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Responsible Investing: Access Denied

Keith MacMaster

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*Keith Edward MacMaster**

Retail investors are increasingly demanding responsible investments as part of their portfolios. Retail investors also, generally, require the services of an advisor. This article argues that traditional mutual funds, while structurally able to provide responsible investments, have not provided responsible holdings to their mass affluent retail investing clientele. While institutional investors, and certain very wealthy retail investors, have a multitude of options to avail themselves of responsible investments, mass affluent retail investors have less of an ability to invest responsibly. Advisors and investors do not have access to the majority of responsible investments, nor are advisors adequately trained or properly compensated to provide advice on these products. Regulatory changes to advisor licensing and training are recommended to address these problems to provide mass affluent retail investors with better access to responsible investing options.

Les particuliers exigent de plus en plus de leurs conseillers en investissement que leurs portefeuilles soient composés de placements responsables. Selon l'auteur de cet article, les fonds communs de placement classiques sont en mesure de répondre à cette demande, mais ils ne le font pas même pour des clients particuliers aisés. Les investisseurs institutionnels et les investisseurs particuliers très fortunés ont une kyrielle d'options; cependant, les individus moins fortunés restent sur la touche : ils n'ont pas accès à la majorité des placements responsables et leurs conseillers n'ont ni la formation ni la rémunération appropriées pour faire des recommandations sur les produits de cette nature. Il faudrait apporter des modifications d'ordre réglementaire à la procédure d'octroi de permis aux conseillers ainsi qu'à leur formation pour combler ces lacunes si on veut permettre aux clients particuliers aisés d'avoir un meilleur accès aux placements responsables.

1. INTRODUCTION

The following story forms the basis of this article. I was sitting in my office on an ordinary Thursday afternoon. The firm that I worked for, one of Canada's largest financial institutions, often gets "walk-in" clients. An elderly gentleman walked into our branch, presented a large cheque, and told the customer service representative (CSR) that he had just sold his house. The CSR asked if the client would like to speak with an investment expert. The client agreed, and after the normal introductions, financial reviews, and the "Know your Client" (KYC)

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procedures, I asked what his intentions were with the money. The client told me that he wanted to invest it in "some sort of ethical or socially friendly way, I am not sure on the right lingo." I told him that our bank (all bank advisors are mutual fund licensed, so by law I was only allowed to provide advice on mutual funds, and only that bank's mutual funds as all advisors can only sell proprietary products) had such a fund. Fortunately, I knew what socially responsible investing was, as most advisors do not. I printed off the Fund Facts, which is the regulatory required document that describes the fund (described in more detail in the retail disclosure section below) and discussed the fund with the client. The house sale was approximately $400,000, so I did not need to refer him to our high net worth group (minimums of $1 million are required). The client agreed, and the transaction was completed. After the client left my office, I researched the fund in more depth. I noticed some peculiarities and began to wonder if this fund was truly socially responsible. I also researched on Morningstar the other funds available at other institutions and noticed many similarities. This discovery led me to asking myself, "Are clients with less than $1 million dollars actually getting responsible investments? Do truely responsible investments of mutual funds actually exist or are financial institutions peddling funds masquerading as responsible?" I, like many advisors, was solely compensated via commissioned sales, and so my income was funded by the transaction. However, I was paid less on this fund than I would have been if I had pushed some of the bank's other funds. Thus, I also wondered if other advisors, even if they knew about responsible investing, would have provided the advice knowing their compensation cheque would be lower than if they suggested other funds. All of these issues made me think that most Canadians do not have access to ethical, environmental and socially responsible funds, and this is a big problem.

The above example is far too common for a financial advisor and forms the basis for this article. The structure and regulation of licensing, standard of care, compensation and education for retail advisors create barriers for the mass affluent investor to access responsible investments (RIs). This article will answer the question of whether legal, regulatory, and policy reform is required to enhance the promotion of responsible investing vehicles and whether regulatory licensing requirements must be updated to allow mutual fund licensed representatives to sell a broader array of investment vehicles to ensure that Mass Affluent investors have access to RI.

The "reasonable investor hypothesis" surmises that the best way to generate returns is to understand long-term economic, social and environmental realities, and relates to a desire to reduce risk.[1] Most individuals in the developed world are "middle income" earners and must personally save for retirement, known as the "Mass Affluent" retail investor.[2] Government sponsored and employer

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1 Cary Krosinsky, Nick Robins, & Stephen Viederman, "After the Credit Crisis — The Future of Sustainable Investing" in *Next Generation of Responsible Investing*, Tessa Hebb (ed.) (Springer: 2012) at Ch. 2.

2 Rob Garver, "Banks Try, Try Again to Woo the Mass Affluent" (2010) 10 American

pension plans are not designed to fully fund retirements, or help invest for other purposes, so there is a real and substantial need for retail investments.[3] Many Mass Affluent investors want to make a substantial return on their investments, all while doing so in an environmentally and socially responsible manner.[4] Individuals, in large part, are unskilled at creating financial plans and require a financial advisor to help them with their retirement and investing goals.[5] As retirement today can mean a timeframe of 25 years or longer, long-term returns become vitally important, as the world will change in the upcoming decades.[6] Simply put, without retail advisors, most individuals would not have the abilities to invest.[7]

RI is investing in a responsible manner, while requiring profit maximization.[8] There is "no authoritative definition," of RI,[9] however; accepted classifications include negative and positive screens, Environmental, Social & Governance (ESG) integration, sustainability themed investing, impact investing, and corporate engagement/activist investing.[10] Positive screens include companies with positive influences, while negative screens eliminate undesirable companies

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Banker 10 at 14; Strategy&, *Wealthy, Young & Ambitious: How banks can profitably serve the rising mass affluent* (PwC/Strategy&, 2013).

3 Many self-employed do not have access to a government plan or to an employer pension plan and must invest solely in retail products to fund their retirements; Government of Canada, *Canada Pension Plan* (December 27, 2018), online: <https://www.canada.ca/en/services/benefits/publicpensions/cpp.html>; the United States uses the social security system, online: <https://www.ssa.gov/benefits/retirement/>.

4 Benjamin Richardson, *Socially Responsible Investment Law: Regulating the Unseen Polluters* (New York: Oxford University Press, 2008).

5 Kevin Dorey, "When do you need a financial advisor?", Chronicle Herald (February 1, 2017); Meryl Landau, "Do You Need a Financial Adviser?", U.S. News & World Report (September 1, 2011).

6 Sun Life Financial Inc., *Retirement Now Report* (Toronto: Sun Life, 2016) at 7; Treasury Board Canada, "Sources of Retirement Income" (December 30, 2016), online: <https://www.canada.ca/en/treasury-board-secretariat/services/pension-plan/plan-information/retirement-income-sources.html>; Emily Brandon, "The Top 10 Sources of Retirement Income", US News (May 13, 2014), online: <https://money.usnews.com/money/blogs/planning-to-retire/2014/05/13/the-top-10-sources-of-retirement-income>; Kenneth S. Shultz & Mo Wang, "Psychological Perspectives on the Changing Nature of Retirement" (2011) 66:3 American Psychologist 170 at 172.

7 *Ibid.*

8 Benjamin Richardson & Wes Cragg, "Being Virtuous and Prosperous SRI's conflicting goals" Paper presented in the Principles of Responsible Investment Academic Conference (Ottawa, ON: October 2009).

9 Benjamin Richardson, "Socially Responsible Investing for Sustainability: Overcoming Its Incomplete and Conflicting Rationales" (2013) 2:2 Transnational Environmental Law 311 at 313.

10 Global Sustainable Investment Alliance, *2016 Global Sustainable Investment Review*, online: <http://www.gsi-alliance.org/members-resources/trends-report-2016/> at 7 [GSIA].

or industries.[11] Impact investing is "targeted investments, typically made in private markets, aimed at solving social or environmental problems."[12] RI is moving away from command and control screens, favouring holistic integration of ESG issues.[13] This evolution is consistent with a "New Governance" theoretical model that believes that firms that place an emphasis on ESG will have less risk and better returns.[14]

This belief in lower risk for RI is important, as retail investors see risk only as a downward drop in prices.[15] Mass Affluent investors have a goal and timeframe to invest.[16] The psychological phenomenon of "loss aversion" relates to investors being more concerned about losses than gains.[17] For retail investors, risk is fundamentally asymmetric.[18]

RI products, in general and over a long-time horizon, produce positive returns. The "good management hypothesis" theorizes that the better the governance of a firm, the better the results should be both financially and reputationally.[19] While there is still some debate in the literature, overall, it appears that RI products outperform their non-RI counterparts.[20] So, if RI

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[11] Thomas Berry & Joan Junkus, "Socially Responsible Investing: An Investor Perspective" (2013) 112 J Business Ethics 707 at 708; H. Boerner, "SRI: Passing Fad or an Investment Approach on the Rise? Sustainable and Responsible Investment Outpaces Most Traditional Indexes and Equity Returns during Downturn" (2011) 16:1 Corp. Fin. Rev 37 at 38; Jacquelyn Humphrey & Darren Lee, "Australian Socially Responsible Funds: Performance, Risk and Screening Intensity" (2011) 102 J Business Ethics 519 at 520; Mark Rhodes, "Information Asymmetry and Socially Responsible Investment" (2010) 95 J Business Ethics 145; Pieter Trinks & Bert Scholtens, "The Opportunity Cost of Negative Screening in Socially Responsible Investing" (2017) 140 J Business Ethics 193.

[12] GSIA, *supra* note 10 at 4.

[13] Natalie Nowiski, "Rising above the Storm: Climate Risk Disclosure and its Current and Future Relevance to the Energy Sector" (2018) 39:1 Energy LJ 1 at 8.

[14] WA Bogart, *Permit but Discourage: Regulating Excessive Consumption* (New York: Oxford University Press, 2011) at 49-50; Mark DesJardine, Pratima Bansal, & Yang, "Bouncing Back: Building Resilience Through Social and Environmental Practices in the Context of the 2008 Global Financial Crisis" (2017) 3 J Management 1.

[15] Matthew Sherwood & Julia Pollard, "The risk-adjusted return potential of integrating ESG strategies into emerging market equities" (2018) 8:1 J Sustainable Finance & Investment 26 at 31.

[16] Franklin Parker, "Quantifying downside risk in goal-based portfolios" (2014) 17:3 J Wealth Management 68.

[17] *Ibid*. at 69.

[18] Frank Sortino, *The Sortino Framework for Constructing Portfolios*, (Elsevier, 2010); Victoria Dobrynskaya, *Downside Risk in Stock and Currency Markets*, (September 2014) PhD Dissertation, London School of Economics, [unpublished manuscript].

[19] Benjamin Auer, & Frank Schumacher, "Do Socially (ir)Responsible investments pay? Evidence from international ESG Data" (2016) 59 Quarterly Review of Economics and Finance 51 at 52.

[20] Europe: Benjamin Auer, "Do Socially Responsible Investment Policies Add or Destroy

products produce better returns than non-RI funds, and clients want to invest in these products, why is there such little uptake? This article addresses this question by showing that current research has failed to address the problems of advisor licensing as an underlying root cause of RI uptake. The licensing of retail advisors impacts RI in terms of both the legal structures utilized, the accessibility of these structures to the Mass Affluent and the compensation offered to advisors.[21] The point of emphasis for this article is that certain products are promoted more enthusiastically than others due to the larger sales commissions embedded in these products.[22]

This article compares Canadian requirements against those in the United States (US) and Australia as these nations have well-established stock markets and a robust Mass Affluent population.[23] This article will conclude that Canada should adopt certain US and Australian licensing provisions to allow a broader array of investments to be made available to the Mass Affluent, including allowing retail advisors access to a broader range of RI products, along with enhanced training and education requirements. This article will also argue that securities laws focus on the type of structure, rather than its underlying complexity, as a way to regulate products and may be partly to blame for the dearth of RI investments available to the Mass Affluent. Construction of RI investments that Mass Affluent investors can access is sorely needed.

Outside the scope of this article are environmentally related disclosure issues, which are weak and are not uniform among jurisdictions.[24] Stephen Kim Park notes that investors must be able to analyze the outcomes of their investments.[25]

European Stock Portfolio Value?" (2016) 135 J Business Ethics 381; Tessa Hebb, *Canadian SRI Mutual Funds Risk / Return Characteristics* (Carleton Centre for Community Innovation: Carleton University, 2015) pub R15-02; Vanita Tripathi & Varun Bhandari, "Do Ethical Funds underperform conventional Funds? Empirical Evidence from India" (2015) 4:2 Int J Business Ethics in Developing Economies; Gunnar Friede, Timo Buschi and Alexander Bassen, "ESG and financial performance: aggregated evidence from more than 2000 empirical studies" (2015) 5 J Sustainable Finance & Investment 210; Kathrin Lesser, Felix Rößle & Christian Walkshäus, "Socially responsible, green, and faith-based investment strategies: Screening activity matters!" (2016) 16 Finance Research Letters 171; Michael Trudeau, "Non-ethical funds outperform ethical rivals" (2011) Financial Advisor 1; Gerasimos Grompotis, "Evaluating a New Hot Trend: The Case of Water Exchange-Traded Funds" (2016) 6:4 J Index Investing 103.

21 Mark Van Hoecke, "Methodology of Comparative Legal Research" (2015) Law and Method 1 at 3; E. Morgera, "Global Environmental Law and Comparative Legal Methods" (2015) 24:3 Review of European, Comparative & Int Env L 254.

22 Rhys Bollen, "'There is no Alpha': Bounded Rationality in the Mutual Funds Market" (2013) 28:2 Banking and Finance Law Review 225 at 227.

23 Jeff Desjardins, "Top 20 Stock Exchanges by Market Capitalization", Visual Capitalist (April 10, 2017), online: <http://www.visualcapitalist.com/20-largest-stock-exchanges-world/>.

24 Task Force on Climate Related Disclosures, *Final Report — Recommendations of the Task Force on Climate Related Financial Disclosures* (June 2017).

Qualitative factors often lead to ESG issues being abandoned, and may preclude an accurate ESG "score",[26] which makes evaluating companies/assets difficult, but not impossible.[27] Junkus & Berry noted that many performance studies have data problems.[28] There is a need to conduct further research on ranking schemes and techniques.[29] Also, outside scope, are the problems with the individual funds themselves. Hawken concluded that many funds are masquerading as responsible when they really adopt conventional investment approaches.[30] Many RI funds are "'plain vanilla' funds, holding the same companies as non-RI funds."[31] It is doubtful that any broad-based plain vanilla RI fund could properly incorporate all ESG factors. Future research should attempt to answer this question.

This article will proceed as follows: it will introduce basic fund structures such as mutual funds, exchange traded funds, bonds and community economic development investment funds; next, the article will compare Canadian provisions against US and Australian counterparts for licensing, advisor standard of care, suitability/know your client, retail document disclosure, fee structures and education requirements; then the article will analyze licensing and suitability against the fund structures; and, will conclude that most advisors do not have access to most RI vehicles which limits the choice available to retail investors and minimizes uptake of RI.

2. ADVISOR REGULATION

Investor licensing is directly related to which products are able to be sold to the retail public. Many RI vehicles are implemented in forms inaccessible to the Mass Affluent.[32] As such, retail RI faces a headwind, not only from valuing the

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[25] Stephen Kim Park, "Social Bonds for Sustainable Development: A Human Rights Perspective on Impact Investing" (2018) 0:0 Business and Human Rights J 1 at 5.

[26] Diane-Laure Arjaliès & Pratima Bansal, "Beyond numbers: How investment managers accommodate societal issues in financial decisions" (2018) 39:56 Organization Studies 691 at 710.

[27] Sally Engle Merry, *The Seductions of Quantification, Measuring Human Rights, Gender Violence and Sex Trafficking* (University of Chicago Press: Chicago Series in Law and Policy, 2016) at 24.

[28] Joan Junkus & Thomas Berry, "Socially responsible investing: a review of the critical issues" (2015) 41:11 Managerial Finance 1176 at 1195.

[29] *Ibid.* at 1196.

[30] Paul Hawken, *Socially Responsible Investing: How the SRI Industry has Failed to Respond to People who Want to Invest with a Conscience and what can be Done to Change it* (California: National Capital Institute, 2004); Karen Benson, TJ Brailsford & JE Humphrey, "Do socially responsible investment managers really invest differently?" (2006) 64:4 J Business Ethics 337 at 352.

[31] Guy Dixon, "Confused about Ethical Investing?", Globe and Mail (April 15, 2017), online: <https://www.theglobeandmail.com/globe-investor/confused-by-ethical-investing-heres-a-primer/article34332548/>; SIF, "Fast Facts", online: <https://www.ussif.org/fastfacts>.

ESG scores of companies, but from its own distribution system: the financial advisor network.[33] Advisors need education, incentives, and the ability to sell RI funds, but current licensing provisions prevent retail advisors from accessing, recommending, or being knowledgeable about RI investments.[34] Six concepts are detailed in this article: licensing, advisor duties, suitability, document disclosure, fee structures, and education. Bollen notes that "actively managed mutual funds may be more promoted, and advisers may have an incentive to recommend products that provide them with better remuneration."[35] Fee arrangements that disincent advisors to provide certain choices for clients should be curtailed.

(a) Why Does this Matter — An Overview of Products

Over one-third of Canadians own mutual funds, accounting for 31% of financial wealth.[36] Approximately 43% of US households (55 million households) own mutual funds.[37] A mutual fund investor obtains instant diversification and access to a broad array of underlying investments.[38] Securities laws serve to align investment decisions with the interests of fund members, so the portfolio is structured to match investment objectives stated in its Prospectus.[39] Mutual funds can be rebalanced easily,[40] and in registered

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32 Outside scope is the Accredited Investor, which exempts certain investors from disclosure obligations, *Securities Act* (Ontario), R.S.O. 1990, c. S.5, s. 73.3 [OSA], *Prospectus and Registration Exemptions*, OSC NI 45-106 41 OSCB 4574 at Part 2.3, Greg Oguss, "Should Size or Wealth Equal Sophistication in Federal Securities Laws?" (2012) 107:1 Northwestern University L Rev 285. Generally Accredited Investors have access to IIROC dealers and as such have the full range of products available to them, based on an arbitrary wealth threshold that has no relationship to knowledge or competency.

33 The systems are separated into the asset management network, those who build and construct the funds, and the broker-dealer market, who distribute these funds to end users.

34 EU High Level Expert Group on Sustainable Finance, *Financing a Sustainable European Economy, Final Report* (European Commission, 2018) at 28.

35 Bollen, *supra* note 22 at 227.

36 IFIC, "Statistics and Facts", online: <https://www.ific.ca/en/info/stats-and-facts/>.

37 ICI, *Review of Trends and Activities in the Investment Company Industry* (2017 Investment Company Fact Book, ICI, 2017); Sarah Holden, *ICI Study: 55 Million US Households Own Mutual Funds* (ICI, 2017).

38 *Investment Funds*, OSC NI 81-102 (2017) 41 OSCB 9993 [NI 81-102]; *Mutual Fund Prospectus Disclosure Rule*, OSC NI 81-101 (2017), 40 OSCB 1584 [NI 81-101]; *Investment Company Act of 1940*, 15 U.S.C. §§ 80a-1 to 80a-64; LL Gremillion, *Mutual fund industry handbook: a comprehensive guide for investment professionals* (Hoboken, N.J.: John Wiley & Sons, Inc., 2005); John Haslam, *Mutual Funds Portfolio Structures, Analysis, Management, and Stewardship* (Hoboken, N.J.: Wiley, 2010); William Bertin & Laurie Prather, "Management structure and the performance of funds of mutual funds" (2009) 62 J Business Research 1364 at 1367.

39 OSA, *supra* note 32, s. 116(a); *Investment Fund Continuous Disclosure,* OSC NI 81-106, (2018) 41 OSCB [NI 81-106].

40 Kent Thune, "How and When to Rebalance your Portfolio", Balance (April 5, 2018),

accounts can be rebalanced without tax consequences.[41] Downside issues include substantial restrictions on the underlying investments — done to "protect" the retail investor[42] — high fees,[43] and explicit and "closet" indexing.[44] Alpha is the measure of active return on an investment.[45] Actively managed funds have larger fees than passive funds, lowering returns, and 66-75% of US active managers underperform the market, while in Canada, the percentage soars to 91%.[46] Many RI funds use active management including diversification strategies, proxy voting, and ESG integration.[47] This management puts RI funds at a disadvantage as exchange traded funds are generally less expensive.

An exchange traded fund (ETF) is a marketable security that tracks an index, commodity, bond, or basket of assets.[48] ETFs trade like stocks on an exchange, with higher liquidity, a wider range of investing strategies, and lower fees than mutual funds, making them attractive to investors.[49] ETFs can short stocks, lend shares, use leverage and use more complex derivative strategies that mutual funds

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online: <https://www.thebalance.com/how-and-when-to-rebalance-your-portfolio-2466529>.

41 Government of Canada, "Registered Retirement Savings Plan" (December 14, 2018), online: <https://www.canada.ca/en/revenue-agency/services/tax/individuals/topics/rrsps-related-plans.html>; Shaun Pfeiffer, "Tax Efficiency of Mutual Funds and Exchange-Traded Funds" (2016) J Financial Services Professionals 19.

42 NI 81-102, *supra* note 38, Part 2.3.

43 John Adams, et al., "Are mutual fund fees excessive?" (2012) 36 J Banking & Finance 2245at 2258; James Cox & John Payne, "Mutual Fund Expense Disclosures: A Behavioral Perspective" (2005) 83 Wash University L Quar 907.

44 Martijn Cremers, et al., "Indexing and active fund management: International evidence" (2016) 120 J Financial Economics 539.

45 Rob Russell, "ABCs of Investing, Alpha, Beta and Correlation", Forbes (July 14, 2014), online: <https://www.forbes.com/sites/robrussell/2014/07/15/abcs-of-investing-for-experienced-investors/#13077bc7393f>.

46 Aye Soe & Ryan Poirier, *SPIVA® Canada Scorecard* (S&P Global, 2016); Jeff Cox, "Bad times for active managers: Almost none have beaten the market over the past 15 years", CNBC News (April 12, 2017), online: <https://www.cnbc.com/2017/04/12/bad-times-for-active-managers-almost-none-have-beaten-the-market-over-the-past-15-years.html>; Owen Walker, "Active fund managers beat market by just 16p for every »100 invested", Press Release (January 28, 2018) via ProQuest database.

47 Indrani De, & Michelle Clayman, "The benefits of socially responsible investing: An active manager's

perspective" (2015) 24:4 J Investing 49 at 50.

48 Martin Lettau & Ananth Madhaven, "Exchange-Traded Funds 101 for Economists" (2018) 32:1 J Economic Perspectives 135.

49 Azhar Mohamad, Aziz Jaafar & John Goddard "Short selling and exchange-traded funds returns: evidence from the London Stock Exchange" (2016) 48:2 Applied Economics 152; James Chong, Monica Hussein, & Michael Phillips, "S&P 500 ETFs and Index Funds: Are Fees All There Is to It" (2011) 14:2 J Wealth Management at 59; Joanne Hill, "The Evolution and Success of Index Strategies in ETFs" (2016) 72:5 Financial Analysts J 8; Gary Gastineau, *The Exchange-Traded Funds Manual*, 2nd ed.

cannot.[50] US investors in ETFs have tax advantages and can defer capital gains tax until the entire ETF is sold, whereas with mutual funds, investors must claim capital gains tax every time assets in the fund are sold.[51] ETFs have played a major role in passive investing.[52] ETFs evolved from complex structures like bull/bear structures and are thus believed (wrongly) that they are more complex (but not necessarily riskier) than mutual funds, even if most ETFs created today are simple index structures.[53] It is this wide range of strategies and low cost which may make ETFs better suited for RI.

Retail investors use bonds as part of the fixed income component of their portfolio.[54] Green bonds pass certification processes to ensure that the projects funded have environmental/social benefits.[55] Legally speaking, there is nothing unique about a green bond, with most being "asset-linked" instruments.[56] Carney notes ". . . the transition . . . provides an annual opportunity worth trillions of dollars for companies and financiers."[57] Green and other RI bonds are a potentially valuable source for RI investments.

Community Economic Development Investment Funds (CEDIF)[58] allow for raising capital to invest in not-for-profit entities within a defined community.[59]

(Hoboken, NJ: John Wiley & Sons. 2010); Anna Agapova, "Conventional Mutual index funds versus Exchange Traded Funds" (2011) 14 J Financial Markets 323 at 324.

50 Mohamad, Jaafar & Goddard, *ibid*.; *see also* Joseph Engleberg, et al., "Short-selling Risk" (2018) LXXIII:2 J Finance 755; Christopher Nicholls, *Corporate Finance and Canadian Law*, 2nd ed. (Toronto: Carswell, 2013) ch.5.

51 Mark Kennedy, "ETF Tax Advantages over Mutual Funds", Balance (June 16, 2018), online: <https://www.thebalance.com/etf-tax-advantages-over-mutual-funds-1215121>; Fidelity Investments LLC, "Benefits of ETFs", online: <https://www.fidelity.com/learning-center/investment-products/etf/benefits-of-etfs>.

52 Cremers et al, *supra* note 44 at 540; Ananth Madhaven, *Exchange Traded Funds and the New Dynamics of Investing* (Oxford Scholarship Online, 2016) Caitlin Dannhauser, "The impact of innovation: Evidence from corporate bond exchange-traded funds" (2017) 125 J Financial Economics 537.

53 Hill, Evolution of ETFs, *supra* note 49.

54 Vasile Dedu & Dan NitÇescu, "Use of fixed income products within a company's portfolio" (2012) 10:10 Theoretical and Applied Economics 5 at 7; SIFMA, *2017 Fact Book* (New York: SIFMA Research Department, 2017) at 4.

55 Amelie Labbe, "PRIMER: green bonds" (2017) Int Fin L Rev London 1; International Capital Markets Association, "Social Bonds Principles" (June 2018), online: <https://www.icmagroup.org/assets/documents/Regulatory/Green-Bonds/SocialBondsBrochure-JUNE2017.pdf>.

56 Michael Flaherty et al., "Financing climate policies through climate bonds — A three stage model and empirics" (2017) 42 Research in International Business and Finance 468 at 471-472; Thiam Ng & Jacqueline Tao, "Bond financing for renewable energy in Asia" (2016) 95 Energy Policy 509 at 514.

57 CTV, "Companies need to come clean about climate change risk, Mark Carney says", CTV News (July 15, 2016), online: <http://www.ctvnews.ca/business/companies-need-to-come-clean-about-climate-change-risk-mark-carney-says-1.2987976>.

58 *Community Economic-Development Corporations Regulations*, NS Reg 79/98, Sch A

Social enterprises often emerge in geographies where the market and state have failed to provide adequate responses to social, economic, and environmental challenges.[60] Local communities are unlikely to have many locally-based investors who are sophisticated and locally focused, and those who are sophisticated are likely using networks to look outside the area for investment opportunities.[61] A CEDIF is small by nature.[62] Advantages include investing locally in a small business and favourable tax treatment.[63] Wind4all Communities III Inc. is an example of a CEDIF with a Mi'kmaq partner highlighting positive Indigenous rights/economic development opportunities.[64] One of these Mi'kmaq partners, the Pictou Landing First Nation,[65] is a historically disadvantaged community that has suffered human rights abuses.[66]

Thus, mutual funds, ETFs, bonds and CEDIFs are all potential RI structures. Unfortunately, licensing provisions, as illustrated in the next section, prevent most Mass Affluent retail investors from accessing these vehicles. Also, of significant note, the issues detailed in this section regarding RI are the same issues that regulators are reviewing for the industry as a whole.[67]

(i) Licensing

Securities in Canada, including advisor licensing, are regulated provincially, and are designed to protect "investors from unfair, improper or fraudulent practices; and to foster fair and efficient capital markets."[68] The securities

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[CEDIF Regs]; Michael Friedman, *Budget 2016: Labour-Sponsored Venture Capital Corporations Tax Credit Re-Introduced* (Toronto: McMillan LLP, 2016).

59 NSSC, "Community Economic-Development Investment Funds (CEDIFs)", online: <https://nssc.novascotia.ca/corporate-finance/community-economic-development-Investment-funds>; NSSC, *CEDIF*, NSSC Policy 45-601 (January 17, 2014), Blanket Order No. 45-521.

60 Douglas Lionais, "Social Enterprise in Atlantic Canada Canadian" (2015) 6:1 J Nonprofit Social Economy Research 25.

61 Harvey Johnstone, "Business model innovation: a case study of venture capital in a depleted community" (2013) 15:1 Venture Capital 77.

62 CEDIF Regs, *supra* note 58, ss. 10-12, 17.

63 *Equity Tax Credit Act*, S.N.S. 1993, c. 3, s. 11; *Equity Tax Credit Regulations*, N.S. Reg. 18/94; Government of Nova Scotia*, Equity Tax Credit, Equity Tax Credit Application* (January 22, 2019), online: <https://www.novascotia.ca/finance/en/home/taxation/tax101/personalincometax/equitytaxcredit/default.aspx>.

64 Assante Wealth Management Hydrostone, "Wind4all Communities III Inc.", online: <http://www.assantehydrostone.com/wind4all/>, s. 28.

65 *Ibid.* at 41.

66 Joan Baxter, *The Mill: Fifty Years of Pulp and Protest* (Pottersfield Press, 2017).

67 Status Report on CSA Consultation Paper 33-404 Proposals to Enhance the Obligations of Advisers, Dealers, and Representatives Toward Their Clients, CSA Staff Notice 33-319 (June 1, 2017).

68 Christopher Nicolls, *Securities Law*, 2nd ed. (Toronto: Irwin Law, 2018), OSA, *supra* note 32, ss. 1.1, 143(13); *Securities Act*, R.S.N.S. 1989, c. 418 [NSSA] ss. 1A(a), 1.2; CSA,

commissions delegate to self-regulatory organizations (SROs) retail advisor licensing and educational requirements, with two primary categories of registration; investment dealers and mutual fund dealers.[69] The two main SROs are the Mutual Fund Dealers Association (MFDA)[70] and the Investment Industry Regulatory Organization of Canada (IIROC).[71] The representatives of each category are limited in terms of the products about which they can provide advice. An investment dealer may act as a dealer in respect of any security; whereas a mutual fund dealer may only act as a dealer in respect of any mutual fund.[72] Mutual funds are regulated by the MFDA and most bank financial advisors are mutual fund licensed.[73] Mutual fund advisors cannot provide advice on stocks, bonds, ETFs and non-mutual fund-based index funds. There are currently approximately 79,800 licensed mutual fund advisors in Canada, which makes funds the most widely available type of structure available.[74]

Investment advisors are regulated by IIROC.[75] There are fewer IIROC advisors as compared to MFDA advisors currently licensed.[76] There are approximately only 8,200 licensed advisors of the big Canadian banks and large independent firms.[77] IIROC advisors also have higher minimum thresholds, with some firms maintaining a "posted" $250,000 investment minimum; however, in personally speaking with several brokers, the actual minimum is closer to $500,000,[78] with seasoned IIROC advisors having minimums of $1 million.[79] These minimums stem from fee structures, as most

"A Provincial/Territorial Memorandum of Understanding Regarding Securities Regulation" (2004), online: <https://www.securities-administrators.ca/aboutcsa.aspx?id=77>.

69 *Registration Requirements, Exemptions, and Ongoing Registrant Obligations*, OSC NI 31-103 (December 4, 2017) para. 7.1(1) [NI 31-103]; OSA, *supra* note 32, s. 21.1; Gary Gassman & Perry Granof, "Global Issues Affecting Securities Claims at the Beginning of the Twenty-First Century" (2007) 43 Tort Trial & Ins. Prac. L.J. 85 at 88.

70 *Ibid.* at para. 9.2.

71 *Ibid.* at para. 9.1.

72 *Ibid.* at para. 7.2.

73 MFDA, "Membership statistics", online: <http://mfda.ca/members/membership-statistics/>.

74 *Ibid.*

75 IIROC, "About IIROC, Know Your Advisor", online: <http://www.iiroc.ca/about/Pages/default.aspx>.

76 *Ibid.*

77 Staff Report, "The Firms with the Biggest Books, the Most Assets and the Largest Rosters" Advisor Magazine (May 4, 2016), online: <http://www.advisor.ca/news/industry-news/the-firms-with-the-biggest-books-the-most-assets-and-the-largest-rosters-205346>.

78 For example, Schultz Group has a minimum threshold of $500,000. Scotia Wealth Management, "The Schultz Group", online: <http://www.schultzgroup.ca/Services/Fee-Based-Investing.html>.

IIROC brokers are compensated via sales commissions and trailer revenue. Only investors with at significant investable assets can access an IIROC broker.[80] Most Mass Affluent investors will not meet these minimum thresholds, they will not be able to access an IIROC broker and will be limited to accessing only mutual fund products. Thus, if a retail investor wishes to purchase an RI ETF or individual bond, they must either use an IIROC broker or use an online brokerage and trade themselves.[81]

In the US, the Securities & Exchange Commission (SEC), the Financial Industry Regulatory Authority (FINRA), and state securities commissions govern adviser licensing.[82] Canadian and US licensing are similar in that both separate the two roles of investment adviser and, in the US case, a limited service adviser.[83] FINRA is authorized by SEC to protect investors and ensure the fair and honest operation of markets.[84] It does not regulate funds but regulates the broker-dealers and approximately 629,525 registered securities representatives that sell funds.[85] There was movement by Congress to separate the regulatory environment for mutual funds and investment advisers, similar to the Canadian experience; however, this has not yet occurred.[86]

The Australian Securities and Investment Commission (ASIC) regulates the fund industry in Australia.[87] Australia has moved to a centralized federal government securities regulatory regime, like the US to oversee its 25,379 advisors.[88] Australia and Canada are similar in that retail investors are more

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79 Mathieu Storrier, Scotia McLeod, online: <http://crescoadvisorygroup.ca/second-opinion/>; David Aston, "A Perfect Fit", MoneySense (May 12, 2011), online: <http://www.moneysense.ca/magazine-archive/a-perfect-fit/>.

80 Edwin Weinstein, *Mutual Fund Fee Research*, Paper submitted to CSA per RFP OSC 201314M -93 (OSC/Brondesbury Group, 2015) at 49 [Weinstein].

81 Online brokers are for the do-it yourself investor. These channels do not provide any advice or guidance on product suitability, nor require a duty of care. If the client requires advice, the only channel for ETFs or stocks is the broker/IIROC channel.

82 *Investment Advisers Act of 1940 15 U.S.C. § 80b-1 through 15 U.S.C. § 80b-21*, s. 203A. ø80b—3a & SEC. 222 ø80b—18a [IAA].

83 *Ibid.*

84 *Securities Exchange Act of 1934*, Pub. L. No. 94-29, sec. 3(6), § 3(a)(26), 89 Stat. 97, 100 (1975) (codified as amended at 15 U.S.C. § 78c(a)(26) (2012)), 15 U.S.C. § 78o-3. Barbara Black, "Punishing Bad Brokers: Self-Regulation and FINRA Sanctions" (2013) 8 Brook J. Corp. Fin & Com. L. 23.

85 FINRA, "About Us", online: <http://www.finra.org/about>; *Exchange Act Release No. 55495*, 2007 WL 1260858 (March 20, 2007) at 9; FINRA, "Statistics", online: <https://www.finra.org/newsroom/statistics>.

86 Barbara Black, "Are Retail Investors Better Off Today?" (2008) 2 Brook J. Corp. Fin & Com. L 303 at 319-20.

87 Australia, *Corporations Act of 2001 (Cth) No. 50, 2001*, Part 7.6 [Australia *Corporations Act*].

88 Pamela Hanrahan & Ian Ramsay, "Regulation of mutual funds in Australia", to be published in *Research Handbook on Mutual Funds,* William Birdthistle and John Morley

likely to retain the services of a financial advisor/financial planner rather than an investment advisor, which means that funds will be the more prominent products being sold.[89] The responsible entities that operate as advisors must be licensed under the Australian Financial Services (AFS) licensing regime.[90] The Australian *Corporations Act* provides that "a financial services licensee may give the authorized representative a written notice authorizing the person, for the purposes of this Chapter, to provide a specified financial service or financial services on behalf of the licensee."[91] The financial services specified may be some or all of the financial services covered by the licensee's licence.[92] Thus, not all licensed individuals will deal in both securities and mutual funds.

All three countries separate mutual fund advisors from the broader securities brokers. The treatment of mutual funds as distinct from other securities creates a potential for systemic bias and suggests a need for a more extensive regulatory review. This separation would affect Australians in much the same manner as Canadians.

(ii) Advisor duties

Investor protection depends on the unique relationship between financial advisor and client. Canadian advisors owe a duty to act fairly, honestly and in good faith with their clients.[93] This obligation, unfortunately, does not amount to a fiduciary duty or even a best interest standard.[94] A fiduciary duty requires fiduciaries to make complete disclosure of all material information.[95] There are

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(eds) (Edward Elgar Publishing, 2017); see also ASIC, *Annual Report 2016-2017* (Sydney: ASIC, 2017).

89 *Ibid.* at 8.

90 *Ibid.* at 12.

91 Australia *Corporations Act*, *supra* note 87, s. 916A.

92 *Ibid.*, s. 921B (2)-(4).

93 OSA, *supra* note 32, ss. 25(1), 36(1), NSSA, *supra* note 68, s. 39A; *Securities Act* (Alberta), R.S.A. 2000, C. S-4, s. 75.2.

94 *Hunt v. TD Securities Inc.*, 2003 CarswellOnt 3141, 66 O.R. (3d) 481, 36 B.L.R. (3d) 165, 39 C.P.C. (5th) 206, 229 D.L.R. (4th) 609, 175 O.A.C. 19, [2003] O.J. No. 3245 (Ont. C.A.); additional reasons 2003 CarswellOnt 4971, 40 B.L.R. (3d) 156, 43 C.P.C. (5th) 211, [2003] O.J. No. 4868 (Ont. C.A.); leave to appeal refused 2004 CarswellOnt 1610, 2004 CarswellOnt 1611, 330 N.R. 198 (note), 196 O.A.C. 399 (note), [2003] S.C.C.A. No. 473 (S.C.C.); *Varcoe v. Sterling*, 1992 CarswellOnt 888, 7 O.R. (3d) 204, [1992] O.J. No. 60 (Ont. Gen. Div.); affirmed 1992 CarswellOnt 976, 10 O.R. (3d) 574, [1992] O.J. No. 1501 (Ont. C.A.); leave to appeal refused (1992), [1992] 3 S.C.R. viii (note), 10 O.R. (3d) xv, 145 N.R. 390 (note), 60 O.A.C. 74 (note), [1992] S.C.C.A. No. 440 (S.C.C.); however, see *Andrews v. Keybase Financial Group Inc.*, 2014 NSSC 287, 2014 CarswellNS 582, 349 N.S.R. (2d) 1, 1101 A.P.R. 1, [2014] N.S.J. No. 418 (N.S. S.C.), and *Industrial Alliance Insurance and Financial Services Inc. v. Brine*, 2015 NSCA 104, 2015 CarswellNS 913, 367 N.S.R. (2d) 108, 54 C.C.L.I. (5th) 1, 392 D.L.R. (4th) 575, 1157 A.P.R. 108, 2015 C.E.B. & P.G.R. 8157 (headnote only), [2016] I.L.R. I-5827, [2015] N.S.J. No. 486 (N.S. C.A.); additional reasons 2016 NSCA 3, 2016 CarswellNS 45 (N.S. C.A.); leave to appeal refused 2016 CarswellNS 399, 2016 CarswellNS 400 (S.C.C.).

limited circumstances where advisors can hold "discretionary" investment accounts, which allow the advisor to make decisions and trades without the clients express consent, and there is full trust and confidence and discretion, then there may be fiduciary duties attached to the advisor.[96] However, this is the exception, not the norm, as most advisors are "order-takers" and the Supreme Court of Canada has ruled that fiduciary duties do not attach to order takers, who offer little to no advice.[97]

The Canadian Securities Administrators (CSA) has been investigating the need to enhance the obligations of advisors, dealers, and representatives toward a best interest standard for their clients.[98] Through the Fund Facts delivery (Point of Sale)[99] and Client Relationship Model Phase 2 (CRM2)[100] initiatives, the CSA has introduced regulatory reforms to make mutual fund fees, registrants' compensation, and clients' investment performance more transparent.[101] Adding a best interest standard and "leveling the playing field" by equalizing compensation structures would be a positive step to all mutual funds, with RI being an unintended beneficiary. The CSA has identified five issues that could be solved by a best interest standard, including rates of returns

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95 Leonard Rotman, "Understanding Fiduciary Duties and Relationship Fiduciarity" (2017) 62:4 McGill L J 1 at 10, 16.

96 *Kent v. May*, 2001 CarswellAlta 721, 298 A.R. 71, [2001] A.J. No. 552 (Alta. Q.B.) at paras. 51-53; affirmed 2002 ABCA 252, 2002 CarswellAlta 1311, 317 A.R. 381, 284 W.A.C. 381, [2002] A.J. No. 1327 (Alta. C.A.) at para. 55; additional reasons 2002 ABCA 306, 2002 CarswellAlta 1626, [2002] A.J. No. 1554 (Alta. C.A.) [Kent v. May]; *Varcoe v. Sterling*, *supra* note 94 at paras. 234-236, Eric Dolden & Tom Newnham, *Legal Liability for Financial Advisors in Canada* (Vancouver: Dolden, Wallace, Folick LLP, 2015) at 19 [Dolden & Newnham].

97 *Hodgkinson v. Simms*, 1994 CarswellBC 438, 1994 CarswellBC 1245, EYB 1994-67089, [1994] 3 S.C.R. 377, 97 B.C.L.R. (2d) 1, 16 B.L.R. (2d) 1, 22 C.C.L.T. (2d) 1, 57 C.P.R. (3d) 1, 117 D.L.R. (4th) 161, 5 E.T.R. (2d) 1, [1994] 9 W.W.R. 609, 49 B.C.A.C. 1, 6 C.C.L.S. 1, 95 D.T.C. 5135, 171 N.R. 245, 80 W.A.C. 1, [1994] S.C.J. No. 84 (S.C.C.) at para. 33 [Hodgkinson v. Simms], Leonard Rotman, "Fiduciary Law's Holy Grail: Reconciling Theory and Practice in Fiduciary Jurisprudence" (2011) 91:921 Boston University L Rev 921 at 965-966.

98 OSC, *Consultation Paper OSC 33-404* (April 28, 2016), online: < http://www.osc.gov.on.ca/en/SecuritiesLaw_csa_20160428_33-404_proposals-enhance-obligations-advisers-dealers-representatives.htm > .

99 *Implementation of the Final Stage of Point of Sale Disclosure for Mutual Funds: Pre-Sale Delivery of Fund Facts,* CSA Notice of Amendments to NI 81-101 Mutual Fund Prospectus Disclosure and to Companion Policy 81-101CP Mutual Fund Prospectus Disclosure (2014) 37 OSCB 10985.

100 CSA *Notice of Amendments to National Instrument 31-103 Registration Requirements, Exemptions and Ongoing Registrant Obligations* and to Companion Policy 31-103CP *Registration Requirements, Exemptions and Ongoing Registrant Obligations (Cost Disclosure, Performance Reporting and Client Statements)* (2013) 36 OSCB 3173.

101 Rudy Luukko, "The days are numbered for embedded fund commissions", Morningstar (June 29, 2016), online: < http://cawidgets.morningstar.ca/ArticleTemplate/ArticleGL.aspx?id = 758402&culture = en-CA > .

and fees (i.e. value for money), misplaced trust, conflicts of interest, information asymmetry, and outcomes based on the regulatory regime.[102] Moving to a best interest standard would alleviate (at least in theory) some of these issues as advisors would need better skill sets to meet their duties.

The duty of care, on the other hand, differs in the US from Canada. Under the *Investment Advisers Act of 1940* (IAA), it is unlawful for any investment advisor to directly or indirectly defraud, deceive, or engage in a deceptive or manipulative practice.[103] It is also illegal for any person willfully to make any untrue statement of a material fact in any registration application or willfully to omit to state in any such application or report any material fact which is required to be stated therein.[104] In the US, the above legislation has been interpreted to be a fiduciary duty standard, and would pose greater obligations on the advisor than their Canadian counterparts.[105]

Like the CSA, the SEC is mandating increased reforms and disclosures for advisors.[106] This reform is characterized as the "fiduciary duty" versus suitability standard of care.[107] As fiduciaries, investment advisors owe their clients a duty to provide only suitable advice, which takes into account the client's financial situation, investment experience, and investment objectives.[108] The disclosures or lack thereof, and the lack of training around RI may not amount to a breach of fiduciary duty, but it could impact a client's purchasing decision, especially if a best interest standard was imposed.[109] Presumably, this fiduciary duty standard should lead to increased and more complete disclosures of RI materials in US than in Canada. Unfortunately, the legislation seems doomed for repeal.[110]

The United Kingdom, European Union, and Australia already mandate a best interest standard.[111] Dealer and advisors in Australia have a fiduciary duty

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[102] *Ibid.* at para. i.

[103] IAA, *supra* note 82, ss. 206, 207, SEC. 206 ø80b—6.

[104] *Ibid.*, s. 207. ø80b—7.

[105] *Securities & Exchange Commission v. Capital Gains Research Bureau Inc.*, 11 L.Ed.2d 237, 84 S.Ct. 275, 375 U.S. 180 (U.S. Sup. Ct., 1963).

[106] SEC, *Commission Guidance on Disclosures*, Securities Act Release No. 33-9106, Exchange Act Release No. 34-61469, 75 Fed. Reg. 6289 (February 2, 2010).

[107] James Wrona, "The Best of Both Worlds: A Fact-Based Analysis of the Legal Obligations of Investment Advisers and Broker-Dealers and a Framework for Enhanced Investor Protection" (2012) 68:1 Business Lawyer 1.

[108] SEC, Investment Advisers Act Release No. 1406 (March 16, 1994).

[109] Joseph Goertz, Swarn Chatterjee & Brenda Cude, "Suitability vs Fiduciary Standard: The perceived impacts of changing one's standard of care" (2014) 27:2 J Financial Planning 20.

[110] *Financial Choice Act* (US), H.R.10 — 115th Congress (2017-2018) [FCA].

[111] Australia *Corporations Act*, *supra* note 87, Part 7.7A, Division 2, Subdivision B, s. 961B; *Standard of Conduct for Advisers and Dealers: Exploring the Appropriateness of Introducing a Statutory Best Interest Duty When Advice is Provided to Retail Clients*, OSC CSA Consultation Paper 33-403 (2012) 35 OSCB 9558 at 3.

to their clients. A duty of care, diligence and honesty includes a "best interests" standard,[112] which is more akin to US standards and is more onerous than Canadian requirements. The Australian Statement of Advice[113] contains even more information and requires a more thorough review of client circumstances than Canada requires, which should uncover more environmental and ethical preferences than Canadian advisors can under current suitablility requirements.

(iii) Suitability/Know Your Client

Despite the differences in advisor standards of care, all three jurisdictions use the KYC rule as one of the most important rules an advisor must follow.[114] KYC obligations mandate that advisors select investments that are suitable for their client's investment needs, time horizons, purpose of investment, and risk tolerances.[115] Breaches of KYC and suitability, while not amounting to a breach of fiduciary duties, do amount to breach of contract and potentially negligence.[116] In Canada, and the US, there are currently no KYC requirements for an advisor to ask about a client's preference, inclination or desire for RI. This lack of such a requirement is a problem as RI, on one hand, may pose diversification risks due to screens limiting assets available for investment, while on the other hand, RI may limit downsize risk on a client's portfolio.[117] Obligations of advisers must be enhanced by adding ESG factors to the KYC.[118]

In the US, FINRA Rule 2111 states that a

> member or an associated person must have a reasonable basis to believe that a recommended transaction or investment strategy involving a security or securities is suitable for the customer, based on the information obtained through the reasonable diligence of the member or associated person to ascertain the customer's investment profile.[119]

Suitability should encompass a client's willingness, desire, aptitude and appetite for RI investments.[120] There are forces that may dissuade an advisor from

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112 FCA, *supra* note 110, s. 601FC(1).

113 Australia *Corporations Act*, *supra* note 87, Part 7.7, Division 3, Subdivision C, s. 946A.

114 NI 31-103, *supra* note 69, s 13.2. *Kent v. May*, *supra* note 96 at para. 65, Dolden & Newnham, *supra* note 96 at 22-25.

115 *Suitability Obligation and Know Your Product*, CSA Staff Notice 33-315 (2009) 32 OSCB 6890.

116 *Kent v. May*, *supra* note 96 at 65.

117 Ick Jin, "Is ESG a systemic risk factor for US equity mutual funds" (2018) 8:1 J Sustainable Finance and Investment 72 at 73, 75.

118 RIA, *Comments Regarding CSA Consultation Paper 33-404: Proposals to Enhance the Obligations of Advisers, Dealers, and Representatives toward their Clients* (September 26, 2016).

119 FINRA, *Suitability* Rule 2111; *Know your Customer*, FINRA Rule 2090, R-FINRA-2010-039 and amended by SR-FINRA-2011-016 eff. (July 9, 2012).

discussing these investment vehicles, including fee structures, advertising, and educational requirements, the same forces that affect advice in Canada.

The Australian best interest standard ensures that advisors recommend financial products that are suitable, having regard to each client's objectives, financial situation, and needs.[121] However, unlike Canada and the US, there is specific guidance for environmental, social and ethical considerations. Australian guidance states that

> Advice providers must form their own view about how far s961B 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.[122]

(iv) Retail document disclosure

Clients cannot make informed, meaningful investment choices unless they obtain all necessary information. Advertising issues complement the problems with disclosures, as advertising includes all sales material provided to the investor.[123] The Fund Facts must be provided to clients for any sales of mutual funds.[124] The Fund Facts contains a description of the purpose of the fund and the appropriate investor, which will indicate whether the fund is intended to be an RI fund.[125] It describes relevant fund elements, including historical rates of return, fees, top holdings, investment mix, and risk rating. The "marketing pitch" from this document needs to be credible in that it should better illustrate how and why the underlying companies and assets are included. This shows the interlink between lack of material disclosures and the need for enhanced KYC and regulatory documents provided to retail investors. This applies to all advisors, regardless of the licensing body.

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[120] FINRA, "Suitability: What Investors Need to Know", online: <http://www.finra.org/investors/suitability-what-investors-need-know>.

[121] Australia *Corporations Act*, *supra* note 87, Part 7.7, s. 961B; see also ASIC, RG 175, (November 2017), ss. RG. 175.254, RG 175.309.

[122] *Ibid.* at RG 175.311.

[123] OSA, *supra* note 32, s. 50(2).

[124] *Mutual Fund Prospectus Disclosure*, *supra* note 38, *Point of Sale for mutual funds and segregated funds*, OSC Framework 81-406, (2008) 31 OSCB 10479; *Implementation of the Final Stage of Point of Sale Disclosure for Mutual Funds: Pre-Sale Delivery of Fund Facts — CSA Notice of Amendments to NI 81-101 Mutual Fund Prospectus Disclosure and to Companion Policy 81-101CP Mutual Fund Prospectus Disclosure* (2014) 37 OSCB 10985 [OSC 81-406]; *ETF Facts: Filing and Delivery Requirements for a Summary Disclosure Document for Exchange-Traded Mutual Funds*, OSC Framework (2016) 39 OSCB 9948; CSA Notice of Amendments to National Instrument 41-101 General Prospectus Requirements Form 41-101F4 *Information Required in an ETF Facts Document* (Form 41-101F4) (2017) 40 OSCB 1585

[125] *Ibid.*

Advertising regulations in the US is another potential issue of RI misrepresentation. FINRA Rule 2210 governs US rules around advertising and client communications.[126] RI is manifestly misunderstood in general, so it is not improbable that advisor communications may not reflect the true nature, intent and performance of RI. More importantly is the lack of communication and advertising for RI. A dearth of communication may be seen as indifference, or apathy towards RI. Lipton notes, "sharing sustainability information, corporate responsibility initiatives and progress publicly on the company's website and bringing them to these investors' attention are significant actions in the new paradigm."[127]

Continuous disclosure obligations in Australia are conducted via a Product Disclosure Statement, much like the Fund Facts in Canada.[128] The regulations contain "Good Disclosure Principles" which require timely, relevant and complete disclosure that promotes product understanding and facilitates product comparison all with regard to consumers' needs.[129] Content requirements include "fees payable in respect of a financial product; risks of a financial product; benefits of a financial product; and significant characteristics of a financial product."[130]

(v) Fee structures

NI 81-105 provides for permitted compensation structures, marketing practices, and other concerns.[131] Fees are usually taken as a percentage of assets, and so the higher the fees, the lower the returns and thus are directly related to performance. Fees are also tied to commissions via trailer revenue, which impacts advisor behaviour.[132] Advisors will often sell to clients the product that gives them the largest commission payment, whether or not this is in a client's best interest.[133] If an advisor is paid 60 bps on a "fund of fund" mutual fund, but only 50 bps on a standalone fund, there is a disincentive to provide advice on that standalone fund, especially if it is an RI fund.[134] Advisors will sell what is easy to sell, not necessarily what is in the client's long-term best interests.

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126 FINRA, Rule 2210 — *Advertising Regulation* (January 9, 2017).

127 *Martin Lipton, Wachtell, Lipton et al.*, "Succeeding in the New Paradigm for Corporate Governance", Harvard Law School Forum on Corporate Governance and Financial Regulation (2018), online: <https://corpgov.law.harvard.edu/2018/01/23/engagement-succeeding-in-the-new-paradigm-for-corporate-governance/>.

128 Australia *Corporations Act*, *supra* note 87 at part 7.9; ASIC, RG 168 *Disclosure: Product Disclosure Statements (and other disclosure obligations)* (October 28, 2011).

129 *Ibid.* at RG 168.4.

130 *Ibid.* at RG 168.38.

131 *Mutual Fund Sales Practices*, OSC NI 81-105 (2013) 36 OSCB (Supp-3).

132 *Investment Fund Continuous Disclosure,* OSC NI 81-106 (2018), 41 OSCB #40 (Supp-2), ss. 15.1, 17.1; see also Weinstein, *supra* note 80 at 16, 26, 28.

133 Weinstein, *supra* note 80 at 47, 75, 79.

The CSA is currently investigating the need to amend fee arrangement structures.[135] A recent CSA study found that funds that pay commission underperform other funds, with distribution costs raising expenses and lowering investment returns.[136] The study found advisors push investors into riskier funds, with compensation influencing the flow of money.[137] Larger embedded commissions stimulate sales, with recommendations being sometimes biased in favour of products that generate more commission for the advisor.[138] The evidence is clear: fee structures impact advice and product recommendations.

Commission is only one form of inducement that influences sales. Other inducements (advancement, recognition, etc.) can also influence sales.[139] Compensation affects the effort made by advisors to overcome investor behavioural biases, including biases that may lead to sub-optimal returns. It is not yet known if banning commission-based products in favour of asset or fee-based structures will result in a net improvement in the overall return to the investor.[140] Selling investments based on an improper match between risk propensity and the risk of the investment will not be eradicated by a change of compensation regime, but it will likely be diminished.[141] In jurisdictions that have moved to fee-based compensation, people with less wealth and less income find it harder to get advisory service than others.[142]

Like the CSA, FINRA has noted that the fee structure of certain products incents advisors to increase their sales.[143] Advisors employed by firms with proprietary funds tend to sell a higher proportion of their most profitable fund classes. Captive advisors are more likely to recommend in-house products.[144] Underlying licensure shapes the focus of advice.[145] Commission-only advisors sell individual equities in greater numbers and asset sizes than others, while ETFs are sold more by fee-only advisors.[146] Similar to the Canadian experience, there

[134] The author experienced this reality as an investment advisor for one of the large financial institutions.

[135] *Review of Practices Firms Use to Compensate and Provide Incentives to their Representatives*, OSC CSA Staff Notice 33-318 (2016) 39 OSCB 10115; CSA Discussion Paper and Request for Comment 81-407, *Mutual Fund Fees* (2012) 35 OSCB 11233.

[136] Weinstein, *supra* note 80 at 15.

[137] *Ibid*. at 25.

[138] *Ibid*. at 17.

[139] *Ibid*. at 26.

[140] *Ibid*. at 6.

[141] *Ibid*. at 7.

[142] *Consultation on the Option of Discontinuing Embedded Commissions*, CSA Consultation Paper 81-408 (January 10, 2017) at 76; IFIC, *IFIC Submission Re: Consultation Paper 81-408* (June 9, 2017) at 4.

[143] FINRA, "Report on Examination Findings" (December 6, 2017), online: <http://www.finra.org/industry/2017-report-exam-findings/product-suitability> at 6.

[144] Weinstein, *supra* note 80 at 35.

[145] *Ibid*. at 34.

is an inherent potential conflict of interest for suitability of investments due to compensation structures. This has repercussions for the entire industry but could have profound implications for RI products.

Fee structures have been studied in Australia.[147] Unlike Canada and the US, Australia has made the proactive choice to regulate commission structures. These regulations could curtail the potentially conflicting methods advisors use to artificially inflate their commission payments. Unfortunately, a recent amendment rolls back many of these amendments.[148] The ban on embedded commissions remains.[149]

(vi) Education

While commission and compensation are issues with all mutual fund products, not just RI, a more serious concern prejudicing RI uptake is the lack of knowledge of the advisor on RI. The educational requirements to be licensed under MFDA are simple and straightforward. There is only one required course, the Investment Funds of Canada (IFIC) course and exam.[150] There are no current educational requirements dealing with either ESG or RI issues. It is difficult to understand how MFDA representatives can accurately and materially recommend (or not recommend) RI investments if they have no education or knowledge on the subject.[151] Like MFDA advisor education, the importance of advisor education on IIROC advisors cannot be understated. The Canadian Securities Course (CSC) is currently the mandatory course to become an IIROC licensed advisor.[152] Like the mutual funds' exam, the CSC does not have an RI/ESG education component. It is thus doubtful that many IIROC advisors have the knowledge to understand and recommend RI products.

A broker-dealer agent ("Agent") in the US must complete the Series 7,[153] Series 63,[154] Series 66[155] and the new Securities Industry Essentials[156] (SIE)

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146 *Ibid*. at 38.

147 Australia, *Corporations Amendment, (Future of Financial Advice Act) 2012*, No 67, 2012 and *Corporations Amendment (Further Future of Financial Advice Measures) Act 2012*, No 68, 2012.

148 *Corporations Amendment (Financial Advice Measures) (Australia) Bill, 2016*, No. 22, 2016.

149 Herbert Smith, "ASIC's new 'fees for service' model: impact on takeovers and schemes", Lexology, online: <https://www.lexology.com/library/detail.aspx?g=828ba0b4-09ea-4715-bc27-c65a8862048f>.

150 IFIC, "IFIC exam" (Course list, 2017), online: <https://www.ifse.ca/courselist/canadian-investment-funds-course-cifc/>; Canadian Securities Institute offers *Investment Funds in Canada* (Course, CSI, 2017), online: <https://www.csi.ca/student/en_ca/courses/csi/ifc_info.xhtml>.

151 The certified financial planner is a designation only.

152 CSI, "Canadian Securities Course" (Course, CSI, 2018), online: <https://www.csi.ca/student/en_ca/courses/csi/csc.xhtml>.

153 FINRA, *Series 7 Exam - General Securities Representative Exam (GS)* [Series 7].

exams. The Agent must then register with the Central Registration Depository maintained by FINRA.[157] A candidate who passes the Series 7 exam is qualified for the solicitation, purchase and/or sale of all securities products, including corporate securities, municipal fund securities, options, direct participation programs, investment company products and variable contracts.[158] Thus, this includes stocks, bonds, mutual funds, ETFs. Series 7 is an equivalent to the CSC, and licensing would be similar to that of IIROC.[159] Series 65[160] are necessary to become a full independent Investment Advisor. Series 6 exams, on the other hand, are similar to MFDA requirements, in that the Series 6 exam assesses the competency of entry-level representatives to perform their job as investment company and variable contracts products representatives.[161] There is no mention of ESG criteria in either the Series 6 or Series 7 exams, or in the SIE.

ASIC has set the minimum training standards for all financial product advisors, not just investment advisors.[162] The type of training depends upon which products are advised.[163] However, qualifications in Australia are much more robust and onerous. Australian financial advisors must have a relevant bachelor or higher degree, or equivalent qualification.[164] These qualifications, plus the suitability requirements noted above, make if much more likely that advisors will have some familiarity with RI products.

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[154] FINRA, *Series 63 - Uniform Securities Agent State Law Examination* (Course, FINRA, 2018).

[155] FINRA, *Series 66 — Uniform Combined State Law Examination* (Course, FINRA, 2018), online: <http://www.finra.org/industry/series66>.

[156] As of October 1, 2018, FINRA Rule 1210.03 was updated to the new Series 7 and the Securities Industry Essential Exam, see "Securities Industry Essentials Exam", online: <http://www.finra.org/industry/essentials-exam>. There is still no ESG requirements for either exam. FINRA, "Securities Industry Essential Examination — Content Outline", online: <http://www.finra.org/sites/default/files/SIE_Content_Outline.pdf>; FINRA, *EC Approves Consolidated FINRA Registration Rules, Restructured Representative-Level Qualification Examinations and Changes to Continuing Education Requirements,* Regulatory Notice 17-30 (October 2017).

[157] E.g. *New Hampshire Securities Act*, Ch. 421-B Uniform Securities Act, at (B)9.

[158] Series 7, *supra* note 153.

[159] Financial Planner World, "Becoming a Financial Advisor in Canada", online: <https://www.financialplannerworld.com/canadian-advisor/>.

[160] FINRA, "Series 65 - Uniform Investment Adviser Law Examination" (Course, FINRA, 2018), online: <http://www.finra.org/industry/series65>.

[161] FINRA, "Series 6 Investment Company and Variable Contracts Products Representative Exam (IR)", online: <http://www.finra.org/industry/series6>. (Also amended October 1, 2018 per FINRA Rule 1210.03).

[162] ASIC, *Regulatory Guide 46, Licensing: Training of financial product advisers* (July 2012).

[163] *Ibid*. at RG 146.7.

[164] ASIC, "Professional standards for financial advisers", online: <https://asic.gov.au/regulatory-resources/financial-services/professional-standards-for-financial-advisers-reforms/>.

(b) Summary Conclusions

Current advisor licensing requirements create significant limitations for RI investment uptake. Mutual fund advisors should be able to provide advice on ETFs, bonds or CEDIFs, structures that as shown in the next section are more likely to be RI. Weinstein found that in the US, there are three other reasons for lower ETF sales:

1. Many financial advisors are not allowed to sell ETFs.
2. Some clients and advisors view "stock-picking" as the focus of their relationship.
3. Advisors may not be willing to expend the time and effort to get clients comfortable with a new product.[165]

Advisors, in both Canada and the US, have commission and compensation structures that favour some products over others which may limit promotion of RI funds. Fee structures that bias advice towards a current product or class of products should be banned. Poor investment decisions by investors around type and style of investment products appear to be the result of a "lack of financial awareness and education, better advertising of active-styled products, and more enthusiastic promotion of actively managed funds by intermediaries perhaps due to sales commissions, and overconfidence biases of investors and advisors and fund managers."[166] Fee structures need to be updated to ensure that RI funds are promoted as enthusiastically as higher commission paying funds.

Current KYC obligations do not mandate any RI-type questions, and it is highly recommended that suitability requirements be updated to incorporate ESG issues. Updating KYC requirements without updating education requirements would be ill advised, as advisors would not be able to provide the advice to satisfy their duty of care. Currently advisors do not have the training or education required for RI promotion. Mandating ESG factors as part of both a mutual fund and an investment advisor's education requirements would aid in RI uptake: "Overcoming these issues requires a mixture of regulation, education, overcoming misconceptions about ESG integration and toolkits for investment practice."[167]

Thus, all areas of advice in Canada contribute to a lack of RI uptake. It is inconceivable that an advisor can recommend the proper products for their clients without understanding either the client or the product.[168] US advisors,

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[165] Weinstein, *supra* note 80 at 38.

[166] Bollen, *supra* note 22 at 234.

[167] UNEP FI, *Fiduciary Duty in the 21st Century — Canada Roadmap* (New York: UNEP FI, 2017) at 5.

[168] FINRA, Rule 2111; Lawrence Ritcie, Louis Tsilivis & Marleigh Dick, "CSA publishes harmonized response to concerns regarding client-registrant relationship", Osler LLP (June 22, 2018) online: <https://www.osler.com/en/blogs/risk/june-2018/csa-publishes-harmonized-response-to-concerns-regarding-client-registrant-relationship.>

like their Canadian counterparts, may conflict due to compensation structures, and also like Canadian advisors, do not have the training required to provide advice on RI.

Australia has moved to a best interest standard, unlike Canada, and has already mandated fee structure changes to limit compensation conflicts. This best interest standard specifically includes mandates to ask clients about their environmental, social and ethical interests. Canada should implement Australia's enhanced duty of care standards, KYC ESG questions, and limits on fee compensation. This best interest standard would elevate the obligations of all advisors while still not becoming a fiduciary standard.[169] The June 2018 proposal would put the client's interest first when making a suitability determination.[170] Unfortunately, the CSA is backtracking on its reforms and RI, which could have been an unintended beneficiary, is an unintended casualty.[171]

3. ANALYSIS

The Mass Affluent, generally speaking, can only access MFDA advisors. IIROC advisors focus on high net worth and accredited investors, mainly due to fee and commission structures.[172] Mutual funds may not be the best vehicles to construct RI portfolios; however, they have been the default product for the Mass Affluent. Unfortunately, there is a paucity of RI mutual funds available to most Canadians.[173] There is especially a lack of accessibility to RI for clients of big banks, as only two banks offer funds with RI mandates.[174] Bank sales representatives must, generally, exclusively sell proprietary products from their FI and thus clients will not be able to access RI funds. Many independent

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169 Michelle Schriever, "Best Interest Standard Could be Fiduciary Duty in Disguise: Expert", Advisor.ca (October 3, 2016), online: <http://www.advisor.ca/news/industry-news/best-interest-standard-could-be-fiduciary-duty-in-disguise-expert-212984>; David Hodges, "Provincial Regulators Raise concerns about best interest standard for advisers", Canadian Press (May 11, 2017).

170 CSA, "Canadian securities regulators align to publish harmonized response to concerns with the client-registrant relationship" (June 21, 2018), online: <https://mailchi.mp/osc/canadian-securities-regulators-publish-harmonized-response-to-concerns-with-the-client-registrant-relationship?e=dcff75c17d>.

171 *Proposed Amendments to National Instrument 31-103 Registration Requirements, Exemptions and Ongoing Registrant Obligations*, CSA Notice (2018), 41 OSCB (Supp-1); Barbara Schecter, "OSC drops push for 'best interest' standard as regulators propose narrower reforms", Financial Post (June 21, 2018), online: <https://business.financialpost.com/news/fp-street/osc-drops-push-for-best-interest-standard-as-regulators-propose-narrower-reforms>.

172 Weinstein, *supra* note 80 at 74.

173 RIA, *Responsible Investment Funds in Canada* (December 31, 2017) (Toronto: RIA, 2018); State Street Advisors, "SPDR SSGA Gender Diversity Index ETF" online: <https://www.bloomberg.com/quote/SHE:US>; *BMO*, "Invest with Impact, Invest in Women", Release (February 16, 2017).

174 *Ibid.*

investment managers, insurance companies, and credit unions, also do not offer RI funds.[175] In other words, no firm provides access an RI investor would expect, and most funds are derivative offerings, with high fees.[176] US funds offer the potential to be more diversified than Canadian funds, given the larger number of companies based in the US, and it should be theoretically "easier" to construct a US equity fund that complies with the tenets of RI.[177] However, several of these funds have large minimum investments, so these were would cater to the accredited investor. Like Canada, none of the major US financial institutions (Wells Fargo[178] or JP Morgan Chase) or the large investment firms (such as Fidelity) create RI mutual fund products.[179] Wells Fargo Private Bank offers custom RI solutions, but only to accredited investors.[180] There are a few funds that specialize in water issues[181] or in women's rights[182] but, like in Canadian context, they are small niche funds. Thus, mutual funds do not currently offer true RI selection.

Licensing restrictions limit the availability of ETFs, as ETFs require similar prospectus disclosure as public companies.[183] Yet, there is much greater selection of RI ETFs, with ETFs constructed for environmentally responsible technologies, such as water, alternative energy, or green technology.[184] Global

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[175] Investors Group, "Socially Responsible Investing", online: <https://www.investors-group.com/en/investments/products/socially-responsible-investing-sri;> Manulife, "Responsible Investment", online: <http://www.manulifeam.com/ca/About-Us/Responsible-Investment-at-Manulife-Asset-Management/>; Desjardins, "Responsible Investment", online: <https://www.desjardins.com/ca/personal/wealth-management/our-solutions/responsible-investement/index.jsp>; IA Clarington, *IA Clarington Inhance Canadian Equity SRI Class* (March 31, 2018); Desjardins, "Desjardins SocieTerra Cleantech Fund, Fund Facts", online: <https://www.fondsdesjardins.com/information/00168_adf_a_en.pdf>; NEI, *NEI Canadian Equity RS Fund, Fund Facts* (July 12, 2018).

[176] Hawken, *supra* note 30.

[177] SIF, "Sustainable, Responsible and Impact Mutual Fund and ETF Chart", online: <https://charts.ussif.org/mfpc/> [SIF].

[178] Wells Fargo, "Mutual Fund Screener", online: <https://mutualfunds.wellsfargo.com/mutual-fund-center/mfScreener.aspx?#:L=N-T:AF=T:SO=T:MRC=0:p=1:c=NM:d=up>.

[179] SIF, *supra* note 177.

[180] Wells Fargo, "Social Impact Investing", online: <https://www.wellsfargo.com/the-private-bank/solutions/social-impact-investing/>.

[181] Calvert Research, "Calvert Water Fund", online: <https://www.calvert.com/Calvert-Global-Water-Fund-CFWAX.php>.

[182] Impax Asset Management, "Pax Ellevate Global Women's Leadership Fund", online: <https://paxworld.com/pax-ellevate/>.

[183] OSA, *supra* note 32, s. 1.1; *Amendments to National Instrument 81-101 Mutual Fund Prospectus Disclosure*, OSC NI 81-101 (2017) 40 OSCB 1584.

[184] Investopedia, "Going Green with Exchange Traded Funds", online: <http://www.investopedia.com/articles/exchangetradedfunds/11/going-green-with-etfs.asp#ixzz4Eu5X0yXO>; Blackrock Inc., "iShares Sustainable ETFs Investing for a Sustainable

water demand is increasing with the SDGs mandating access to water and sanitation.[185] There are no Canadian mutual funds that invest in water or water infrastructure but there is one Canadian ETF and two US ETFs that focus on water.[186] There are ETFs that focus on low carbon technologies,[187] clean technologies,[188] infrastructure,[189] battery technologies,[190] electric vehicles,[191] and Sustainable Development Goals (SDGs).[192] This contrasts with the mutual fund industry, which, save for one fund, offers no such opportunities. In short, ETFs offer a potential solution to the construction of RI.

Mass Affluent investors can only use bond mutual funds as part of their fixed income.[193] High net worth clients can access individual bonds. Green bonds offer the greatest opportunity for RI; however, they are generally not available to the Mass Affluent. In Canada, individual bonds are only available via an IIROC advisor. The 2017 TD green bond was available only through the TD Wealth Management IIROC network.[194] Ontario green bonds were issued via

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Future", online: <https://www.ishares.com/us/strategies/sustainable-investing/sustainable-etfs-product-overview>; iShares, "Jantzi Social Index ETF", online: <https://www.blackrock.com/ca/individual/en/products/239574/ishares-jantzi-social-index-etf>.

185 United Nations, *Transforming Our World: The 2030 Agenda for sustainable development. Draft resolution referred to the United Nations summit for the adoption of the post-2015 development agenda*, UN General Assembly, 2015, 69th session. UN Doc. A/70/L.1 of (September 18, 2015), SDG 7; UNESCO, *The United Nations World Water Development Report 2015 Water for a Sustainable World* (France: UN, 2015); Lady Justice Arden, "Water for all? Developing a Human Right to Water in National and International Law" (2016) 65 Int Comparative L Quar 771 at 787.

186 Blackrock Inc., "iShares Global Water Index ETF, Fund Facts", online: <https://www.blackrock.com/ca/individual/en/products/239755/ishares-sp-global-water-index-fund>; Invesco, "Invesco S&P Global Water Index ETF", online: <http://etfdb.com/etf/CGW/>.

187 iShares, "MSCI ACWI Low Carbon Target ETF (CRBN), Fund Facts", online: <https://www.ishares.com/us/products/271054/ishares-msci-acwi-low-carbon-target-etf>; SPDR MSCI ACWI Low Carbon Target ETF (LOWC).

188 Invesco, "Invesco Cleantech EFF, Fund Facts", online: <https://www.invesco.com/portal/site/us/investors/etfs/product-detail?productId=PZD>.

189 First Trust Advisors LP, "First Trust NASDAQ Clean Edge Smart Grid Infrastructure Index Fund" (GRID), online: <https://www.ftportfolios.com/retail/etf/etfsummary.aspx?Ticker=GRID>; NASDAQ OMX, "Clean edge Smart Grid Infrastructure", online: <https://cleanedge.com/indexes/stock-index/qgrd>.

190 Global X Funds, "Lithium & Battery Tech ETF", online: <https://www.globalxfunds.com/funds/lit/>.

191 Global X Funds, "Autonomous & Electric Vehicles ETF", online: <https://www.globalxfunds.com/funds/driv/>.

192 *iShares MSCI Global Impact ETF* (MPCT).

193 Green bond funds do not yet exist in Canada. US, Calvert Investments, "Calvert Green Bond Fund (A)", online: <https://www.calvert.com/Calvert-Green-Bond-Fund-CGAFX.php>.

prospectus, so only IIROC advisors have access.[195] Government documents state that the province may examine opportunities to sell Green Bonds directly to retail investors, but only if it is cost effective and after the domestic market has matured.[196] Both bonds were oversubscribed, so it was a missed opportunity to allow retail investors the ability to purchase this vehicle, stimulating interest in green bonds. It is this questionable line of thinking that prevents RI uptake from hitting the mainstream.

US and international investors have similar problems as Canadian retail investors. Many issuers in the US fear a green bond issuance due to potential litigation due to claims of misrepresentation, leaving large organizations to issue green bonds to which mass affluent investors cannot access.[197] Access in Australia to green bonds is also very limited. National Australia Bank launched Australia's first green mortgage bond in 2018.[198] It had pricing similar to a non-green bond, (i.e. no greenium), yet the bond was oversubscribed.[199] The largest investor has been asset managers and individual investors cannot purchase these bonds.[200] The World Bank has issued green bonds but investors in these bonds are almost solely institutional investors,[201] with few issuances available to

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194 TD Bank, "TD Bank Green Bond DNV GL Eligibility Assessment", online: <https://www.td.com/document/PDF/Verification_Statement.pdf>.

195 Ontario, "Green Bonds", online: <http://www.ofina.on.ca/greenbonds/>; Sean Kidney, "Ontario issues long-awaited inaugural green bond", CBI (October 6, 2014), online: <https://www.climatebonds.net/2014/10/ontario-issues-long-awaited-inaugural-green-bond-cad-500m-4481m-175-4yrs-aa2e-mixed>.

196 Ontario, "Ontario Green Bond Q&A's" (January 26, 2017), online: <http://www.ofina.on.ca/greenbonds/>.

197 Kate Allen, "Strict US market rules limit corporate sellers of green bonds", Financial Times (February 20, 2018), online: <https://www.ft.com/content/baa217c4-157c-11e8-9376-4a6390addb44>; Cicero, '*Second Opinion' on Fannie Mae Multifamily Green Bond Framework* (June 8, 2018); Alicia Jones, "Fannie Mae Wins Recognition as Largest Issuer of Green Bond by the Climate Bonds Initiative", Press Release (March 20, 2018); BoA, "Bank of America Issues Its Third and Largest Green Bond", Press Release (November 10, 2016).

198 NAB, *NAB Climate Bonds*, online: <https://capital.nab.com.au/information/green-and-sri-bonds>.

199 Paulina Duran, "Australia green bond market muzzled by policy uncertainty", Reuters (February 5, 2018), online: <https://www.reuters.com/article/us-australia-bonds-green/australia-green-bond-market-muzzled-by-policy-uncertainty-idUSKBN1FP0OS>.

200 Cole Latimer, "Climate bonds market to hit a new benchmark in 2018", Sydney Morning Herald (January 10, 2018), online: <https://www.smh.com.au/business/banking-and-finance/2018-the-year-of-the-green-bond-20180109-p4yycb.html>; Oliver Yates, "Australia's budding green bond market", Clean Energy Finance Corp. (June 2015), online: <https://www.cefc.com.au/media/feature-articles/files/australias-budding-green-bond-market/>.

201 World Bank, *Green Bond Impact Report* (Washington, DC: World Bank Treasury, 2017) at 7; World Bank, "Green Bonds Attract Private Sector Climate Finance", Press Release (June 10, 2015), online: <http://www.worldbank.org/en/topic/climatechange/brief/

Accredited Investors.[202] There are no World Bank green bonds for the Mass Affluent. In sum, the ability of any Mass Affluent retail investor to procure a green bond is extremely limited. A green bond ETF is the only current method to invest in these vehicles.[203]

Institutional investors have an advantage as they are able to purchase investments inaccessible to the retail investor.[204] The Greening Canada Fund (GCF) invested directly in carbon credits and is an example of an alternative model mandated to combat climate change.[205] The advantages/disadvantages of offsets are outside the scope of the article.[206] The GCF followed a private equity model, rather than a mutual fund structure.[207] The offering was by a private placement and was unavailable to the public.[208] Ironically, despite the lack of a prospectus, investors had more information available to them prior to purchase than an investor would normally have.[209] Securities law thus may have it wrong. It is not the complexity or structure of the product that should warrant public

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green-bonds-climate-finance>; World Bank, "Green Bonds", online: <http://treasury.worldbank.org/en/about/unit/treasury/ibrd/ibrd-green-bonds>.

202 World Bank, World Bank Launches First Kangaroo Green Bond, Press Release (April 16, 2014); World Bank, "World Bank Green Bonds for Merrill Lynch Wealth Management Investors", Press Release (June 8, 2011), online: <https://www.worldbank.org/en/news/press-release/2011/06/08/the-world-bank-and-bank-of-america-merrill-lynch-announce-world-bank-green-bonds-for-merrill-lynch-wealth-management-investors>.

203 S&P Dow Jones, "A Look Inside Green Bonds: Combining Sustainability With Core Fixed Income" (May 2018), online: <https://ca.spindices.com/indices/fixed-income/sp-green-bond-index>; *iShares*, "ESG USD Corporate Bond ETF", online: <http://etfdb.com/etf/SUSC/>.

204 S. Kaplan & A Schoar, "Private equity performance: returns, persistence, and capital flows" (2005) 60 J Finance 1791, Keith Black, "Defining Liquid Alternative Investments" (2015) 17:3 J Alternative Investments 6 at 8; UN PRI, *Integrating ESG in Private Equity: A Guide for General Partners* (New York, PRI, 2014); Patricia Crifo, Vanina Forget & Sabrina Teyssier, "The price of environmental, social and governance practice disclosure: An experiment with professional private equity investors" (2015) 30 J Corporate Finance 168 at 169.

205 Greening Canada Fund LP., *Amended and Restated Limited Partnership Agreement* (September 30, 2009), S. 3.1.

206 Kathy Dhanda & Laura Hartman, "The Ethics of Carbon Neutrality: A Critical Examination of Voluntary Carbon Offset Providers" (2011) 100 J Business Ethics 119; Shi-Ling Hsu, "International Market Mechanisms" in *The Oxford Handbook of International Climate Change Law*, Cinnamon Carlarne, Kevin Gray, and Richard Tarasofsky (eds) (Oxford University Press, 2016) at 249; Brianne Riehl et al., "Lessons Learned in Mandatory Carbon Market Development" (2017) 10:3-4 Int Rev Env and Resource Economics 227.

207 Greening Canada Fund LP, *Limited Partnership Interests, Confidential Offering Memorandum* (September 17, 2009).

208 *Ibid.*

209 Marcelo Labbe & Colin Atkinson, "On the pricing of Emission Reduction Purchase Agreement contracts" (2010) 3:2 J Energy Markets 69.

access; rather it is the amount of information that could allow investors to make informed decisions. Had a prospectus offering been made, the fund could have been made available to IIROC-based retail investors. Structured as a mutual fund, the fund could have been marketed to the Mass Affluent.

Given their local focus, CEDIFs should be a valuable tool to use for RI and could be structured to provide tangible ESG benefits, but accessibility by most Mass Affluent investors is precluded.[210] A purchaser must use an IIROC advisor, yet not all IIROC advisors can access this vehicle.[211] A mutual fund of several CEDIF entities should be created to offer diversification to reduce the inherent risks in a CEDIF.[212] Jurisdictions could use this as a true model of a unique legal structure to "incent" investors to incorporate using this structure.

(a) Summary Conclusions

ETFs show more evidence of "RI-ness" as there are ETFs that invest in low carbon, alternative energy, water, solar, and cleantech. ETFs are not riskier than funds and precluding investors from accessing vehicles due to structure rather on complexity fails to protect investors from risk. There does not seem to be a solid justification for preventing greater access to these products. Green bonds also hold great promise but are not made readily available to the Mass Affluent. They are not structurally different from other bonds, so there is no justification for why they are not part of a fixed income mutual fund. To access ETFs, bonds, and CEDIFs only two options currently exist. The first is to go to an IIROC licensed investment advisor, but as noted, most of these advisors have large minimum investment assets making this not an option for the Mass Affluent. The second option is to use an online brokerage account, but most clients do not have the time, energy or ability to undertake "do it yourself" investing. Most Mass Affluent investors need the services of an advisor. The unfortunate reality is that there is an inherent lack of accessibility for the Mass Affluent. At the retail level, access, not theory is what is needed. MFDA and Series 6 licensed representatives need to be allowed to sell a wider array of products, including ETFs and green bonds.

New regulations around the licensing of MFDA advisors are required. New structures of fixed income investments that are available to the Mass Affluent are required. FIs must eliminate propriety offerings, or at the very least, allow their advisors access to the universe of investments within their licensing.

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[210] Cedif.ca, "Community Economic Development Investment Funds", online: <http://cedif.ca/funds/bca-investment-co-operative-limited/>.

[211] CEDIF Regs, *supra* note 58, s. 3(4) *CEDIF Application Process FAQs*, para. 12, C*ommunity Economic Development Investment Funds*, NSSC CP 45-601 (January 17, 2014) ss. 1.2, 3(4) Wind4all Communities III Inc., *Offering Memorandum* (January 14, 2016) at 29.

[212] *Ibid.* at 13.

4. CONCLUSION

Securities laws are designed to "protect" Mass Affluent investors against loss due to complex structures, creating a system whereby most investors do not have access to all investment vehicles. Retail investors need RI products. MFDA advisors should be able to access all types of mutual funds, granting access to specialized products and certain CEDIFs. A better method of "mainstreaming" RI is required. This article is not advocating for all products be available to all advisors, as any specific investment must be reviewed to determine suitability, and this article is not advocating for its use as a valid or "good" investment option. Rather, regulators must look at broadening the options available for RI investments.

Secondly, standards for retail advisors must improve. Implementing a best interest standard, along with enhanced pay structures and education requirements on RI is necessary. More informed advisors with knowledge of potential RI options would encourage investment. Aligning pay and commission structures would help RI uptake and it would stop the disincentive of promoting products that pay the advisor better, rather than the client preference.

Timing could not be better for change, as there are many other issues that securities regulators are dealing with for mutual funds and advisors. However, CSA backtracking makes this unlikely, which is cause of concern for RI going forward.