment products designed to meet this demand. However, there is a significant gap between the number of Canadian investors that are interested in responsible investing and the number of Canadian investors that ultimately hold responsible investments. We submit that this is because investors simply are not being asked about responsible investing by their financial services providers. In the same survey mentioned above, 75% of respondents indicated that they would like their financial advisor or financial institution to talk to them about responsible investments, but only 28% of respondents reported that their advisor or institution had done so.[2] Clearly, there is a significant disconnect between what investors are seeking with respect to RI and ESG-focused products and the information that their financial services providers are providing. In our view, this is a gap that the Proposed Amendments can, and should, help to bridge.

We note that elsewhere in the Proposed Amendments, it is explicitly stated that registered individuals may need to assist their clients in articulating their investment needs and objectives – in our view, and considering the disconnect between investors and advisors regarding RI and ESG-focused products as discussed above, this concept directly applies to responsible investing. **If a client is interested in responsible investing and cannot articulate this objective, and if the registrant does not know about this objective and/or does not inquire about it, it cannot be said that a registrant knows their client well enough to make suitable investment recommendations.**

Accordingly, we propose that the explanation of client investment needs and objectives set out in the proposed subsection 1.B. (d) in the Proposed Amendments should include consideration of a client's desire to invest in ESG-focused mutual funds, or to have their investment portfolio shaped by other preferences (such as investing in compliance with religious principles or avoiding/obtaining exposure to certain industries). Increasingly, investors are looking beyond investing solely to achieve narrow and discrete goals, and are seeking to incorporate other values and beliefs into their investment decisions. As a result, many investors' investment objectives have become more holistic in nature. However, as noted above, many financial services providers do not appear to have responded by altering their KYC/suitability processes to reflect this. For these reasons, it is our view that our proposed amendment to the proposed subsection 1.B. (d) in the Proposed Amendments is necessary to assist mutual fund dealers in meeting their obligations and their clients' needs.

Comparable Regulatory Approaches in Other Jurisdictions

We note that other jurisdictions are already taking steps to integrate RI concepts into the KYC and suitability assessment processes. The Australian Securities and Investment Commission has provided guidance to investment advisors that is similar to what we have proposed above, noting that in respect of an advice provider's duty to act in their client's best interests:

> *Advice providers must form their own view about how far [the best interest duty] requires inquiries to be made into the client's attitude to environmental, social or ethical considerations. Advice providers may need to ascertain whether environmental, social or ethical considerations are important to the client and, if they are, conduct inquiries about them*.[3]

As with the Australian guidance, our suggested revisions to the Proposed Amendments do not create a positive obligation on a registrant to inquire about a client's RI or ESG preferences. Rather, they encourage registrants to consider that their clients may have investment objectives that focus on personal preferences, and that they should seek to gain an understanding of these preferences.

Other jurisdictions have not only included sustainability preferences in the umbrella category of "investment objectives", but have made consideration of sustainability preferences mandatory. Most notably, recent amendments to the MiFID II framework in the European Union will require that an investment firm's obligation to act in the best interests of its clients dictate that when identifying a client or potential client's investment objectives, relevant information includes "*…the length of time for which the client wishes to hold the investment, his or her preferences regarding risk taking, his or her risk tolerance, the purpose of the investment and in addition his or her sustainability* preferences".[4] The EU has been a leading jurisdiction with respect to RI and ESG regulatory approaches, and its decision to require the consideration of sustainability preferences in identifying a client's investment objectives may be instructive to other jurisdictions.

Conclusion

We submit that the idea that sustainability preferences fall within the scope of "investment objectives" is not novel, and reflects a desire by investors in Canada and across the world to invest according to their values or sustainability preferences. Canadian investors need their financial services providers to guide them through the process of articulating their preferences or values in terms of investment objectives, and this cannot be done unless providers ask the right questions. Amending the Proposed Amendments to encourage this is a step in the right direction.

We appreciate the opportunity to provide comments, and would be pleased to discuss this further.

Sincerely,

Dustyn Lanz
Chief Executive Officer
Responsible Investment Association
111 Peter Street, Suite 700
Toronto, Ontario, M5V 2H1
(416) 461-6042 x 3

References

[1] Responsible Investment Association, "2020 RIA Investor Opinion Survey" (October 2020) at 7, online: *Responsible Investment Association* < https://www.riacanada.ca/research/2020-ria-investor-opinion-survey/>.

[2] *Ibid*, at 10-11.

[3] Australian Securities and Investments Commission *Regulatory Guide 175: Licensing: Financial product advisers – conduct and disclosure* (July 2021), at RG 175.321. <https://asic.gov.au/media/ymvbee1n/rg175-published-15-june-2021.pdf. >

[4] EC, *Commission Delegated Regulation (EU) 2021/1253 of 21 April 2021 amending Delegated Resolution (EU) 2017/565 as regards the integration of sustainability factors, risks and preferences into certain organizational requirements and operating conditions for investment firms*, [2021] OJ, L 277/1 at 6(b) (effective August 2, 2022). <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32021R1253&from=EN.>