L'INDÉPENDANCE AU CŒUR D'UN RÉSEAU SOLIDE | INDEPENDENCE AT THE CORE OF A SOLID NETWORK

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April 12, 2013

British Columbia Securities Commission
Alberta Securities Commission
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
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
Superintendent of Securities, Nunavut

Attention:
John Stevenson
Secretary
Ontario Securities Commission
20 Queen Street West, Suite 1900, 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

Re: CSA Discussion Paper 81-407: Mutual Fund Fees

We are writing to provide you with comments on behalf of PEAK Financial Group Inc., with respect to the Canadians Securities Administrators' ("CSA") *Discussion Paper 81-407 – Mutual Fund Fees* (the "Discussion Paper"), published on December 13, 2012. We appreciate the opportunity to participate in this discussion.

About PEAK Financial Group Inc ("PEAK")

Headquartered in Montréal, Québec, present from coast to coast in Canada, and with over $6 billion in assets under administration, PEAK is positioned as a leader among multidisciplinary and fully independent financial services companies, operating as a mutual fund dealer (PEAK Investment Services Inc.), as well as a securities dealer (PEAK Securities Inc.) and a life insurance services dealer (PEAK Insurance Services Inc.). PEAK is also a member of the MFDA and of IIROC.

The mutual fund arm of PEAK, PEAK Investment Services Inc., caters to clients through its network of financial advisors in the areas of mutual funds and financial planning. PEAK further offers its advisors and clients the unique combination of full access to financial products, and specifically Canadian mutual fund products, as well as industry-leading technology and powerful services, all delivered in an environment free from any conflict of interest, sales quotas and in-house products.

General Comments

While we appreciate the fact that the CSA has chosen to initiate this policy discussion in the form of a Discussion Paper, we do have some legitimate concerns in regard to the arguments presented in the Discussion Paper, and how they may be used going forward.

Based on the facts that funds and fund distribution in Canada are already highly regulated, that there are further regulations being implemented which may mitigate most if not all of the CSA's concerns, and that the examples provided of regulation in foreign jurisdictions are in very early stages of implementation, PEAK's view is that these developments be monitored carefully and that further research and analysis be undertaken by the CSA before proceeding with any regulatory changes related to the Discussion Paper.

In addition, the Discussion Paper makes no reference to other products that have trailing commissions, such as segregated funds. Any action on mutual fund fees without simultaneous action on segregated funds would likely lead to a form of arbitrage, where clients and/or advisors will defer to the product options (namely segregated funds) that have the least administrative and regulatory costs and burdens, all else being equal.

The Discussion Paper leads the discussion on this question with a few misconceptions about trailing commissions. The first is the underlying theme that trailing commissions are used exclusively for the compensation of advisors.

The reality is that trailing commissions paid to the dealer pay for --- in addition to the advisor's compensation --- a whole host of regulatory and supervisory functions and services of a dealer, many of which directly benefit investors and other stakeholders. The dealer may retain as much as one half or more of the trailing commission to pay for, for example: regulatory costs including fees to fund the SROs, OBSI, and securities commissions, client complaint handling processes, tier 1 and tier 2 supervision and the systems that support it, advisor investigation and enforcement requirements, general compliance obligations of the SROs, securities commissions and other regulatory bodies, client reporting, and due

diligence on industry products. This component of the trailing commission which supports the regulatory obligations of a dealer is well aligned with investor interests and absent any proof to the contrary, has been functioning well for all mutual fund industry stakeholders.

The portion of the trailing commission that goes to the advisor also benefits clients through the provision of advisory services. These services include but are not limited to: suitability reviews, reviews on transfers, reviews of material changes in client circumstances, responses to client questions, general financial advice that can be unrelated to mutual funds (such as financial planning), the rebalancing of portfolios, advice on investment strategies and specific registered products and the setting up of savings programs.

In addition, PEAK does not agree with the position that a conflict of interest exists wherein because balanced or equity mutual funds have higher MERs than fixed income or money market funds, advisors are therefore more likely to recommend balanced or equity funds to their clients in order to generate greater advisor trailing commissions.

There is no existing empirical evidence that PEAK knows of to support this position, and further, in order to arrive at this conclusion, one would have to:
(a) overlook the know your client obligations that advisors must abide by and which the vast majority of advisors do abide by, and
(b) Assume that mutual fund companies are *de facto* in a position of conflict of interest relative to investors.

At the end of the day, everything leads back to the investor's communicated risk profile. If he/she is a self-acknowledged low-risk investor, then an advisor has a regulatory duty to recommend a low-risk product, such as a money market or fixed income fund, with resulting lower trailing commissions for the advisor. Conversely, if the investor has a medium- to-high risk profile, then balanced/equity funds are more likely to be recommended, with resulting higher trailing commissions. There is no conflict of interest here; simply a logical process that must be followed by advisors in order to satisfy the investor's requests and risk profile.

Furthermore, trailing commissions related to balanced / equity funds are higher because (a) there are significantly more of such products to choose from and that an advisor needs to analyze and understand than for fixed income/money market funds, and (b) the dealer's research, suitability assessment and supervision tasks and related costs associated with balanced / equity funds are significantly greater, due to the complexity and higher risk element to be considered in such products. This is consistent with all other similar investment product/management situations.

Lastly, in relation to potential conflicts of interest, we draw the CSA's attention to and encourage the CSA to consider the findings of regulators' dealer audit reviews (such as those undertaken by the MFDA). Specifically, such regulators tend to insist during their audits that conflicts of interest can be reduced by ensuring that advisors recommend products with trailer fees instead of those with high initial commissions.

PEAK's comments on Potential Regulatory Proposals

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

PEAK supports provisions that would lead to investors being better informed on what is being paid in the form of trailing commissions, and what corresponding services should be expected by the investor in return. In our view, the alignment of services and fees has seen significant improvement with the CSA's recent development of rules for Point of Sale ("POS") disclosure and Client Relationship Model ("CRM").

We look forward to seeing how the final versions of these rules, taking into account comments received from all industry stakeholders, will evolve and play a role in increasing investor awareness of a whole slew of issues, including costs of investing and conflict of interest disclosure.

A significant issue to consider is that we must ensure that any new regulations brought in to shed light on the usage of trailing commissions and what they pay for do not lead to confusion on the part of investors, i.e. thinking that trailing commissions are additional charges over and above the management fees already disclosed elsewhere.

We do not agree, however, that consideration should be given to the establishment of a minimum level of ongoing services or a requirement for advisors and their dealer firms to record and monitor the nature, extent and frequency of the services provided. This highly restrictive approach raises a number of questions and issues:

- How would a minimum level of service be defined for different business models, for advisors who sell multiple types of products, and across the different advice relationships within an advisory practice, and further, what entity/organization would determine the standard?

- How would defined service levels impact the development of alternative distribution models?

- How would service levels of advisors be monitored against such a requirement?

There is no doubt in our mind that such measures are likely to create a significant burden on dealers and many other industry stakeholders, as well as increasing distribution and product costs without any corresponding, demonstrable benefit to investors.

2) ***Cap commissions***

PEAK is not in favour of any regulatory undertaking that would directly intervene in the decision of firms, investors and advisors on the appropriate level of compensation for services provided by advisors and dealers. PEAK views the implementation of a model to cap commissions constitutes a form of discretionary price control by regulators, which objectively speaking is not the mandate given to them.

In support of this view, we refer to IIROC's recently issued draft guidance on compensation structures for retail investment products. The draft guidance takes the view that the promotion of transparency and investor protection with respect to compensation structures in the Canadian market can be achieved within the framework of IIROC rules and identifies specific considerations that should be taken into

account by IIROC dealer members and approved persons when they are developing, recommending or supervising the various compensation structures available in the market. PEAK believes that IIROC's balanced assessment and regulatory approach to this issue has value and should be given due consideration by the CSA.

We believe that the specific measures related to capping commissions would be difficult and quite costly to implement. These costs would be borne by investors. A cap could also cause serious economic inefficiencies in the market. The capping model assumes, for example, that dealers and advisors would no longer have ongoing costs for the support and service of their clients beyond a prescribed number of years. Limiting the level of trailing commissions below the cost of providing current services may require advisors to reduce the level of service they provide to their clients, which surely is not the aim of any industry stakeholder.

In any case, the likelihood of an investor reaching the cap is quite limited, as the average mutual fund holding period is 4.5 years, based on a recent survey by Investor Economics. As the majority of investors do not hold their funds for a long enough period of time for the cap to be triggered, we believe that the costs of tracking and converting investor holdings will significantly outweigh any benefits derived.

Finally, it can be observed that over the last five (5) years, overall advisor compensation has not risen, it has fallen. There is evidence that advisors are not earning more because of trailing commissions, but less. The total dollars earned from trailing commissions may well have increased over that 5-year period, but correspondingly, initial commissions have almost disappeared. This cannot be overlooked and needs to be taken into consideration by the CSA in its analysis. The figures cited in the Discussion Paper suggest that trailing commissions have increased by as much as 60 %. Whether that figure is accurate or not remains to be seen, however, this trend has been welcomed by both dealers and regulators as a way to reduce initial commissions and align long term client goals with long term advisor involvement.

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

In general, PEAK would not have issue with this potential change. Nonetheless, we believe that unbundling trailing commissions from the management fee rather than merely separately disclosing the trailing commission may result in adverse tax effects for investors. Currently, the Tax Act allows a deduction for funds for the payment of management fees, which are presently charged in an amount to compensate the manager for the trailing commission it pays to dealers. Once unbundled from the management fee, the trailing commission would only be deductible if the deduction were specifically provided for in the Tax Act. While it is possible that the tax authorities may allow such a deduction over 60 months, this is not a certain outcome. The tax implications of this option need to be analyzed further.

In addition, an argument can be made that the fund company should be considered the collection agency for fees, at the investor's request. For many investors, especially those who want the tax attributes or the convenience of bundled fees, the current MER approach is likely the better one. Bundling is not only bundling of management fees and advisor fees, it is also bundling of fees and costs associated with custodians, reporting, tax combining, and other similar and inescapable costs.

4) ***Discontinue the practice of advisor compensation being set by mutual fund manufacturers***

PEAK is not in favor of any regulatory undertaking that would restrict the decision-making process of firms, investors and advisors on the appropriate level of compensation for advisor and dealer services.

PEAK further reiterates that it is not the mutual fund manufacturer that sets the compensation of the advisor. The mutual fund manufacturer pays the dealer a trailing commission that is used by the dealer to pay for its regulatory, supervisory and dealer functions, including the compensation of advisors. PEAK does not agree that the payment of trailing commissions by the manufacturer is properly characterized as setting advisor compensation or, as noted above, that this practice presents a conflict of interest for the manufacturer.

The pros and cons of eliminating third party compensation schemes embedded fees were first discussed in the OSC's Fair Dealing Model Concept Paper of January 2004. Disadvantages from the elimination of embedded fees were recognized at that time to include: reduced access to advice for clients with smaller accounts; the unwillingness of consumers to pay for investment and financial planning advice; costs to the industry and to advisors; and loss of convenience of payment. These same drawbacks continue to be relevant today.

Embedded fees provide certain benefits to Canadian investors. Small households and investors will likely be significantly disadvantaged by any action which calls for and leads to the discontinuation of embedded advisor compensation, as the fee-for-service model is not geared towards small investors.

PEAK's own experience is that the existence and payment of trailing commissions are rarely the source of consumer complaints. As a result, if the explanation is that investors do not know enough about the existence of trailing commissions to formulate complaints about them, then the solution should be to improve disclosure of trailers, instead of determining that restrictions on costs are the only solution. In that vein, PEAK notes that existing rules for the disclosure and management of conflicts are being strengthened with the useful and timely introduction by the CSA of new rules for POS disclosure and the CRM. PEAK suggests that regulators take a wait and see approach to determine if these new rules are having the desired effect before concluding anything to the contrary and potentially adopting new rules that may be redundant or unnecessary.

The Discussion Paper refers to major international jurisdictions which have very recently implemented, or proposed, regulatory reforms aimed at addressing conflicts perceived to exist with embedded compensation structures. While still very early in the implementation stage of these reforms in the U.K. and Australia, some evidence of the effects are now beginning to emerge, and it is far from being all positive, especially for investors. In the U.S. where the move to an unbundled fee structure has been underway for several decades led by market forces, there is a history of experience that requires substantive analysis before any conclusions can be drawn. Also, contrary to the other jurisdictions mentioned in the Discussion Paper, the regulating of the Canadian mutual fund industry is at a quite mature level, with several useful and important regulatory approaches having been implemented in the 1990s, such as the IFIC Code of Conduct, that still exist today and benefit investors. Reducing the choices that investors have cannot be a good thing.

PEAK's view is that the CSA should take the required time to fully assess the effects of the above-referenced developments on both investors and the mutual fund industry in the other jurisdictions mentioned before moving towards any similar regulatory modifications in Canada.

Additional Research/Analysis that should be undertaken

Among the research and analysis we believe should be undertaken:

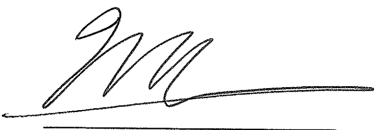
• After finalizing the new rules for POS disclosure and the CRM (including the recently adopted CRM2 rules), incorporating comments from the various mutual fund industry stakeholders, an examination and analysis of the effects of the full implementation of and transition to such rules, over a sufficiently meaningful period of time;

• A period of monitoring outcomes in the jurisdictions cited (U.K., U.S.A., Australia, and EU) to determine whether the reforms truly work to enhance investor protection, or instead have created unintended negative consequences;

• A full and complete cost-benefit analysis, including tax implications for investors, of any major change contemplated.

We thank you in advance for the opportunity to participate in this consultation. We also would appreciate it if you were to consider PEAK, and specifically its president, Mr. Robert Frances (an ex-president of IFIC), as a panelist for the OSC's upcoming roundtable to be held on June 7, 2013. As one of the only independent mutual fund dealers and securities dealers (PEAK Securities Inc.) with a cross-Canada presence, as well as a strong presence in Québec, and having also a securities dealer arm, we feel that PEAK is well positioned to bring a fair, balanced and comprehensive 360 degree viewpoint to the table, which should yield useful results to the panel. Alternatively, if PEAK is not chosen as a panelist, we would appreciate being considered as a general participant for the roundtable.

Sincerely,



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