BY EMAIL: comments@osc.gov.on.ca; consultation-en-cours@lautorite.qc.ca

April 12, 2013

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

Attention: The Secretary
Ontario Securities Commission
20 Queen Street West
19th Floor, Box 55
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 (Québec) H4Z 1G3

Dear Sirs/Mesdames:

RE: CSA Discussion Paper 81-407 – *Mutual Fund Fees*

AGF Investments Inc. ("**AGF**") is writing to provide comments in respect of the Canadian Securities Administrators' ("**CSA**") Discussion Paper 81-407: *Mutual Fund Fees*, as published on December 13, 2012 (the "**Discussion Paper**").

AGF appreciates the opportunity to provide feedback to the CSA on the topics for consideration raised in the Discussion Paper to assist it in determining whether further regulatory responses are desirable in Canada with respect to improving investors' awareness and understanding of the costs associated with mutual funds.

AGF certainly values the CSA's declaration that investor protection and fairness is a paramount concern for the regulators. That said, AGF's general position is that the current landscape with respect to the costs of mutual funds does not counteract the tenets of investor protection and fairness. In particular, at the outset, AGF wishes to draw attention to the following key points that should be considered by the CSA in assessing the topic of evaluating mutual fund fees:

- **Advantage of Advice**. One of the key components in the cost of mutual funds is the payment for advice. The fact that many investors employ the use of financial advisors in their decision to invest should not be diminished or discounted. Not all investors are "do-it-yourself" types. Many investors rely upon their financial advisors to provide them with the tools and information necessary to make informed investment decisions. And, as a result, the necessary costs for the provision of such investment advice are built into the costs of owning mutual funds. This should not be seen as "wrong" or "unfair" to investors – particularly when there is emphasis and importance placed by investors on this advice.

- **Trailing Commissions Pay For More Than Just Advice**. The payment of trailing commissions should not be misinterpreted as compensating only for advice. Trailing commissions are paid to the dealer firm to cover the many operational costs associated with the provision of "dealer" services; operational, compliance-related or otherwise. Advisor compensation is just one component of those costs. Regulatory and supervisory obligations must also be covered by the dealer, and trailing commissions are partially meant to assist in covering those costs.

- **Unfair Targeting of Mutual Funds**. While AGF appreciates that the CSA may not have jurisdiction with respect to other "non-securities" financial products, we do not believe that mutual funds should be unfairly targeted for having costs of distribution embedded in the overall cost of ownership. Compensation for distribution is typically embedded in the margins and spreads of other investment products – i.e. not just mutual funds. Investors should not be seen as being unfairly disadvantaged for having embedded distribution costs built into the costs of owning mutual funds. This is simply just the way that most financial products are structured. To require mutual funds to move away from this widely accepted broader "financial industry" practice would be to create an unlevel playing field between financial products. While AGF does not presume that the CSA should be precluded from making rules within its own "securities" jurisdiction simply because it does not have scope to regulate other "non-securities" financial products, AGF does not believe that the CSA should unduly target the mutual fund industry in the absence of broader intended changes throughout the entire financial products sector.

- **Cost-Benefit Analysis Required.** AGF strongly encourages the CSA to consider the cost implications of the proposals outlined in the Discussion Paper as compared to the net benefits that the CSA expects to achieve for investors. As indicated above, AGF does not feel that investors are currently prejudiced by the

existing mutual fund costs regime; however, if there is impetus on the part of the CSA to explore the principles of investor protection and fairness further in relation to the proposals raised, AGF believes that a quantitative cost benefit analysis is required. AGF does not feel that simply employing a qualitative analysis will be sufficient in these circumstances – particularly where smaller, more vulnerable investors may be the most adversely impacted (as has been experienced in the United Kingdom's adoption of its Retail Distribution Review).

- **Time Needed For Existing Transparency Rules**. AGF believes in the need for transparency of information to investors. That said, in light of the recent publication of the final set of NI 31-103 amendments relating to cost disclosure, performance reporting and client statements, AGF strongly urges the CSA to let those rules take effect, and for the impact of such rules to become known over time, before imposing further rules geared toward the costs of mutual fund ownership. If the CSA's ultimate goal in assessing the costs of mutual fund ownership is protection for investors, then AGF submits that better transparency for investors through the new NI 31-103 amendments is a big step toward ensuring that protection. Further, the impact of such added transparency definitely needs to be assessed over time before assuming that investors require more rules geared toward their protection. For these reasons, AGF does not believe that mandated structural changes with respect to embedded compensation are warranted or required at this point in time.

In addition to the general comments raised above, AGF specifically wishes to comment upon the seven proposals outlined in the Discussion Paper, as follows.

Comments on Potential Regulatory Changes as set out in the Discussion Paper

1. ***Advisor services to be specified and provided in exchange for trailing commissions***

AGF supports the concept of greater transparency for investors associated with trailing commissions. And, as indicated in our general comments above, AGF believes that such added levels of transparency will be achieved through the CSA's implementation of the new NI 31-103 rules regarding cost disclosure, performance reporting and client statements.

AGF does not support, however, proposals that would see trailing commissions only paid to dealers when certain minimum service thresholds are met. There are inherent challenges associated with setting minimum service thresholds, particularly across fund managers, dealer firms and their advisors, and AGF does not believe that the administrative burden of attempting to monitor and enforce any type of compliance program associated with this proposal could be properly achieved or sustained. Further, the cost burden of employing such a service level standard would undoubtedly increase distribution costs – thereby negatively impacting investors.

We also reiterate the need to recognize that trailing commissions are not just about compensation for advice. As previously indicated in our general comments above,

trailing commissions are paid to the dealer firm to cover many operational costs associated with the broader spectrum of dealer services – advice is just one component.

2. ***A standard class for DIY investors with no or reduced trailing commission***

AGF is not a proponent of mandating the creation of a separate series for each mutual fund for the discount channel, as it would prove to be a costly requirement for investment fund managers. This proposal would result in additional legal, audit, custodial, operational and administrative expenses that would impact investors. New series, just like new mutual funds, require launch and ongoing operating costs that need to be rationalized against projected asset levels. This ensures that costs can be managed adequately at reasonable levels. Therefore, a series with very low assets is simply not economically efficient for both a fund manager or for the investor, barring some form of subsidy. Consequently, AGF submits that the adoption of a discount "do-it-yourself" series specifically for each mutual fund, or the imposition of a direct to investor distribution model on a mutual fund manufacturer, should remain an optional choice for mutual fund manufacturers, and should not be imposed by the regulator.

3. ***Trailing commission component of management fees to be unbundled and charged/disclosed as a separate asset-based fee***

As indicated in our response to proposal #1 above, AGF supports greater transparency with respect to trailing commissions. That said, AGF does not believe that the unbundling of trailing commissions from management fees should be mandated by the regulator in an effort to try and provide further transparency for investors. As indicated in our general comments above, AGF firmly believes that the transparency associated with the new NI 31-103 rules should be examined by the CSA in due course before presuming that further transparency with respect to the costs of mutual fund ownership is a necessary step with regard to investor protection.

Also, as referenced in our general comments above, AGF does not believe that investors are unfairly disadvantaged for having embedded distribution costs built into the costs of owning mutual funds. This is simply just the way that most financial products are structured. To require mutual funds to move away from this widely accepted broader "financial industry" practice would be to create an unlevel playing field between financial products. This would not seem to be a justified response in light of the broader repercussions for mutual funds as compared to other financial products.

AGF submits that the payment of trailing commissions is a highly efficient mechanism for the facilitation of payment to the dealer and the advisor. Further, unbundling trailing commissions from management fees and charging them separately may create adverse tax effects for investors – thereby negatively impacting investors. This consequence requires further study and exploration by the CSA.

4. ***A separate series or class of funds for each purchase option***

With respect to this proposal, AGF submits that the legal, operational and administrative costs associated with maintaining a separate series for each purchase option would far outweigh any negligible benefits (see also comments above under proposal #2). These

costs would result in an increased level of expense to investors – a seemingly unintended consequence that doesn't appear to be commensurate with the minimal advantages of seeking to rule out "cross subsidization" entirely.

AGF further submits that a reasonable amount of unequal cost sharing is simply a part of a commingled vehicle structure. The trade-off to this is that investors get all of the added advantages associated with a commingled vehicle – including professional money management, diversification and accessibility.

5. ***Cap commissions***

AGF does not support this regulatory proposal, as it would unduly represent the regulator's intervention in a competitive marketplace. This kind of intervention does not seem to be a warranted or necessary step in seeking to advocate for investor protection. As indicated in our general comments above, AGF proposes that the implementation of the new NI 31-103 rules regarding commission transparency negates any type of need (i.e. with a view toward investor protection) for the regulator to consider capping commissions outright.

6. ***Implement additional standards or duties for advisors***

AGF submitted a letter to the CSA, dated February 22, 2013, in which we outlined our position in respect of Consultation Paper 33-403: *The Standard of Conduct for Advisers and Dealers: Exploring the Appropriateness of Introducing a Statutory Best Interest Duty When Advice is Provided to Retail Clients*. We continue to stand behind those submissions.

7. ***Discontinue the practice of advisor compensation being set by mutual fund manufacturers***

AGF submits that mutual fund manufacturers do not in fact set advisor compensation at all. Mutual fund manufacturers have established the total commission payments (which include advisor compensation) for their funds in direct response to dealers' pricing policies; such policies having evolved through the dealers over time.

Trailing commissions are paid by mutual fund manufacturers (including AGF) to the dealer firm. The trailing commissions are then used by the dealer to pay for a number of dealer functions, including (but not limited to) the compensation of advisors. As a result, there really is not a conflict of interest that needs to be addressed by the regulator with regard to this topic as it relates to mutual fund manufacturers.

AGF reiterates that the new NI 31-103 rules with respect to commission disclosure will help to address certain perceived issues the regulator may currently have with the transparency of trailing commissions. It would seem that the regulator is most concerned with making investors "more informed" about trailing commissions to ensure that they are "better protected". If that assumption is correct, then these new rules will certainly facilitate the transparency of "better" information for investors. As such, AGF believes that there does not seem to be a reason for the regulator to interfere with the widely

accepted market practice of embedding advisor compensation in the trailing commissions that are paid to dealer firms.

In support of some of the proposals outlined in the Discussion Paper, the CSA has referenced certain international jurisdictions which have adopted or proposed certain regulatory reforms with respect to embedded compensation structures. AGF urges the CSA to consider some of the early evidence that these reforms have not been as highly beneficial to investors as may have been intended. For instance, the United Kingdom's Retail Distribution Review has shown early evidence of concern that small investors are losing access to advisory services as a result of their inability and/or unwillingness to pay for advice, and that pricing structures are becoming more complex, less comparable and less transparent.

AGF proposes that the CSA should allow more time to consider and study the effects of the reforms in other jurisdictions (including the United Kingdom) before making any determinations as to the value of similar reforms within the Canadian context. AGF believes that a reformed system that would see the discontinuance of embedded commissions could prove prejudicial to small investors (as indicated by the United Kingdom experience). AGF submits that not only would such an outcome be an inadvertent consequence of reform, but also that fewer investors with access to advice is not commensurate with the primary tenets of investor protection and the fostering of efficient capital markets.

We thank you for the opportunity to raise the above issues with you. We look forward to continued constructive dialogue with respect to the CSA's proposals on this topic. AGF certainly promotes the necessary balance of investor protection while not unduly prejudicing the industry.

Yours very truly,

Mark Adams
Senior Vice President, General Counsel & Corporate Secretary
AGF Investments Inc.

cc. Gordon Forrester, Executive Vice President, Marketing and Product and Head of Retail