MACKENZIE Investments | CONFIDENCE IN A CHANGING WORLD

E-MAIL:
comments@osc.gov.on.ca; consultation-en-cours@lautorite.qc.ca

October 19, 2018

British Columbia Securities Commission
Alberta Securities Commission
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marches financiers
Financial and Consumer Services Commission of New Brunswick
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
Registrar of Securities, Northwest Territories
Registrar of Securities, Yukon Territory
Superintendent of Securities, Nunavut

The Secretary
Ontario Securities Commission
20 Queen Street West
22nd Floor, Box 55
Toronto, Ontario
M5H 3S8

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

Re: Canadian Securities Administrators ("CSA") Notice and Request for Comment dated June 21, 2018 – Reforms to Enhance the Client-Registrant Relationship ("Client Focused Reforms")

We are pleased to provide comments on behalf of Mackenzie Financial Corporation ("Mackenzie Investments") on the Client Focused Reforms.

Founded in 1967, Mackenzie Investments provides investment management and related services through diversified investment solutions using proprietary investment research and experienced investment professionals, to deliver our holistic product offerings. We partner with thousands of Canadian financial advisors and the investors they work with by bringing them innovative investment solutions through mutual funds, exchange-traded funds ("ETFs"), alternative investments, private wealth pools and managed solutions. We strive to bring insights, data and tools to advisors to help them support their clients.

Our company is registered as a portfolio manager and investment fund manager with total assets under management as at September 30, 2018 of approximately $141 billion, including investment fund assets under management of approximately $62 billion. Mackenzie Investments primarily distributes its retail investment products through third-party financial advisors. Our sales teams work with approximately 175 firms across Canada and many of the more than 30,000 independent financial advisors to distribute our products to over 1 million Canadian clients.

Mackenzie Investments is a wholly owned subsidiary of IGM Financial Inc., which in turn is a member of the Power Financial Corporation group of companies.

General Comments

At Mackenzie Investments, we are committed to the financial success of investors, through their eyes. We strongly believe in the value of advice provided to our investors by the financial advisors with whom they work with.

Overall, we support the CSA's efforts to better align the interests of advisers, dealers and representatives ("registrants") with the interests of their clients, to improve outcomes for investors, and to make clearer to investors the nature and the terms of their relationship with registrants. We were very encouraged to see that the CSA has incorporated into the Client Focused Reforms many of the comments received on the earlier CSA Consultation Paper 33-404. As an independent fund manager, we believe in the importance of retaining an innovative, competitive financial services industry in Canada, which provides investors and the advisors with whom they work with, access to a broad range of solutions and product manufacturers. Accordingly, we are supportive of the guidance in the Client Focused Reforms to firms that offer both proprietary and non-proprietary products, to make non-proprietary products as easy to access for its registered individuals and its clients as its proprietary products.

Mackenzie Investments is committed to bringing innovative and distinctive products, strategies and solutions to Canadian investors. We offer a number of differentiated products for the specific investment needs and objectives of individual investors (both actively and passively managed), as well as non-traditional strategies, which we believe are unique to the market and can help investors achieve good outcomes. For example, we offer investors products that allow them to have a positive environmental and social impact, such as the Mackenzie Global Leadership Impact Fund and Mackenzie Global Leadership Impact ETF. These products provide an opportunity for investors to affect social and governance change through a focus on promoting the benefits of women in leadership. We also recently launched the Mackenzie Multi-Strategy Absolute Return Fund, the first absolute return fund available to retail investors based on the CSA's alternative mutual funds framework. This fund offers investors a non-traditional solution to increase portfolio stability by using alternative strategies to diversify a component of their portfolio that is not correlated with the markets.

As the CSA examines the feedback received in this consultation and moves forward with the Client Focused Reforms, it is important that the CSA ensures that the reforms will not result in any unintended results that could impede innovation and good investor outcomes. We believe good investor outcomes, and vibrant capital markets, depend on ongoing product innovation, the introduction of unique products, and investor access to a diverse range of products, both actively and passively managed. As drafted, we are quite concerned that the Client Focused Reforms' emphasis on the "cost" of the security, seemingly above all other factors, when determining KYP and suitability, may discourage registrants from choosing actively managed, alternative and non-traditional products in both product shelf development and client recommendations, to the detriment of investors and the capital markets. We discuss this in further detail below.

With the foregoing in mind, we wish to provide the following feedback on certain aspects of the reforms. Much of our feedback is based on the discussions and insights we have gained through our engagement with the financial advisors with whom we partner.

Comments on Specific Aspects of the Client Focused Reforms

Know your product

i. Comparison of "similar securities"

With respect to the requirement for a firm to understand how a security compares to similar securities available in the market (as well as the related requirement for registered individuals to compare securities available at the firm), registrants seek additional clarity on what constitutes a "similar security".

In our view, registrants should be comparing securities that have similar fundamental attributes, which for investment funds would include similar investment objectives and strategies, portfolio mix, geographic allocation, liquidity, leverage, expected return characteristics, risk profile, and structure. We do not believe comparisons between active and passive investment funds are appropriate under KYP, as there can be very different return characteristics (e.g. potential for growth above and beyond market returns) and risks (e.g. how they may perform during market downturns or in crises events) even when the investment objectives and strategies of the funds are alike.

Similarly, ETFs (whether passive or active) should not be compared against similar conventional mutual funds, as there are differences in the implementation of the objectives and strategies of these funds, particularly when actively managed, because of their differing structures, which impacts their portfolio construction and risk profile. For instance, active ETF portfolios generally are designed to hold a greater proportion of their assets in more liquid securities than a comparable conventional mutual fund to manage the costs associated with the creation and redemption of units, which directly affect the bid-ask spread (and costs to investors).[1] The conventional mutual fund counterpart can therefore have greater flexibility in the execution of its investment strategies, and as a result, have added opportunity to take less liquid positions to seek further growth potential.[2]

[1] We note that this result is true regardless of whether an ETF invests primarily in equites or fixed income products.

[2] For example, while there are similarities between the investment objectives and strategies of the Mackenzie Strategic Bond Fund and the Mackenzie Core Plus Canadian Fixed Income ETF, the mutual fund has greater exposure to high yield and leveraged loans as well as greater exposure to foreign fixed income securities. The differences can also be

We also do not believe that conventional funds such as alternative funds should be evaluated against funds distributed in the exempt market, even when the funds have similar investment objectives and strategies, because the funds typically have very different redemption rights, leading to large differences in liquidity.

It is also important that the KYP requirement to compare "similar securities" available in the market does not prevent registrants from considering non-traditional or innovative investment funds, simply because these types of funds often can have varying costs and fewer "similar" products in the market, if any. Without further guidance clarifying how products may be evaluated when there are fewer or no similar securities in the market, we are concerned registrants will be discouraged from offering such products. This, in turn, will lessen the growth of non-traditional and innovative investment funds and the tools that investors may have to meet their specific investment needs and objectives.

Ultimately, the comparison of "similar securities" when it relates to investment funds should, in our view, be predicated on the suitability of the proposed investment strategy for the client, in light of the client's specific investment needs and objectives and risk profile, and having regard to the client's overall portfolio concentration. Different types of investment funds (both active and passive) provide different exposure to industries and asset classes through varying investment strategies. A comparison of "similar securities" where the impact of cost is emphasized must be a comparison of "apples" to "apples". Additional guidance in this regard would be welcome by registrants.

ii. "General" vs. "thorough" understanding

We are supportive of the changes the CSA has made with respect to KYP from the earlier CSA Consultation Paper 33-404 regarding the move away from registered individuals having to demonstrate "sufficient" knowledge of each product their firm trades or advises on. Mackenzie Investments had expressed the concern on behalf of registrants that such a requirement would likely significantly reduce the product lists of firms, as a way to facilitate both advisor and firm compliance, to the detriment of investor outcomes.

To assist firms with ensuring that their registered individuals have the necessary information about each approved security and ongoing training as required under the Client Focused Reforms, registrants seek greater clarity on the CSA's expectations as to what is expected in terms of the standard for registered individuals to understand "at a general level" the securities available through the firm, versus to "thoroughly understand" each specific security the registered individual will purchase, sell or recommend to a client, which is the subject of significant guidance. While the terminology is clear, the guidance is not. It specifies that a "general level" of knowledge means "a high level of understanding" of the structure, features, returns, risks and cost of each security that a firm makes available, before the registered individual is able to select a smaller universe to focus on. In our view, this will likely be impracticable, given the breadth of investment funds made available and approved today on a firm's product shelf, which can be hundreds, if not thousands, of fund codes in addition to securities and deposit products.

We urge the CSA to consider changes to the guidance with respect to what is meant by a "general understanding" as we believe the resulting outcome of the current proposal will be similar to what we had previously identified. Namely, a significant reduction in approved investment funds and

---

demonstrated by examining the minimum weighted average credit weighting of the ETF, which is A- relative to BBB for the fund.

securities on a firm's product shelf, resulting in investors and advisors having less access to a broad range of products and fund manufacturers to choose from.

As a manufacturer of innovative and distinctive products, including non-traditional and alternative strategies which we believe are integral to sophisticated portfolio construction and good client outcomes, we also urge the CSA to reconsider the role asset managers can have in providing information for a firm's due diligence process, and in the continuing education of registered individuals as part of KYP. As a fiduciary, we believe it is our responsibility to educate and provide information to registrants and investors on the products we offer, and we believe that we are best positioned to do so. For example, with the recent launch of the Mackenzie Multi-Strategy Absolute Return Fund, we provided firms and registered individuals with a general education guide, investment strategies brochure, and videos, to comprehensively explain each of the strategies employed by the fund, and importantly, the associated risks. This included, for example, detailed explanations of the use of uncovered derivatives, cash borrowing, and the fund's greater flexibility to short sell than a conventional mutual fund. Accordingly, as we discuss further below, we recommend as part of the Client Focused Reforms that it be permissible, depending on the information provided by the issuer, for the firm to approve a security based on the information provided from the issuer.

iii. Due diligence and security approval process

Another aspect of the Client Focused Reforms that registrants seek further guidance and clarity on, is the expectations of the CSA with respect to the firm's due diligence and security approval process. Currently, there is some inconsistency in the guidance. The CSA notes that the extent of the KYP process required for a security will depend on the structure and features of the security, with the recognition that more complex investment products may require a more expansive review than more straightforward securities. However, the guidance also explicitly states that a firm cannot approve a security based solely on the representations, information, documentation, analyses or reports received from issuers or other third parties, or rely on its similarities to other securities. This guidance seems to undermine the ability of the firm to vary the degree of it's due diligence and approval process.

For conventional securities that are offered pursuant to a prospectus, such as listed equities, corporate and government issued bonds, and retail investment funds, it is unclear what criteria the CSA expect a firm to base its approval on beyond the information provided in the prospectus and accompanying disclosure documents as well as third-party analysis. We also question why firms should not be able to rely on the information provided by issuers since it is provided pursuant to the CSA's public offering and continuous disclosure regime, which is information that the CSA has deemed sufficient for an end investor to make an informed decision.

We encourage the CSA to permit firms to have the flexibility and discretion to determine its due diligence and approval process, based on the type of security. In our view, these processes should be tailored based on the attributes of the security, consistent with the guidance the CSA provides for tailoring the KYC process. For conventional securities that are offered pursuant to a prospectus, this would allow firms to rely on factual information and disclosure documents provided by issuers, as well as analysis of securities completed by independent third-parties. If firms are not afforded this flexibility, we are concerned that the compliance burden imposed by the current guidance may cause firms to limit the products they offer to investors, ultimately reducing investor choice and the tools they may have to meet their investment needs and objectives.

Suitability

We strongly support the CSA's emphasis on portfolio concentration as an important factor in determining suitability. At Mackenzie Investments, we believe in the importance of sophisticated portfolio construction that consists of a range of asset classes, geographic regions and investment styles for a well-diversified portfolio. Accordingly, we offer a range of investment solutions that include active, strategic beta and passive strategies through mutual funds, ETFs, alternative investments, private wealth pools and managed solutions.

Our concern with the Client Focused Reforms is on the emphasis of "costs and their impact" as a predominant factor in both the suitability and KYP requirements, which we believe may create a bias against active and strategic beta, as well as alternative and non-traditional products. These products inherently have a higher management fee than traditional products such as passively managed index funds, but nevertheless play an important role in a client's portfolio. We caution the CSA that an unintended consequence of the weight given in the guidance to a consideration of "costs and their impact" above all other factors could lead some registrants to favour the "lowest cost security", which generally will be an index managed product, not because it is most suitable for the client, but because it eases the compliance burden of the registrant to document the "reasonable basis" of the suitability determination, particularly in light of the perceived predisposition of the CSA against actively managed products.

This regulatory partiality in the Client Focused Reforms towards the "lowest cost" security also seems at odds with the CSA's focus on portfolio level suitability and guidance on the importance of a broadly-based portfolio of issuers and a consideration of overall concentration. While costs and their impact are certainly important factors in determining suitability, it is not the only factor that leads to recommendations that put the client first. Suitability must be based on the client's specific investment needs and objectives, time horizon and risk profile, having regard to the client's overall portfolio concentration and liquidity across all of the client's accounts. Other factors that can, in certain circumstances, have equal or greater prominence to the security's cost include the product's expected return, risk profile, geographic and market exposure, overall complexity, liquidity, history and track record of the issuer, and the intended investment strategy.

If registrants focus on costs at the exclusion of other important factors, investors may lose access to crucial investment tools that can assist them in furthering their investment needs and objectives. For example, alternative strategies can provide investors with access to shorting and leverage to capture different market opportunities across a wide range of asset classes, and in doing so, provide better diversification, improve downside protection, reduce correlations to traditional benchmarks, and smooth out performance over a full market cycle.

This focus on the cost of each security is also contrary to the guidance on account type suitability, where the fees or commissions associated with the account type may influence the suitability determination of a particular security. For example, an embedded series of a mutual fund may be a higher cost security than its unbundled series counterpart, however, when client costs and their impact are considered at the account or portfolio level, the overall cost to the client is less with the higher cost security because of account type.

We strongly urge the CSA to reconsider the guidance to both suitability and KYP, to convey a more balanced perspective on the importance of considering many factors as part of a client recommendation of a security, with the cost of the security and its impact being but one. In our view, a focus on investment costs must never be at the expense of ensuring investors are provided with products that are best suited to their individual investment needs and objectives.

Consistent with the objectives of the Client Focused Reforms, the focus must always be on providing investors with products that are centered on improving investor outcomes.

Embedded Commissions and Third-Party Compensation

The CSA's proposed amendments to National Instrument 81-105 published September 13, 2018 ("CSA Embedded Commission Proposals") specifies that the CSA is proposing to continue to allow the payment of embedded commissions, subject to the enhanced conflicts of interest mitigation measures in the Client Focused Reforms, as well as the additional explicit considerations in the suitability and KYP obligations, which as discussed above, focus on the consideration of the costs of each security and the impact of costs on client returns.

Registrants seek greater specificity on the CSA's expectation of what factors, notwithstanding the CSA's proposal to continue to allow the payment of embedded commissions, must be met to demonstrate the registrant has a reasonable basis to recommend the embedded commission series of a mutual fund. This is especially crucial given that the security will generally always be at a higher cost than its unbundled series counterpart when examined without consideration of the total costs to the client at the account or portfolio level. As currently drafted, we are concerned that registrants do not have the necessary clarity of how to demonstrate that they are resolving the conflict of interest in their client's best interest, as well as meeting their suitability and KYP obligations with respect to both product shelf development and client recommendations.

This issue is heightened for registrants that provide products and services to clients exclusively through commission based accounts. The proposed controls appear to force firms to consider how embedded commission based products compare against alternatives that do not pay embedded commission – without any consideration given to the total costs for a client at the account or portfolio level. For example, the guidance suggests that firms should include securities that provide "lower levels or no third-party compensation" in the product evaluation process, and further that that firms should undertake due-diligence to ensure that the products they offer are competitive with comparable alternatives available in the market, "including those that do not provide third-party compensation". In our view, this guidance cannot be reconciled with firms that provide products and services to clients exclusively through embedded commission based accounts. Again, it is not clear what the CSA's expectation is with respect to such firms having to demonstrate that product shelf development and client recommendations are without influence from any third-party compensation. The guidance is not very helpful with this business model.

If the CSA has concluded to not discontinue embedded commissions, then we believe the CSA must not indirectly, through the Client Focused Reforms, make its use unnecessarily difficult or unattainable for registrants to meet the conflict of interest mitigation requirements as well as their suitability determination and KYP obligations. The CSA indicate in the CSA Embedded Commission Proposals that the proposed policy changes are intended to minimize potential adverse consequences to market participants and investors. Therefore, it is important in our view, that the CSA provide greater transparency as to what factors or circumstances it will accept the embedded commission series of a mutual fund to be suitable over its unbundled counterpart. Without this clarity, registrants may stop offering embedded commission accounts even if this choice puts the client first, and will deprive investors of a crucial payment option that assists Canadian investors in attaining advice.

Referral Arrangements

We appreciate that the CSA continues to recognize that referral arrangements are an established and legitimate business practice that can assist investors in obtaining access to securities related advice and other services. We do, however, believe aspects of the proposals with respect to such arrangements are overly broad and may have the unintended outcome of limiting arrangements where there is no clear policy rational to do so.

For example, we question why the CSA has effectively capped the duration and amount of a referral fee without any exception or contemplation for the substance of the arrangement. Provided registrants can demonstrate ongoing services are provided to clients in exchange for a referral fee, supervision is performed, all fees are clearly disclosed to clients, and clients explicitly consent to the referral, we do not see why any limits on the duration or amount of a referral fee are necessary. We also question why the CSA has introduced such a wide-ranging restriction to not allow registrants to engage in referral arrangements with all non-registrants. For example, why would professionals who are not securities registrants, but nevertheless possess other types of registrations and/or designations (such as accountants, lawyers, financial planners, mortgage specialists, etc.) be prohibited from receiving referral fees, even on a one-time basis.

To ensure that the proposals on referral arrangements as well as the underlying policy rational is well understood by all market participants, and to limit any negative, unintended consequences, we would encourage the CSA to articulate its policy concerns as well as engage in further discussion and engagement with stakeholders beyond this first comment period.

Transition

We encourage the CSA to reconsider the proposed transition periods for all aspects of the proposals. As acknowledged in the Regulatory Impact Analysis accompanying the Client Focused Reforms, the proposals will impose significant one-time transition costs as registrants evaluate, adapt and implement new compliance processes and controls for their particular business model. Such changes will also require engagement with industry service providers to ensure system modifications can facilitate the changes, and will require extensive staff training. In our view, a transition period of 3 years will better position registrants to minimize client disruption and to smoothly and effectively transition to the Client Focused Reforms.

Conclusion

We thank you for the opportunity to provide comments on the Client Focused Reforms. We would be pleased to engage with you further on this topic. Please feel free to contact Rhonda Goldberg, Senior Vice-President, General Counsel at Rhonda.goldberg@igmfinancial.com or myself, if you wish to discuss our feedback further or require additional information.

Yours Truly,

MACKENZIE FINANCIAL CORPORATION

Barry S. McInerney
President and Chief Executive Officer