BLACKROCK®

September 30, 2016

Submitted via electronic filing: comments@osc.gov.on.ca; consultation-en-cours@lautorite.qc.ca

British Columbia Securities Commission
Alberta Securities Commission
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
Financial and Consumer Services Commission (New Brunswick)
Office of the Superintendent of Securities, Prince Edward Island
Nova Scotia Securities Commission

Attention:
Josée Turcotte
Ontario Securities Commission
20 Queen Street West
22nd Floor
Toronto, ON M5H 3S8

Me Anne-Marie Beaudoin
Corporate Secretary
Autorité des marchés financiers
800, square Victoria, 22e étage
C.P. 246, tour de la Bourse
Montréal, QC H4Z 1G3

Re: Canadian Securities Administrators Consultation Paper 33-404 – Proposals To Enhance the Obligations of Advisers, Dealers, and Representatives Toward Their Clients ("Proposed Reforms")

Dear Sirs/Mesdames:

A. About BlackRock

BlackRock Asset Management Canada Limited ("**BlackRock Canada**" or "**we**") is an indirect, wholly-owned subsidiary of BlackRock, Inc. ("**BlackRock**") and is registered as a portfolio manager, investment fund manager and exempt market dealer in all the jurisdictions of Canada and as a commodity trading manager in Ontario.

BlackRock is one of the world's leading asset management firms, managing assets for clients in North America and South America, Europe, the Middle East, Africa, Asia and Australia. Our client base includes corporate, public, multi-employer pension plans, insurance companies, mutual funds and exchange-traded funds, endowments, foundations, charities, corporations, official institutions, banks and individuals around the world.

As of June 30, 2016, BlackRock's assets under management totalled US$4.890 trillion across equity, fixed income, cash management, alternative investment, real estate and advisory products.

B. General Observations

BlackRock commends the Canadian Securities Administrators ("**CSA**") on its ongoing efforts to enhance the client-registrant relationship and ultimately improve outcomes for investors. As a general principle, we support initiatives that encourage long-term savings by improving the quality of advice, better aligning interests of registrants with those of their clients, and broadening the choice of investments and services offered to investors.

The key investor protection concerns outlined in the Proposed Reforms are ones which with we agree, but have reservations regarding the statement that "clients are not getting the value or returns they could reasonably expect from investing"[1]. This is the first time the CSA has provided what appears to be an expectation about the performance of a client's portfolio. With respect, we are worried this statement may create a regulatory expectation that all registrants must generate at least a minimal rate of return for their clients, even if the markets as a whole are down and all regulatory obligations applicable to the registrant are met. Such a high bar is concerning.

Moreover, the BIS Consulting Jurisdictions note that the proposed regulatory best interest standard is "not intended to guarantee that clients' investments never lose value, result in the "best" or "highest" returns for the client, or result in the lowest risk"[2]. However, when combined with the proposed suitability requirement that registrants identify a target rate of return clients will need in order to achieve their investment needs and objectives[3], we are concerned that the proposed best interest standard will be misinterpreted by clients as guaranteeing a rate of return, and may, contrary to the CSA's intentions, further exacerbate the expectations gap between clients and registrants. If the issue truly lies with the fact that the current suitability obligation is not clearly worded, then the Proposed Reforms can do much to address this. However, we question the appropriateness of attempting to regulate "investment outcomes".

In addition, prescriptive rules can preclude flexibility in service offerings. Not all clients want or require a full financial plan (which also requires clients to disclose significant information regarding their personal circumstances). The CSA should be thoughtful about not introducing requirements that will reduce the service options available to investors, or which require investors to disclose more information than necessary to obtain the service they desire, as this may have the overall impact of reducing access to advice for investors.

Beyond this general caution, we have questions and concerns regarding certain elements of the Proposed Reforms, which are set out in greater detail below. For ease of reference, we have included the full text of each consultation question to which our comments correspond.

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1 Proposed Reforms, page 3956.

2 Proposed Reforms, page 3968.

3 Proposed Reforms, page 3989.

C. BlackRock's Responses

1. Targeted Reforms

A. Conflicts of Interest

Question 1 – Is this general approach to regulating how registrants should respond to conflicts optimal? If not, what alternative approach would you recommend?

BlackRock agrees with the CSA's desire to better align the interests of registrants with the interests of their clients, and generally supports the CSA's proposed approach with regard to identifying and appropriately addressing conflicts of interest affecting registrants. While certain elements of the Proposed Reforms provide welcome clarifications to the current guidance in National Instrument 31-103 – *Registration Requirements and Exemptions* and its companion policy ("**NI 31-103**") we believe that certain other elements of the Proposed Reforms require further consideration.

We are concerned with the proposed requirement that firms/representatives should have a reasonable basis for believing that a client fully understands the implications and consequences of each conflict of interest that is disclosed. In our view, requiring registrants to make this type of subjective judgement goes beyond seeking to align interests and shifts undue onus onto registrants. We expect that this requirement will be complex to meaningfully implement on a large scale. It may also put registrants in a difficult position when dealing with unsophisticated or vulnerable investors and may create undue risk for registrants in advising these types of clients. We are concerned that introducing this requirement could have the unintended consequence of reducing access to advice for such investors. In addition, it is not clear in the proposal what process the CSA expects registrants to follow in ascertaining client understanding and what documentation the CSA will require from a registrant in order to support the registrant's determination regarding a client's understanding.

BlackRock has the same reservations regarding the similar proposed requirement in the relationship disclosure targeted reforms, which would require a registrant to have a reasonable basis for concluding that a client fully understands the implications and consequences of the content of such disclosure. In our view, rather than attempting to regulate a client's understanding of a registrant's conflicts of interest disclosure, it is more appropriate for the CSA to focus on requiring registrants to provide prominent, clear, and meaningful disclosure in order to address any information asymmetry concerns. Ultimately, a client's understanding is not fully within a registrant's control, while the content and timing of providing disclosure is.

BlackRock is also of the view that the proposed requirement to include within a conflicts management framework a "clear delineation of firm and representatives' responsibilities with respect to identifying and managing conflicts of interest" is impractical to implement. We do not believe that a bright line always exists in the case of conflicts of interest, and this line may move depending on new facts. As such, we would encourage the CSA to provide more specific guidance with respect to the expected delineation.

Furthermore, the guidance in the Proposed Reforms as currently drafted requires a firm to disclose *material* conflicts of interest, but then stipulates that this disclosure should include all outside business activities of the firm and applicable representatives, without regard to materiality. We question the purpose of disclosing immaterial outside business activities, as we

do not believe this information is meaningful to investors and may detract from other, more material disclosure.

We would also welcome specific guidance from the CSA with regard to the proposed requirement that a firm periodically test its conflicts management framework, including the CSA's view regarding the essential elements of an effective testing program.

Question 2 – Is the requirement to respond to conflicts "in a manner that prioritizes the interest of the client ahead of the interests of the firm and/or representative" clear enough to provide a meaningful code of conduct? If not, how could the requirement be clarified?

We encourage the CSA to provide further guidance on this requirement, including specific examples, in order to ensure all registrants have a clear understanding of the CSA's expectations and what actions will and will not be viewed as adequately prioritizing a client's interest.

Question 3 – Will this requirement present any particular challenges for specific registration categories or business models?

For firms that trade in or advise on proprietary products, the CSA cite an inherent conflict between the incentive to recommend the proprietary product and ensuring adherence to applicable suitability obligations[4]. The CSA indicate that such firms must not rely on disclosure alone in responding to these conflicts, and must implement thorough controls that effectively mitigate the conflict[5]. We request that the CSA confirm that this statement does not apply to firms that solely service sophisticated clients.

Question 44 – Is it appropriate that disclosure by firms be the primary tool to respond to a conflict of interest between such firms and their institutional clients?

We believe that disclosure is an appropriate primary tool to respond to conflicts of interest between firms and their sophisticated clients, as we believe that many of the concerns underlying the Proposed Reforms, particularly information and financial literacy asymmetry, are less prevalent when providing services to sophisticated clients. Moreover, we are of the view that the current disclosure requirements, as set out in NI 31-103, adequately meet the needs of sophisticated clients.

In our experience, sophisticated clients often actively engage in detailed discussions with registrants on matters that are of particular concern to them, including performance and conflicts of interest, and frequently negotiate key terms in engaging a firm, including with respect to fees and/or product costs. In addition, many sophisticated clients have access to additional expertise and resources to assist them in understanding the disclosure provided.

We note that the CSA has indicated that there are a sub-set of conflicts of interest that cannot be adequately mitigated through disclosure to sophisticated clients, and must be avoided entirely. To assist registrants in understanding and applying these boundaries, further guidance, citing specific examples, would be welcome. As a general comment, further clarification in

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4 Proposed Reforms, page 3977.

5 Proposed Reforms, page 3976.

Appendix A regarding which obligations will apply to a registrant when dealing with sophisticated clients when a conflict arises would be helpful.

Question 46 – Is this definition of "institutional client" appropriate for its proposed use in the Companion Policy? For example: (i) where financial thresholds are referenced, is $100 million an appropriate threshold?; (ii) is the differential treatment of institutional clients articulated in the Companion Policy appropriate?; and (iii) does the introduction of the "institutional client" concept, and associated differential treatment, create excessive complexity in the application and enforcement of the conflicts provisions under securities legislation? If not, please explain and, if applicable, provide alternative formulations.

Question 47 – Could institutional clients be defined as, or be replaced by, the concept of non-individual permitted clients?

BlackRock believes the differing treatment of sophisticated clients, as articulated in the Proposed Reforms, is appropriate for the reasons cited above. However, BlackRock has strong reservations regarding the introduction of an additional category of sophisticated clients given the existing definitions of "accredited investor" and "permitted client" in applicable securities legislation. We believe that adding a further definition will lead to unnecessary complexity for registrants and potential confusion for clients. For example, under the proposed definition of "institutional client", a prospective investor could qualify as an accredited investor and/or permitted client for purposes of participating in a private placement, but may not qualify as an "institutional client" for purposes of conflicts of interest and relationship disclosure. It is unclear why, in this limited context, sophisticated clients would be deemed in need of additional relationship and conflicts disclosure, while they are not required to be provided with prospectus-level disclosure regarding their investments. This inconsistency could result, for example, in clients within the same pooled fund having different information provided to them. For these reasons, BlackRock encourages the CSA to adopt either of the existing "accredited investor" or "permitted client" definitions as currently set out in applicable securities legislation. In addition, we encourage the CSA to consider whether the use of a novel definition in the Proposed Reforms could lead to a competitive disadvantage as between registrants and international firms relying on registration exemptions that are permitted to offer their products or services to "permitted clients".

With respect to the use of a financial threshold, we believe that $100 million is too high for the Canadian market. This threshold may make sense in larger markets such as the United States, where, as of December 2015, the total externally managed assets under management for U.S. pension plans was approximately $28,313 billion (U.S. $21,779 billion)[6]. Comparatively, this figure is approximately $1,908 billion[7] for Canadian pension plans. Given the large disparity in market size, BlackRock strongly suggests that the CSA not implement financial thresholds.

B. Sales Practices

Question 49 – Are specific prohibitions and limitations on sale practices, such as those found in NI 81-105 appropriate for products outside the mutual fund context? Is guidance in this area sufficient?

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[6] Willis Towers Watson, *Global Pension Assets Study*, 2016. All values in USD have been converted to CAD using a foreign exchange rate of 1 USD = 1.3 CAD.

[7] Investor Economics, *Managed Money Report*, Spring 2016.

Question 50 – Are limitations on the use of sales practices more relevant to the distribution of certain types of products, such as pooled investment vehicles, or should they be considered more generally for all types of products?

Questions 52 – What type of disclosure should be required for sales practices involving the distribution of securities that are not those of a publicly offered mutual fund, which are already subject to specific disclosure requirements?

BlackRock cautions the CSA from taking a "one size fits all" approach with respect to sales practices, given the key differences between publicly-offered mutual funds and products offered in the exempt market. In our experience, products offered in the exempt market typically do not include embedded commissions. In addition, intermediaries do not wield as much influence in this space, as distribution of these products to sophisticated clients that qualify as accredited investors or permitted clients often occurs directly, without the use of an intermediary. Where those investors are of an institutional nature, they are also often limited by their own internal policies and/or procedures and other existing legal requirements with respect to accepting gifts and entertainment or other inducements. Sophisticated clients also often have detailed and consistent metrics by which they measure and review the performance of their investments and their advisors, which helps to mitigate the influence of sales practices.

For these reasons, BlackRock does not believe it is necessary to introduce specific prohibitions or limitations on sales practices for products outside of the publicly-offered mutual fund context, nor that disclosure in addition to current requirements under NI 31-103 is required.

Question 51 – Are there other requirements that should be imposed to limit sales practices currently used to incentivize representatives to sell certain products?

Question 53 – Should further guidance be provided regarding specific sales practices and how they should be evaluated in light of a registrant's general duties to his/her/its clients? If so, please provide detailed examples.

In order to better align the interests of registrants with those of their clients, BlackRock is strongly supportive of measures that simplify and clarify the sales practices regime for publicly-offered mutual funds. BlackRock suggests that the CSA consider introducing more prescriptive limitations or caps on these activities. For example, the CSA may consider implementing per-dealing representative limits of $250 per year for gifts.

C. Know Your Client

Questions 4 – Do all registrants currently have the proficiency to understand their client's basic tax position? Would requiring collection of this information raise any issues or challenges for registrants or clients?

Question 54 – To what extent should the KYC obligation require registrants to collect tax information about the client? For example, what role should basic tax strategies have in respect of the suitability analysis conducted by registrants in respect of their clients?

BlackRock acknowledges that taxes can have an important impact on investment outcomes. However, we respectfully disagree with the CSA's proposal that registrants take reasonable steps to obtain sufficient information about their clients' basic tax position and to use this information as part of their suitability analysis.

Tax is a highly complex and fact-driven field, in which minor differences in taxpayer circumstances can have a major impact on outcomes. There are entire professions and groups of professionals that specialize in understanding and advising clients on their tax affairs. Registrants, by contrast, are experts in providing advice on and/or transacting in securities, and generally do not have a level of tax proficiency commensurate with that of trained tax professionals.

By legislating that tax discussions become a part of the KYC and suitability processes, the CSA risks leading investors to rely solely on registrants for tax advice, thereby exacerbating concerns regarding misplaced trust and reliance. We believe that this is not in the best interests of investors, as there is an increased risk that key facts could be overlooked and/or misinterpreted, leading to costly errors.

If the CSA feels strongly about requiring registrants to develop and apply tax knowledge, we believe it would be more appropriate, and less risky for registrants, to situate this obligation within the proposed Know Your Product requirements. In this context, a registrant could take reasonable steps to understand the basic tax characteristics of the securities it offers/trades as part of the registrant's initial and ongoing diligence processes. This could include, for instance, understanding whether a security is a registered investment, whether it is an eligible investment for registered plans and identifying the tax characteristics of distributions paid on different securities.

D. Know Your Product – Firms

Question 8 – The intended outcome of the requirement for mixed/non-proprietary firms to engage in a market investigation and product comparison is to ensure the range of products offered by firms that present themselves as offering more than proprietary products is representative of a broad range of products suitable for their client base. Do you agree or disagree with this intended outcome? Please provide an explanation.

Question 9 – Do you think that requiring mixed/non-proprietary firms to select the products they offer in the manner described will contribute to this outcome? If not, why not?

BlackRock commends the CSA on its ongoing efforts to protect investors and to preserve investor choice. We do, however, have some concerns with the KYP requirements for firms as currently drafted. We believe that the bifurcation of firms into proprietary and mixed/non-proprietary models does not address the key investor protection concerns contemplated by the CSA, introduces excessive complexity, and may, contrary to the CSA's objectives, inadvertently decrease investor choice and create an opportunity for regulatory arbitrage.

Specifically, we believe that the proposed requirements for mixed/non-proprietary firms to engage in a "fair and unbiased market investigation, a product comparison and an optimization process"[8], while well intentioned, are difficult to interpret and unduly onerous as compared with the requirements contemplated for proprietary firms.

In order to satisfy the requirement noted above, mixed/proprietary firms would be required to incur significant additional costs, which could include procuring expensive third party research

[8] Proposed Reforms, page 3986.

reports, increased compliance burdens, technology builds and hiring additional personnel or service providers. Alternatively, proprietary firms may satisfy their KYP requirements through internal due diligence and disclosure.

Question 11 – Will this requirement raise challenges for firms in general or for specific registration categories or business models? If so, please describe the challenges.

Question 12 – Will this requirement cause any unintended consequences? For example, could this requirement result in firms offering fewer products? Could it result in firms offering more products?

Question 13 – Could these requirements create incentives for firms to stop offering non-proprietary products so that they can fit the definition of proprietary firm?

BlackRock has concerns that firms who fall within the definition of "mixed/non-proprietary" may shift to a strictly proprietary model in order to avoid the additional regulatory requirements and attendant costs. Such a model could create a competitive advantage for large, vertically-integrated firms and present significant distribution challenges for small and independent providers. Antithetically, this could result in fewer products being offered by fewer firms.

In addition, as the CSA recognizes through the guidance in Appendix A on conflicts of interest related to compensation structures, the focus on justifying the product list of mixed/proprietary firms may be misplaced. Should there be a decrease in mixed/proprietary business models, the CSA could be exacerbating the conflicts which the Proposed Reforms are intended to ameliorate.

Similarly, we worry that the costs of complying with the regime as proposed will ultimately be passed on to investors in the form of increased fees. This could also encourage some firms to narrow the scope of their client base to only those with assets over a certain threshold, thereby reducing access to advice for smaller retail investors.

Question 10 – Are there other policy approaches that might better achieve this outcome?

We believe that regulation can drive effective change by focusing on the delivery of a client-centered advice model rather than an incentives-driven model. To that end, we suggest that rather than delineating between business models, the CSA instead focus on ensuring that the remuneration and pricing models of registrants are aligned with their clients' goals. In this regard, we support the recent work of the CSA relating to mutual fund fee reform, and encourage the CSA to also ensure that firms and representatives do not receive any additional compensation or incentives for offering proprietary products. In addition, we support the CSA's continued review of sales practices that may give rise to material conflicts of interest with a view to prioritizing the interest of the client in receiving unbiased advice.

E. Relationship Disclosure

Question 23 – Do you agree with the proposed disclosure required for firms registered in restricted categories of registration? Why or why not?

Please confirm that the obligations set out under "Restricted Registration Category Disclosure" in Appendix F will not apply when firms deal with sophisticated clients (there appears to be an

omission in the Appendix that is inconsistent with the summary description of the proposed targeted reforms).

Question 27 – Would additional guidance about how to make disclosure about the relationship easier to understand for clients be helpful?

We would welcome further guidance from the CSA regarding their expectations for registrants describing the "actual nature of the client-registrant relationship".

F. Suitability

Question 63 – Should we provide further guidance on the suitability requirement in connection with ongoing decisions to hold a position?

We are concerned with proposed requirement that firms and representatives must perform a suitability analysis of a client's portfolio upon the occurrence of a "significant market event" to which the client is exposed[9]. In our view, the lack of a definition of "significant market event" could create uncertainty, and may be difficult and costly to implement in practice. We also worry that this requirement could feed panic with respect to market events, and could lead to a focus on short-termism, rather than constructive, long-term strategies. Rather than requiring a full suitability analysis, we suggest instead that the CSA revise the Proposed Reforms to instead require a registrant to *consider* whether a market event requires a review of client accounts.

2. Regulatory Best Interest Standard Proposal

Question 36 – Please indicate whether a regulatory best interest standard would be required or beneficial, over and above the proposed targeted reforms, to address the identified regulatory concerns.

BlackRock strongly supports the underlying policy goal of strengthening the principled foundation of the client-registrant relationship, and welcomes outcome-oriented reforms aimed at improving the investor experience. We do, however, have reservations about the implementation of a regulatory best interest standard as currently proposed.

The CSA has recently implemented or proposed a number of initiatives aimed at strengthening the client-registrant relationship and addressing investor protection concerns, including CRM 2, Point of Sale disclosure for mutual funds, ETF summary documents, and the soon-to-be released consultation on mutual fund fee reform. We strongly encourage the CSA to carefully assess the impact and effectiveness of these changes, together with the proposed targeted reforms, prior to considering the implementation of a further overarching best interest standard. It may be that the CSA has already addressed, or proposed to address, relevant policy concerns through targeted securities regulation.

Furthermore, BlackRock strongly advocates for harmonization of securities regulation in order to promote the efficient functioning of Canadian capital markets. In this regard, we have serious concerns about the impacts of a regulatory best interest standard that is not introduced consistently across all Canadian jurisdictions. The absence of a harmonized and integrated regime may exacerbate confusion and legal uncertainty, increase costs which may be ultimately

[9] Proposed Reforms, page 3991.

borne by investors, create the potential for regulatory arbitrage, and, ultimately, create an environment that limits investor choice.

D. Conclusion

BlackRock appreciates the opportunity to provide input on this important regulatory initiative and would be pleased to make appropriate representatives available to discuss any of these comments with you. We would also be happy to participate in any roundtable discussions.

Sincerely,

"Margaret Gunawan"

Margaret Gunawan
Chief Compliance Officer and Secretary, BlackRock Asset Management Canada Limited