Mackenzie INVESTMENTS

April 12, 2013

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

To the attention of:

Mr. John Stevenson, Secretary
Ontario Securities Commission
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Me Anne-Marie Beaudoin
Corporate Secretary
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Re: Canadian Securities Administrators (CSA) Discussion Paper and Request for Comment 81-407: *Mutual Fund Fees* (Discussion Paper)

We are writing to provide comments on the CSA's Discussion Paper on mutual fund fees published on December 13, 2012.

Mackenzie Financial Corporation (Mackenzie Investments) is a portfolio adviser and investment fund manager registered under National Instrument 31-103 of the CSA with total assets under management of over $64.3 billion (including mutual funds under management of approximately $42.4 billion) at March 31, 2013. 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. Mackenzie Investments distributes its products through approximately 253 dealers representing approximately 41,000 financial advisers.

It is important to have the broadest and deepest understanding of the desired policy objectives when changes are being considered that affect the fundamental way in which financial services are offered to the public, especially if the potential effects are as far reaching as they appear to be in this document. We welcome the opportunity to add clarity and additional background to this discussion, and strongly recommend that this discussion be more broadly focused on the overall desired distribution model for financial services and products in Canada.

1. General Comments

Many of the critical elements of the Discussion Paper are focused on the transaction of mutual fund purchases and how advisers are paid for the services and advice they provide to the clients they serve. The Discussion Paper concludes that the current environment leads to potential conflicts of interest, and proposes changes that the CSA believes would mitigate those conflicts.

We urge a broader discussion on the broad strengths and weaknesses of the financial services industry in Canada. It is not clear to us what problems or issues the CSA is trying to solve relative to the overall policy needs for retirement saving in Canada.

At Mackenzie Investments, we believe that building long-term relationships with clients is the best way for financial advisers to help individuals reach their financial goals at each stage of their lives. We see financial planning and advice as integral parts of reaching those targets. That advice is usually delivered through an adviser, who keeps clients focused on their long-term goals. Clients currently have choices as to how they access, utilize and pay for professional financial advice in Canada. Some pay directly, through a fee to their adviser's dealer or through transactional commissions, while others pay indirectly through trailing commissions embedded in the products they hold in their investment portfolio. However, it is important to recognize that adviser compensation comes from many sources, not only mutual funds. This narrow focus on mutual fund compensation in the Discussion Paper seems flawed when we look at how advisers use funds within client portfolios.

Independent research has demonstrated the significant value of delivering financial advice to the public, at all income and asset levels.[1] Among other things, advised households (i) are twice as likely to save for retirement at all ages (ii) have significantly higher levels of investable assets at all ages (iii) improve their regular saving for retirement at all income levels (iv) rate themselves as more financially knowledgeable; and (v) are more comfortable making the financial decisions they need to make to plan for their future.

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[1] Value of Advice Report 2012, IFIC; Montmarquette, Claude and Nathalie Viennot-Briot, Econometric Models on the Value of Advice of a Financial Advisor, CIRANO Institute, July 2012

At one time, most financial products, including mutual funds were purchased on a fixed front end load basis, where clients would pay an up-front commission at the time of purchase, and there was no concept of a fee for service or trail commission. However, markets changed, commissions became negotiable and low value or no service transaction models were introduced. The marketplace evolved away from fixed commissions, to negotiated commissions and eventually into the current model today of a fee for service model either through an embedded trail fee or paid directly by the client to the adviser.

While a significant amount of planning and advice is provided at the time of the initial investment, this planning and advice continues for the life of the investment. The current advice compensation model in Canada aligns the dealer's and adviser's compensation with the client's goals (since a significant portion of the compensation is paid out over the life of the investment and will increase as the value of the client's portfolio goes up and decline if it decreases). Further, it provides a basis for the dealer to provide infrastructure and services and for advisers to provide up front counseling to clients with small amounts to invest where a fixed fee or commission model may deter clients from seeking investment planning help. Since the dealer will continue to receive fees from the investments as long as the client remains with the adviser, the client, dealer and adviser can benefit into the future as the investment program continues to evolve to meet the changing needs of the client. In effect, the dealer and adviser are held continuously accountable for his/her initial and ongoing advice. The latest trend to separate the payment for advice increases flexibility and choice for clients to decide how they wish to compensate their adviser and dealer firm. It is important that clients and advisers have flexibility to determine how best to position the consideration for their relationship.

No one distribution model provides a significant advantage over another; rather we should facilitate a regulatory environment that provides flexibility and permits the broadest access possible for individuals to access financial advice. Reducing flexibility and choice can have significant unintended consequences. For example, countries that have banned embedded compensation, such as the United Kingdom and Australia, are beginning to experience a trend identified as the "advice gap". A growing number of clients are unable or unwilling to access the guidance they need to manage their investments[2] and meet their financial planning needs. Given the strong correlation between financial advice and positive financial outcomes that has been referenced in a number of studies[3], this is a worrying development, and one that should be given consideration in this process.

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[2] Deloitte LLP, *Bridging the Advice Gap: Delivering investment products in a post-RDR world.* November 2012.

[3] Value of Advice Report 2012, IFIC; Montmarquette, Claude and Nathalie Viennot-Briot, Econometric Models on the Value of Advice of a Financial Advisor, CIRANO Institute, July 2012

A large proportion of Canadians have access to financial advice through their mutual fund investments, with very positive outcomes compared to other countries.[4] This is a factor that is important in the overall retirement preparedness policies in Canada.

Completely apart from the mutual fund industry, embedded compensation is the standard in approximately 45% of the average Canadian household's investments, including deposits, fixed income, segregated funds, and insurance.

The presentation of the issues in the Discussion Paper focuses only and entirely on mutual funds, which is misguided. The broader financial policy questions relate to the ability of Canadians to access different models of financial advice. The distribution channel as a whole should be the focus of this discussion. Singling out one product that is commonly held with other security types in a client portfolio is inconsistent with the broad policy concerns of disclosure, suitability, compensation and access to financial advice. It leaves impression that the embedded compensation model is unique to the mutual fund industry, that market forces are not driving sufficient innovation, that current regulations are lacking and that clients are exposed to unmanageable conflicts that do not occur elsewhere. There is no support presented for these positions and indeed there is overwhelming evidence that the existing structures have served the investing public very well.

2. Response to Specific Proposals

The Discussion Paper sets forth a series of topics for consideration. The following are our comments on each.

A. Tie Trailing Commissions to Advisers to Specific Services

This proposal arises from an apparent misunderstanding that 100% of trailing commissions are paid for ongoing services provided by advisers. In fact, the compensation is paid to the dealer in connection with the distribution of the financial products and is generally the only source of revenue for mutual fund dealers. This revenue pays for a variety of dealer costs, including supervision, compliance, back office functions, client statement production, insurance and similar expenses – many of which, we note, have increased as a result of recent regulatory requirements – in addition to the cost of compensating advisers. The dealer, not the manufacturer, determines the level of service its advisers are to provide, and their compensation.

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[4] Based on *Canada's retirement-income provision: An international perspective* by Edward Whitehouse Retirees in Canada have well-above average income adequacy compared to other OECD countries (while Australia and the UK are well below average), and Canadian retirees derive a very large proportion of their income from accumulated capital, and little from public transfers when compared to the OECD average.

Regulating service levels is not the best approach. Compensation levels, service levels and service models are best left to competitive and market forces. Consumers enjoy choice and many financial service providers compete through different models with different forms or degrees of advice, but it doesn't mean the cost or benefit is any more or less. That should be up to the client to decide. A component of trail commissions represents compensation to advisers for the initial work done by them in providing advice to clients at the time of the original investment. Second, the payments are made for the continuing services provided by the dealer and the adviser to the client. Because of this, the services provided by advisers to clients will vary depending on a number of factors, including the size of the portfolio and specific needs of the particular client including desired frequency of contact and updates. We have a disclosure regime today which establishes activity of an adviser. We see no downside to increasing disclosure about the types of services that are provided by firms or individuals servicing clients, but again, it should be applied universally to the services of all advisers and firms and not be limited to one product.

B. Mandate a "Do It Yourself" Class for all Funds

"Do It Yourself"(DIY) clients currently have access to a growing selection of investment products, including mutual funds, and if there are unfulfilled client needs, the market will respond, as it has always done. Fund manufacturers should continue to be free to structure their offerings for the clients in their target market whether it includes the advice channel or direct. If a manufacturer decides to focus on clients who seek advice, they should be able to do so. Conversely, a manufacturer who decides to provide products to suit a broader range of clients should be able to offer low cost products suited for clients at discount brokers who do not provide advice if they choose. The particular mutual fund series and the firm or type of advice is a decision of the distributor. Since the majority of mutual fund manufacturers are not distributors, this particular question is more suitably directed to distributors of financial services that target DIY clients and their wish to price and be compensated for their services.

C. Unbundling Trailing Commission and Replacing Them with an Asset Based Fee

Unlike other financial products with embedded ongoing compensation, the trailing commission component of mutual fund expenses is already fully disclosed and readily available to clients.

Unbundling the management fee would enhance disclosure to clients and make products more easily comparable. We would be in favour of this approach if it was applied to all financial products with actual or implied embedded compensation. Further, clients already have access to multiple distribution models with different service not just mutual funds and fee levels – including embedded fees, asset-based fees and transaction commission. The CSA should continue to develop policies and regulations that broaden consumer choice and not drive clients into one specific model which happens to be preferred at the time.

D. Separate Series or Classes for No Load Funds

A number of Canadian fund manufacturers already use this approach.

The argument presented in the Discussion Paper that unit holders choosing the no load option are cross-subsidizing those choosing the deferred sales charge (DSC) option that do not have a separate series is incorrect, in our experience. Although DSCs have an up-front commission paid, they also are typically combined with a lower ongoing trailing commission compared to a no load or front-load product. Which pricing option (if any) proves to be costlier to the fund manager will depend on the details of the product, volumes, size, etc. The DSC pricing option arose in response to client demand and has important beneficial features that the Discussion Paper has not covered and should review in its consultation process.

A fund manufacturer should be able to make a business decision whether to offer these separate series (and at a separate cost), and not mandated to do so by regulators. Furthermore, the administrative burden and associated costs of implementing this are not insignificant and would ultimately be borne by clients. We do not believe that the benefit of requiring separate series outweighs the costs, nor have we seen analysis or research to the contrary.

E. Cap Commissions

Canadian securities regulators have traditionally refrained from regulating compensation and commissions, and for good reason. These issues are best left to the market and the competitive forces that operate to shape it. Freedom to compete is a cornerstone of the financial services sector in Canada and has served the public well. The goal should be to ensure a wide range of consumer choice, which is what the market has done.

If capping fees is being considered as a way to avoid increased cost pressure, there is no evidence to suggest such action is necessary in the mutual fund industry in Canada. There is no trend toward increased cost among mutual funds or in the payment of compensation to dealers and advisers in Canada. In fact, the trend on management fees is down. One significant difference in Canada related to fees arose in the 1990s when GST was introduced, and then HST in the last few years in Ontario and other provinces. Absent these government imposed costs to the client, MERs have been trending downward in a highly competitive market.

F. Implement Additional Standards for Advisers

The question of whether the duties that advisers owe to their clients should be amended, specifically by adding a "best interest" standard, is extensively canvassed in CSA 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.*

Advisers are already governed by a comprehensive set of obligations based on recommending only suitable investments for clients, coupled with the duty to act fairly, honestly and in good faith. We would refer you to the comment letter we submitted on that paper.

G. Discontinue Practice of Having Manufacturers Set Compensation for Advisers

Again, this proposal is based on a faulty premise that fund manufacturers set compensation for advisers. Dealers set compensation for their advisers, not fund manufacturers. Mutual fund sponsors pay commissions to dealers. Those dealers in turn enter into compensation arrangements with their advisers, which are dependent on a number of factors, including the competitive landscape with respect to other distributors as well as the costs that the dealer has to bear in carrying on business. The percentage of the compensation paid to dealers that is in turn paid to advisers is steadily declining, due in large part to the increased costs faced by dealers, including compliance with new or enhanced regulatory requirements.

One assumption behind this proposal appears to be that mandating a fee-only model for adviser compensation would remove a source of potential conflict of interest through increased transparency. In fact, the information clients receive is actually reduced under a fee-based model because clients now must negotiate advisory fees with dealers directly and independently, with no frame of reference as to what is reasonable, or what others are paying for similar services. This contrasts starkly with the current structure where there is comprehensive public disclosure of all fees and commissions in the Simplified Prospectus, Fund Facts and Management Report on Fund Performance. The client would be at an information disadvantage.

There is no cost advantage to clients either. For example, when all factors are taken into account, overall financial advice fees in Canada are on average comparable to those in the United States, where fee-for-service is the dominant model[5]. Indeed for clients with lower asset levels, the all-in cost may be significantly lower in an embedded compensation model than a fee for service model.

Fee for service accounts already exist in Canada, as do fund series designed to work in these structures (that is, funds that have lower or no trailing fee component). Advisers who want to provide financial advice through a fee-based service model are free to do so and to argue its merits. Further, fund manufacturers are able to structure their product offerings to address the needs of clients who prefer having a fee-based advisory relationship. Those clients who want to pay an additional fee for an advisory relationship currently have that option. Freedom of competition and market forces will continue to evolve the offerings to clients over time.

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[5] Investor Economics and Strategic Insight, *Monitoring Trends in Mutual Fund Cost of Ownership and Expense Ratios, A Canada-U.S. Perspective,* November 2012.

Clients who prefer to invest in a fund with all the fees included, fully disclosed, and widely available for comparison and public scrutiny, should not be deprived of the opportunity to do so. Ultimately the goal of this exercise should not be to limit freedom of choice for clients. We see no advantage to clients to support a proposal that eliminates one option in favour of an option that may not be as advantageous for them.

We thank you for the opportunity to provide comments on the Discussion Paper. Please feel free to contact Tim Pryor (tpryor@mackenziefinancial.com) or myself, if you wish to discuss our letter further, if you require additional information or have any questions.

Yours truly,

MACKENZIE FINANCIAL CORPORATION

Charles R. Sims, FCA
President and Chief Executive Officer