



October 19, 2020

Via Electronic Submission

The CFA Institute

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Re: Consultation Paper on the Development of the CFA Institute ESG Disclosure Standards for Investment Products

OVERVIEW

The Portfolio Management Association of Canada (**PMAC**), through a working group consisting of CFAs and ESG experts and through its wider Industry, Regulation & Tax Committee, is pleased to have the opportunity to submit the following comments regarding the CFA Institute's Consultation Paper on the Development of the CFA Institute ESG Disclosure Standards on Investment Products (the **Consultation** and the **Standard**, respectively).

PMAC represents over [280 investment management firms](#) registered to do business in Canada as portfolio managers. Some firms manage large mutual funds or pooled products and others manage separately managed accounts on behalf of private clients or pension plans and foundations. In addition to this primary registration, most of our members are also registered as investment fund managers and/or exempt market dealers. PMAC's members encompass both large and small firms managing total assets in excess of N \$2.8 trillion for institutional and private client portfolios.

GENERAL COMMENTS

The following context about PMAC's members is important to our comments on this Consultation and will help inform the CFA Institute's understanding of our perspective on the Standard. Our member firms range from asset managers that operate globally and are subject to a plurality of legal and regulatory requirements to smaller firms that operate solely within Canada.

PMAC's mission statement is "advancing standards" and, as part of our effort to support that mission, upon applying for PMAC membership, we require all member firms to attest that: 1) they have adopted the CFA Institute Asset Manager Code of Professional Conduct; or 2) that the firm's code of ethics/conduct complies with the six principles of conduct of the CFA Institute Asset Manager Code of Professional Conduct.

Additionally, in order to become registered as an advising representative (**AR**) or associate advising representative (**AAR**) with a portfolio management firm with the various members of the Canadian Securities Administrators (**CSA**), an individual must meet stringent proficiency requirements; one of two ways to meet these proficiency standards is by having the CFA Charter and 12 months of relevant industry experience (for ARs) or having Level 1 of the CFA and 24 months of relevant industry experience (for AARs). As such, the vast majority of our members' individual registrants hold a CFA Charter.

KEY RECOMMENDATIONS

The following are PMAC's key recommendations to the CFA Institute with respect to the Consultation:

1. Calibrate the Standard very carefully to ensure that it will be voluntary and sufficiently flexible so as not to conflict with or duplicate legally mandated disclosure requirements and ESG standards that asset managers already comply with;
2. Allow asset managers that adopt the Standard to determine the manner in which they disclose this information to investors in order to leverage existing disclosure documents and available technology;
3. Recommend the independent examination as best practice but leave the ultimate decision to the professional judgement and capacity of the asset manager; and
4. Amend the proposed ESG features to focus only on those that are distinct in order to bolster the goal of the Standard increasing investor understanding of ESG-related features within investment products.

These recommendations and others are discussed in further detail in the body of the letter.

RESPONSES TO SELECTED CONSULTATION QUESTIONS

Our members have the following comments on certain of the questions set out in the Consultation. We have used the numbering found in the Consultation but for brevity, did not include any questions to which members did not respond and, as such, the numbering is non-sequential.

Question 1: Do you agree that a standard is needed to help investors better understand and compare investment products with ESG-related features?

Members agree on a high level that the industry is looking for ESG standards and we appreciate the CFA Institute's focus on ESG investing. Generally, members believe that the Standard is a starting point and approve of the CFA Institute's proposal of ESG standards, not requirements, that are voluntary in nature. As the demand and interest for ESG investing continues to grow, along with concerns about "greenwashing", a robust and widely-accepted disclosure framework is essential.

However, PMAC members have noted the existence of multiple other global ESG disclosure standards. Firms are also concerned about whether the CFA Institute should create such standards given the existence and/or development of these numerous other ESG disclosure standards and because of the CFA Institute's considerable influence over the asset management industry. The concern is that this influence may create pressure for asset managers to use the Standard, similar to the way in which the industry has

experienced pressure to adopt the Global Investment Performance Standards (**GIPS**) as a *de facto* requirement.

Members noted that there may be redundancy and potential confusion with other ESG disclosure regimes as well as with firms' existing legal disclosure requirements. Based on the Consultation, it is unclear whether the Standard would be able to successfully avoid or reconcile conflicts between the Standard and existing ESG disclosure standards and legal disclosure requirements. Unintended consequences in the form of duplicative or conflicting disclosure requirements should be avoided at all costs, as this would undermine the objectives of the Standard, drive up the cost of ESG-related funds and cause confusion for investors – all without any investor benefit.

It is also important to acknowledge that, while there is a growing trend toward ESG products and awareness, firms are at different stages of adopting and integrating ESG strategies and considerations. For this reason, the Standard may be more easily adopted by firms that are further ahead in their ESG usage while taking more resources and lead-time for firms that are still in the earlier stages of this process. The rate of adoption of the Standard may also be impacted by the jurisdiction(s) in which firms are operating. For firms already operating in the European Union (**EU**), the Standard may be more easily adopted to their products while, for firms operating in Canada, some of the principles may not be relevant. In some cases, geopolitics can influence investor norms and expectations in ways that differ from jurisdiction to jurisdiction. For example, European standards may be more prone to excluding fossil fuels, whereas this type of investment would represent a large part of the Canadian equity market.

At the same time, the Standard could create additional burden given the existence of other, more developed industry and regulatory ESG disclosure standards. For example, the Securities Industry and Financial Markets Association (**SIFMA**) is suggesting that the CFA Institute should consider a substituted compliance regime so that firms are able to meet the Standard by evidencing compliance with other acceptable rules and ESG disclosure standards, such as those listed in Table 1 of the Consultation.

Question 2: Are any of the defined terms ambiguous? If so, how could they be clarified?

Members generally find the defined terms to be appropriate.

Question 3: In addition to the examples listed in Table 1, which regulations and standards, either in existence or in development, should be considered during the development of the Standard to avoid duplication or conflict and to ensure alignment and referencing if and when applicable?

The Investment Company Institute (**ICI**)'s now-finalized ESG standards should be reflected as final in Table 1 and considered in the development of the Standard. PMAC appreciates that there are many ESG standards in existence or currently in development that may warrant consideration and/or that could potentially conflict with the Standard. However, we support the CFA Institute's attempt to create guidelines that could work on a global basis.

For example, we understand that the EU will require asset managers to use ESG integration in their fund investment process and will require disclosure in prospectuses.

We believe this would result in an unintended consequence since the CFA Institute proposes that ESG Integration would be an ESG-related feature which would mean that if an asset manager were to be required to apply the Standard to all products with ESG Integration, they would then be required to apply the Standard to all funds distributed in the EU.

Question 4: Do you agree that a disclosure-based approach would be more helpful to achieve the Standard's goals of transparency and comparability than a prescriptive-based approach?

PMAC supports principles-based approaches to the development of standards, recognizing that principles-based approaches tend to be far more adaptable to product innovation, markets and the wide variety of business models and clients served by asset management firms.

PMAC agrees that a disclosure-based approach would be preferable to a prescriptive approach. The architecture of the Standard provided in the Consultation seems to support this notion. However, in order to properly opine on whether the Standard will be able to achieve the goals of transparency and comparability, members will need to review the proposed final Standard. The text of the Standard, including examples of what the disclosure might look like for a variety of products will be very important to review.

We do, however, recognize that there is a tension between the needs of larger and smaller firms. While smaller firms might be more able to adopt the Standard if there are more concrete examples and expectations articulated by the CFA Institute, the same level of detail may hamper larger firms or may reduce the effectiveness of the Standard as products and firms evolve.

Question 5: Do you agree that the Standard should focus only on product-level disclosures and not firm-level disclosures?

PMAC agrees that the Standard should only focus on product-level disclosures. We believe that firm-level disclosures are otherwise prescribed by applicable securities regulation and are sufficient to provide relevant information to investors. As we note below, not all products offered by a firm may meet the Standard. Moreover, entity-level disclosure is not conducive to comparing whether different products meet an investor's ESG needs so we do not believe it would further the CFA Institute's objectives for the Standard.

Question 6: Do you agree that an asset manager should be permitted to choose the investment products to which they apply the Standard rather than be required to apply the Standard to all their investment products with ESG-related features?

Members voiced disparate views on the issue of permitting asset managers to choose the investment products to which they apply the Standard.

Certain members felt that the ability to choose which products with ESG-related features they will apply the Standard to or which elements of the Standard would apply would provide greater flexibility and, therefore, increased adoption of the Standard without constraining a firm to incur the resources to apply the Standard to all products with ESG-related features. These members noted that investment products can have different

objectives, investment regions, universes, constraints, and that this can make it challenging to apply one standard to all products.

Members can foresee situations in which the Standard could apply only partially to one product and, in such cases, the Standard may need to contemplate how to address such situations. For example, if an asset manager applies one governance factor in selecting a product, that product could fit into the Proxy Voting feature, triggering the need to apply the Standard across many products. These examples show how the Standard could lead to “over-labelling” or unnecessary labelling which we believe undermines the goal of identifying products that meets an investor’s ESG needs.

Asset managers that are signatories of the UN Principles for Responsible Investment (**PRI**), have committed to integrating ESG factors across their investment teams and portfolios, but would not likely elect – at least not initially – to apply such standards on a firm-wide basis.

Conversely, other firms were concerned that the ability for asset managers to selectively apply the Standards to certain products could undermine the goal of comparability for investors and exacerbate existing issues of confusion and lack of clarity around ESG products.

Additional information is needed about the exact content of the Standard – including how prescriptive it will be – and regarding whether the independent evaluation will be required or voluntary. These two matters may impact our views as to whether asset managers should be able to apply the Standard selectively.

Members considered, then rejected, the potential alternative of adopting a threshold approach to this disclosure. This is because members noted that one ESG feature could have a large impact on the product, while many other ESG features, even when taken together, could have a minimal impact. Members instead believe that the various ESG features should help investors determine the extent to which the ESG factor is considered. This does not necessarily need to be done quantitatively, but it should be done in a clear and concise manner.

Question 9: Should the Standard require that all disclosures be made in a single document? If disclosures were spread across multiple documents, would that pose a challenge for investors to understand and compare investment products?

PMAC urges the CFA Institute to allow asset managers to determine how to implement the Standard as it relates to their products, be that via a single or several disclosure documents. Because some of our members operate globally, firms need the flexibility to determine the form and delivery method of disclosures, including the option of using multiple documents. If other disclosure documents, such as prospectuses, are already available, firms should be permitted to leverage those documents.

We also ask the CFA Institute to allow asset managers to leverage technology that would increase the efficiency and reach of this disclosure while minimizing cost and environmental impacts (i.e. allowing disclosure via a firm’s website).

Question 10: Do you agree with the design principle for independent examination?

PMAC has concerns that the independent examination could create a new audit industry and increase costs for asset managers that are seeking to meet investor's ESG needs. Due to the still-developing nature of ESG disclosure standards, it may be prudent to allow some time for firms to adopt the Standard while giving the CFA Institute the opportunity to assess which metrics should be used to assess the use of the Standard.

Question 11: Should independent examination be required, or should it be recommended as best practice but ultimately left to the discretion of the asset manager?

PMAC believes that the independent examination should be recommended as best practice and left to the professional judgment (and capacity of) the asset manager. Some members suggest that, after an initial roll-out period, the CFA Institute will have better information to evaluate how the Standard is being used and can then consider whether to mandate the independent examination requirement. At that point, firms believe that they should be permitted to use their own internal audit departments to conduct such an examination.

Members also noted that investors have recourse against firms that make misrepresentations about their products, providing adequate protection against abuse of the Standard.

Question 13: Do you agree with the scope of the general disclosure requirements? Are there topics that should be added, deleted, or modified?

Members generally feel the proposed scope of the general disclosure requirements are appropriate and that they may warrant review and amendment from time to time as additional social, environmental and governance issues may arise. We should not assume that the concerns of the moment will continue to be relevant or static.

However, if the general disclosure requirements are already covered by applicable regulatory requirements – such as investment objectives, or already disclosed in the product's offering documents, what the CFA Institute is proposing could be duplicative and therefore, unnecessary. We believe that asset managers should not be subject to duplicative disclosure requirements as this is inefficient, unnecessary and not useful to investors, thereby undermining the objectives of the Standard.

Question 14: Should the disclosure requirements address an investment product's intention to align with policy goals, such as the UN Sustainable Development Goals¹⁰ (SDGs), and if so, should these requirements be part of general disclosure requirements or feature-specific disclosure requirements?

No, PMAC does not believe this should be mandatory, as all products may not align with SDGs.

Question 15: Should the disclosure requirements include an explanation of whether, and if so how, an investment product considers principal adverse impacts on sustainability factors and where to find additional information, as required by Article 7 of Regulation EU 2019/2088 Sustainable Finance Disclosure Regulation?

PMAC does not believe this should be required. This disclosure seems to be far more applicable to firms in the EU and some firms may not be equipped to disclose this.

ESG Integration (A)

Question 16: Do you believe that “ESG Integration” is a clear and appropriate name for this feature? If not, please suggest an alternative and explain why it would be a better choice.

The majority of PMAC members do not believe that ESG Integration warrants inclusion as a distinct feature in the Standard. PRI signatories^[1] commit through Principle 1 to “incorporate ESG issues into investment analysis and decision-making processes”. In light of the wide spectrum of strategies investors implement to consider material ESG factors, we do not believe the ESG Integration should be viewed as a distinct feature. ESG Integration is viewed as a capability required to become an effective asset manager, not as a specific ESG feature. Most asset managers are already using ESG Integration in their risk management and investment processes and, in the view of most members, it could be misleading to characterize products as ESG products simply because of the use by the manager of broad ESG integration techniques.

Further, these members believe the term ESG Integration does not speak to how these factors are applied in the analysis of investment products and is a broad term that could potentially be applicable to all of the features described. Since ESG Integration and the consideration of ESG-related features may occur to varying degrees with respect to investment products, the majority of members do not feel that this is a sufficiently distinctive feature. If the ESG factor(s) is material, then the adviser should consider it as part of their fiduciary obligation and therefore, does not warrant specific disclosure.

The members that do agree with the inclusion of ESG Integration in the Standard noted that disclosure about how and the extent to which a firm considers ESG Integration is important information for investors to have so they can assess the different ways an asset manager is considering these factors as part of a broader framework when considering one ESG product versus another. Since firms engage in varying levels of ESG Integration, this information can help further investors’ ability to compare investment products.

Question 17: If an investment product had Feature (A), and only Feature (A), as defined, would it be consistent with the CFA Institute policy paper “Positions on Environmental, Social, and Governance Integration”? In other words, would it be clear that material ESG-related factors are considered alongside traditional financial factors solely for the purpose of seeking to improve risk-adjusted returns? If not, please suggest how that could be made clearer.

Please see comments on Question 16 above.

^[1] We note that, according to the [PRI website](#), there are 3,300 signatories globally and 170 Canadian signatories.

ESG-Related Exclusions (B)

Question 20: Do you believe that “ESG-Related Exclusions” is a clear and appropriate name for this feature? If not, please suggest an alternative and explain why it would be a better choice.

Members believe this to be clear and appropriate.

Question 21: Are “negative screening” and “norms-based screening” similar enough, particularly in the types of issues to be addressed by disclosure requirements, that they can both be covered by Feature (B) ESG-Related Exclusions? If you prefer that they be two separate features, please explain the key differences in function, benefits, and disclosure requirements.

We believe that these are sufficiently distinct as to warrant separate features. Members note that negative screening is typically more product-oriented whereas norms-based screening is typically geared towards international standards.

Question 22: Is Feature (B) clearly defined? If not, please suggest how the definition could be made clearer or more precise.

We believe Feature (B) is clearly defined.

Best-in-Class (C)

Question 24: Do you believe that “Best-in-Class” is a clear and appropriate name for this feature? If not, is “Positive ESG Performance Profile” a better name? If you dislike both of these names, please suggest an alternative and explain why it would be a better choice.

PMAC does not believe that the use of “Best-in-Class” is appropriate for several reasons. We believe this term would cause concern amongst regulatory authorities due to the subjective and potentially misleading nature of its meaning. The use of this term is further complicated by the fact that some asset managers leverage third-party ESG ratings to formulate their list of “Best-in-Class” investments. Members are also concerned that this term lends itself to gamification and manipulation so that exploitative asset managers can lay claim to the term.

Additionally, for asset managers governed by the Financial Industry Regulatory Authority in the United States (**FINRA**), we understand that FINRA has expressed concerns with the use of the term “best-in-class”.

Furthermore, any reference to “best” or “positive” may have the unintended implication that firms that do not incorporate these strategies are somehow “worse” or “negative”, which should be avoided.

A potential alternative for consideration is the term “ESG Tilting” which is more aligned with the feature definition that “aims to invest in companies... that perform better than peers on one or more performance metrics related to ESG matters”. Members note, however that Morgan Stanley Capital International (**MSCI**) has used “ESG Strategic Tilting” in [research reports](#) which may complicate the wider adoption of the term if it is owned by MSCI. We understand that some firms have adopted other terms to describe products that invest in securities based on their overall ESG performance, including both

securities with the best ESG ratings and those whose ESG ratings have improved over time.

Question 27: Do you agree with the issues to be addressed by the disclosure requirements specific to Feature (C)? Are there issues that should be added, deleted, or modified?

It is unclear what the “Best-in-Class” feature aims to capture when comparing companies and issuers that perform better than peers on one or more performance metrics related to ESG. Without a clear (and by necessity industry and/or region-specific prescriptive) definition of what a company or issuer’s peer group is, PMAC is concerned that referring to peer group comparisons will continue the challenges articulated in the CFA Institute paper “[Fixing the Peer Group Problem](#)”.

Members also note that there are other means by which these types of features can be quantified. For example, data analytics platforms such as Refinitiv can be applied to generate a scoring-based approach to arrive at an ESG-optimized portfolio.

ESG-Related Thematic Focus (D)

Question 28: Do you believe that “ESG-Related Thematic Focus” is a clear and appropriate name for this feature? If not, please suggest an alternative and explain why it would be a better choice.

PMAC agrees that ESG-Related Thematic Focus is a clear and appropriate name.

Question 29: Do you agree Feature (D) is distinct enough, particularly in the types of issues to be addressed by disclosure requirements, that it should be separate from other features? If not, please suggest the feature with which it should be combined.

PMAC believes that this feature is distinct and appropriate. We are of the view that disclosure standards around ESG-Related Thematic Focus can assist investors in making decisions.

Impact Objective (E)

Question 32: Do you believe that “Impact Objective” is a clear and appropriate name for this feature? If not, please suggest an alternative and explain why it would be a better choice.

PMAC agrees that Impact Objective is a clear and appropriate name.

Question 33: Is Feature (E) clearly defined? If not, please explain how the definition could be made clearer or more precise.

PMAC believes that this feature is distinct and appropriate. We are of the view that disclosure standards around Impact Objectives can assist investors in making decisions.

Question 34: Do you agree with the issues to be addressed by the disclosure requirements specific to Feature (E)? Are there issues that should be added, deleted, or modified?

Proxy Voting, Engagement, and Stewardship (F)

Question 36: Do you agree that “Proxy Voting, Engagement, and Stewardship” should be a distinct feature? If not, would you prefer that the types of issues to be addressed by disclosure requirements be redistributed to other features or to general disclosures?

PMAC does not agree that Proxy Voting, Engagement and Stewardship should be a distinct feature and believes that this does – and should continue to form - part of general disclosures. Please also see our comments above from certain members on ESG Integration. We note that the European Union does not permit this type of “call out” as a way to promote ESG funds.

Question 40: Does this list of ESG-related needs represent the spectrum of investors’ ESG-related needs?

PMAC believes the list of ESG-related needs generally represents the current spectrum of investors’ ESG-related needs, but cautions that these needs shift in response to political, social and other events and should be monitored for relevance.

Question 41: Are these five ESG-related needs clearly differentiated and mutually exclusive?

PMAC believes the five needs are not mutually exclusive and view them instead as existing on a spectrum where there may be a considerable amount of overlap. While these ESG-related needs are framed in the Consultation as separate objectives, certain investors may require all these needs simultaneously. For example, an investor may want to invest across certain thematic areas, but may then also want to exclude tobacco because they have a personal aversion to the use of tobacco.

Additionally, members note that the needs expressed under 2 and 3 of Table 2: “Typical ESG-Related Needs” are vague and inter-related. For instance, the investor’s personal beliefs (need 2) would be supported by having fewer negative effects or more positive effects (need 3). Doing “good” and doing “well” are not necessarily conflicting or mutually exclusive objectives. While the table linking ESG-related needs with ESG-related features could be useful in certain circumstances, we do not believe that all investors will view their needs in such a discrete or siloed fashion.

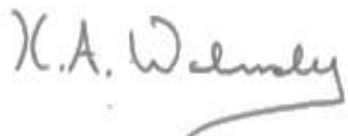
CONCLUSION

We would like to thank the CFA Institute for the opportunity to respond to this Consultation.

If you have any questions regarding the comments set out above, please do not hesitate to contact Katie Walmsley at (416) 504-7018.

Yours truly,

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