



SOCIAL INVESTMENT ORGANIZATION

The Canadian Association for Socially Responsible Investment

184 Pearl St. 2nd floor
Toronto, Canada M5H 1L5
416-461-6042 t
416-461-2481 f
www.socialinvestment.ca

March 7, 2011

Richard J. Corner
Vice President, Member Regulation Policy
Investment Industry Regulatory Organization of Canada
1600 - 121 King St. West
Toronto ON
M5H 3T9
rcorner@iiroc.ca

Angie F. Foggia
Policy Counsel, Member Regulation Policy
Investment Industry Regulatory Organization of Canada
1600 - 121 King St. West
Toronto ON
M5H 3T9
afoggia@iiroc.ca

Dear Mr. Corner and Ms. Foggia:

Re: IIROC NOTICE – PROPOSALS TO IMPLEMENT THE CORE PRINCIPLES OF THE CLIENT RELATIONSHIP MODEL

I am writing on behalf of the members of the Social Investment Organization, the national association for socially responsible investment (SRI). Our sustaining and associate members include 34 financial institutions, asset management firms, fund companies, investment consulting firms and credit unions. As well, our membership includes about 150 advisors, consultants, lawyers and non-profits from across Canada. Our members are committed to the development of socially responsible investment, which is the integration of social and environmental considerations into the selection and management of investments. Our members serve more than a million Canadian depositors and investors.

With this letter, we are responding to the recent request for comment on the proposed rules and amendments regarding the client relationship model.

Let me take this opportunity to commend IIROC on this initiative. As we stated in our previous letter to you regarding the *Know your client suitability guidelines*, we believe the issue of investment suitability is at the centre of the advisor-client relationship. It's critical that regulators such as IIROC provide proper guidance and establish appropriate rules so that advisors know clearly what is required to establish client suitability.

Rules and amendments, Client Relationship Model.....2

As we stated in our last letter of December 17, 2009, we want to raise a matter that we feel is a major deficiency in your guidelines; namely, the lack of guidance on the assessment of client suitability on environmental, social and governance (ESG) issues. There is significant client demand for investments that reflect personal values on ESG issues. The majority of Canadians are demanding investments that take into consideration non-financial impacts, as well as traditional parameters of risk and return. Yet your know your client suitability guidelines failed to cite these concerns specifically. As a result, we want to raise this issue once again, and strongly recommend that your client relationship package adequately deal with this pressing concern.

Background

To set the context, let me touch on some of the points we originally raised in our 2009 letter:

- Nearly nine out of ten investors believe the financial community should pay more attention to social and environmental performance when valuing companies
- More than nine out of ten investors agree that corporate CEOs and Boards should monitor the performance of their companies on corporate social responsibility
- More than three-quarters of investors are interested in learning more about the social performance of companies in their portfolio
- More than three-quarters of investors believe that corporate social responsibility reporting is an important factor when making an investment decision
- Sixty-six per cent of investors have not considered or had a discussion with their financial advisor about the corporate social responsibility performance of companies in their portfolio
- A further 11 per cent have considered the issue, but not brought it up with their advisor
- Thirteen per cent have brought the issue up with their advisor, and one per cent said that both they and their advisor have brought it up
- Only eight per cent of advisors have brought it up with their clients.¹

We believe that this lack of advisor inquiry into social and environmental concerns by their clients represents an important gap in the client suitability assessment process. Just as it is absolutely essential to assess client suitability on issues such risk tolerance and investment horizon, it is also critical that advisors determine client preferences on ESG issues.

With this background, in 2009 we recommended the following:

¹ GlobeScan. Expectations of companies. Presentation to the Canadian Responsible Investment Conference. June 13, 2005. http://www.socialinvestment.ca/SIO_pres_GlobeScan_.pdf

Rules and amendments, Client Relationship Model.....3

- That you add a statement in your guidance document to note the importance of determining client preferences on environmental, social and governance considerations. The wording could be similar to the ASIC reg. 175.124, except that we would recommend the use of the term “environmental, social and governance considerations” rather than “environmental, social and ethical considerations,” as stated in the ASIC guidelines.
- That you add a reference to environmental, social and governance considerations in the Know Your Client Form.
- That you should also give consideration to drafting a Guidance Note specifically on ESG investments that would clarify advisor obligations to match appropriate investments with client ESG preferences.

We note that in your responses to the comments on the proposed Guidance (see Attachment G in the current request for comment) that you state that ESG issues are considerations in determining investment objectives and, as such, fall within existing required consideration in the rules.

It is encouraging to us that IIROC believes that ESG considerations are a part of the existing requirement to determine investment objectives. However, given the lack of awareness of this issue by advisors, as demonstrated in the GlobeScan research, we believe it is critical that IIROC specifically state that ESG considerations are to be included in the determination of investment objectives.

The reason that this needs to be stated explicitly is because it is a relatively new area of financial industry practice. Socially responsible investment has been in existence only since the 1980s; most advisors are still trained exclusively in financial analysis and are not inclined by temperament or training to ask clients about ESG factors. It is important that they receive regulatory guidance on this point.

Recommendations

Given this, we make the following recommendations to the proposed rules and amendments for the Client Relationship Model. We'll confine our recommendations to the account suitability for retail clients portion of the proposed rules.

In Attachment C, you propose new wording on Rule1300, specifically mandating Dealer Members to “use due diligence to ensure that the acceptance of any order from a client is suitable for such a client based on factors including the client’s current situation, investment knowledge, investment objectives and time horizon, risk tolerance, the account’s current investment portfolio composition and risk level.” Further, you propose a new mandate that “each Dealer Member, when recommending to a client the purchase, sale, exchange or holding of any security, shall use due diligence to ensure the recommendation is suitable for such client based on factors including the client’s current financial situation, investment knowledge, investment objectives and time horizon, risk tolerance and the account’s current investment portfolio composition and risk level.”

It is not realistic for advisors to understand that ESG factors are included within the term “investment objectives” in this context. In this context, investment objectives are considered to be one of many financial considerations that the advisor must bear in mind when recommending investments.

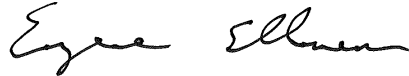
Rules and amendments, Client Relationship Model.....4

We would recommend the following sentence to follow the proposed wording in proposed rules p and q: "Further, that Dealer Members shall use due diligence in determining client preferences in regard to environmental, social and governance considerations of investments, and that the [order] [recommendation] are suitable within these considerations."

Such an amendment would clarify what appears to be the view of IIROC now that appropriate investment objectives include ESG considerations. However, until IIROC makes this view explicit, advisors will continue to have unclear guidance on this point.

In addition, we continue to recommend that the suitability guidelines be clarified to include ESG considerations. Our view is that since this is a new area of financial advisory practice, that the regulators should issue a special, separate guidance on this. We would be pleased to work with IIROC staff in drafting such a guidance.

Sincerely,



Eugene Ellmen
Executive Director
ellmen@socialinvestment.ca

CC Manager of Market Regulation
 Ontario Securities Commission
 20 Queen St. West
 19th floor, Box 55
 Toronto ON M5H 3S8
 marketregulation@osc.gov.on.ca