Association of Canadian Compliance Professionals
Association canadienne des professionnels en conformité

March 12, 2014 VIA E-MAIL ONLY

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

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CSA Notice 81-324 and Request for Comment Proposed CSA Mutual Fund Risk Classification Methodology for Use in Fund Facts
http://www.osc.gov.on.ca/documents/en/Securities-Category8/csa_20131212_81-324_rfc-mutual-fund-risk.pdf

On behalf of the undersigned, and more particularly the Association of Canadian Compliance Professionals, (ACCP) we appreciate the opportunity and are pleased to reply to the request for comments by submitting

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the following feedback. We believe that understanding the key drivers behind the push for standardization is paramount. Our perception suggests that the principle proponents e.g. industry players; fund companies and managers whom have a substantive stake in the final product, maintain critical positions of influence that if unchallenged threaten to skew the outcomes. We are obliged therefore, to support Investment Dealers, Investment Advisors and Investors so as to ensure that the proposed methodology is sound and results in an appropriate balance for all stakeholder groups. Categorically, we believe standardization is a good thing. Standardization affords universal benefit and endeavors to eliminate discretionary judgment. We are therefore, prepared to endorse an industry-wide standard methodology that is inherently unbiased and transparent.

True to its' mission, we believe CSA has an opportunity to seize upon its' commitment to harmonize the regulatory environment in Canada, to provide certain and specific protections to investors from unfair, improper and fraudulent practices, to foster the growth and maintenance of capital markets and reduce risks to market integrity and to investor confidence, while retaining flexibility and innovation.

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Issues for Comment on the Notice and Request for Comment

1. As a threshold question, should the CSA proceed with (i) mandating the Proposed Methodology or (ii) adopting the Proposed Methodology only as guidance for fund managers to identify the mutual fund's risk level on the prescribed scale in the Fund Facts? Are there other means of achieving the same objective than by mandating the Proposed Methodology, or by adopting it only as guidance? We request feedback from investment fund managers and dealers on what a reasonable transition period would be for this.

   It is our opinion that the proposed methodology be prescriptive and mandated. We understand the proposed methodology is intended as an inclusive exercise. It stands to reason therefore, that interested parties / stakeholders will and should benefit equally from its' universal application.

   We would argue that entertaining other means of achieving the objective i.e. voluntary cooperation with guidance, simply maintains a status quo. Voluntary cooperation ignores the existing irregularities. The manner in which fund risk levels have been allowed to be determined over time has resulted in a certain and specific randomness. We understand the exercise is intended at least in part, to address this randomness.

   Value Creation;

   "Big Data. Unstructured data. Semi-structured data. Data is all over the technology news, and for good reason. It is overwhelming organizations, requiring them to find new ways to operate, stay competitive, better serve their customers and bring new products to market faster."

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"Gartner predicts that enterprise data will grow by 800 percent in five years, with 80 percent of it unstructured. The accelerating growth and fragmentation of data – in the cloud, in social media and in enterprise systems – creates a bigger knowledge access problem. It makes it nearly impossible to executives, employees and customers to leverage contextually relevant information when they need to solve challenges, make critical decision and simply do their jobs."

"Very few organizations are far along the maturity curve in dealing with Big Data, but the incentive is there. The ability to address Big Data is going to be the most intensive and important infrastructure change for IT in the next decade. Moreover, it has major implications for knowledge management. Organizations need to start treating knowledge and knowledge workers as strategic assets in order to compete and meet the challenges of the future."

eBook – the Next Wave of Value Creation 2013
Measuring Return on Knowledge in a Big Data World - Leveraging Knowledge as Your Greatest Asset.
info@coveo.com, www.coveo.com.

Coveo - Measuring Return on Knowledge

"What if the next great phase of computing innovation and wealth creation is less about consumer adoption of new technologies and more about unlocking the untapped value inherent in every company's disparate sources of data – from websites, to social media, to email, CRM and ERP systems, to old Word and Excel documents stored in every computer of every employee? Imagine a world where every document on every data platform is instantly organized, indexed and searchable in much the same way consumers search the Web, with natural language queries? Imagine if every company could instantly become 10% more efficient?"

Bruce Rogers, Forbes' Chief Insights Officer, September 2012.

The Regulator has a substantive opportunity to lead on this issue by leveraging impending changes, notably the Point of Sale (POS) regulation (National Instrument 81-101 Mutual Fund Prospectus Disclosure) and Fund Facts delivery.

Transition period; we believe it too soon to make a reasonable assessment on transition. Consider costs, impending legislation, industry appetite, etc.

2. We seek feedback on whether the Proposed Methodology could be used in similar documents to Fund Facts for other types of publicly-offered investment funds, particularly ETFs. For ETFs, what, if any, adjustments would we need to make to the Proposed Methodology? For instance should standard deviation be calculated with returns based on market price or net asset value per unit?

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It is our opinion that the proposed methodology could be used principally, in similar documents to Fund Facts for other types of publicly-offered investment funds, particularly ETF's. Again, provided the exercise to determine the usefulness of the objective is inherently unbiased and transparent.

Whether the proposed methodology would require adjustments and whether standard deviation for other types of publicly-offered investment funds is best measured based on market price or net asset is or would be best determined by a focussed investigation to establish same.

3. We seek feedback on whether you agree or disagree with our perspective of the benefits of having a standard methodology, as well as whether you agree or disagree with our perspective on the cost of implementing the Proposed Methodology.

   Agreed. A standard methodology is universally beneficial.

   It is our opinion the implementation costs however, will be substantial. Consider the following;

   Financial costs:
   - *changes to Dealer documents,*
     - *policies,*
     - *procedures,*
     - *KYC,*
     - *risk tolerance questionnaires,*
     - *disclosures,*
   - *back-office systems changes,*
   - *other.*

   Intangible costs:
   - *timing of the proposal,*
   - *customer interface and relationship; what benefits accrue from having to explain to customer the difference between 'High' and 'Very High' risk, this in our opinion calls into question the intention of the proposed methodology; who's benefit is the exercise intended to serve,*
   - *suitability assessments / account management; what benefits accrue from having to return to customers whom are immediately 'offside' once implementation has been considered,*
   - *material changes debate; systemic changes may become over-reaching, 'matching' KYC to product is counter-intuitive and potentially unmanageable.*

4. We do not currently propose to allow fund managers discretion to override the quantitative calculation for risk classification purposes. Do you agree with this approach? Should we allow discretion for fund managers to move their risk classification higher only?

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It is our opinion that fund managers should not be allowed discretion to override the quantitative calculation for risk classification purposes. It is clear, an appetite for simplicity exists otherwise the issue is not on the table. Discretion for fund managers to 'move' risk classification is in part, the reason for this debate. In circumstances limited or otherwise, we believe allowing fund managers to continue using discretionary judgment is not in keeping with the intention of the exercise and ignores the appetite for change.

Issues for Comment on the Proposed Methodology

5. Keeping the criteria outlined in the introduction above in mind, would you recommend other risk indicators? If yes, please explain and supplement your recommendations with data/analysis wherever possible.

   At this time we do not endorse nor do we recommend the use of other risk indicators.

6. We believe that standard deviation can be applied to a range of fund types (asset class exposures, fund structures, manager strategies, etc.). Keeping the criteria outlined in the introduction above in mind, would you recommend a different Volatility Risk measure for any specific fund products? Please supplement your recommendations with data/analysis wherever possible.

   Our position concerning standard deviation we believe is established.

   EFT's and Exempts by their nature are different products. While we agree that the proposed methodology could be used principally in similar documents, we would accordingly, support investigating the possibility of using a different volatility risk measure for specific fund products.

7. We understand that it is industry practice (for investment fund managers and third party data providers) to use monthly returns to calculate standard deviation. Keeping the criteria outlined in the introduction above in mind, would you suggest that an alternative frequency be used? Please specifically state how a different frequency would improve fund risk disclosure and be of benefit to investors. Please supplement your recommendations with data/analysis wherever possible.

   See 8.

8. Keeping the criteria outlined in the introduction above in mind, should we consider a different time period than the proposed 10 year period as the basis for risk rating disclosure? Please explain your reasoning and supplement your recommendations with data/analysis wherever possible.

   We canvassed the opinions of a number of Advisors. It is felt that standard deviation, in terms of defining risk mathematically is not perfect but may be the easiest method to understand in its' simplest form and therefore, easiest to convey to customers.

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"The way it has been used in the past, has been monthly standard deviations for 36 months. This never made sense to me in that, risk levels are difficult to measure over such a short time span; over 36 months or three years. Most fund companies are now using a standard deviation based on years rather than months. I think that a fund that has been in operation for 25 years or a fund manager that has been managing for years gives a much better picture of risk when standard deviation is used for comparison. The beauty about standard deviation is that it can be applied to portfolios and measured from time to time. It exemplifies the risk reduction that comes from diversification which is a big part of Financial Planning and the achievement of investment goals. The regulator spends too much time on risk without defining it mathematically and 'prescribing its' universal application' (sic). It is something the industry could adjust to 'over time' and finally the regulator would have something to lead with. It would also be a way for advisors to protect themselves when accused of inappropriate risk by a customer after the fact."

Ed Thompson, CFP, BSc.Ag Money Concepts. February 2014.

We believe a minimum of 10 years be prescribed.

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9. Keeping the criteria outlined in the introduction above in mind, should we consider an alternative approach to the calculation by series / class? Please supplement your recommendations with data/analysis wherever possible.

   Similar to EFT's and Exempts. See 11 ii. If an alternative approach to calculations by series / class can be shown in an inherently unbiased, transparent and understandable manner we would support an investigation. Again however, diluting the objective by layering seemingly endless options is of limited or no value.

10. Keeping the criteria outlined in the introduction above in mind, do you agree with the criteria we have proposed for the use of a reference index for funds that do not have sufficient historical performance data? Are there any other factors we should take into account when selecting a reference index? Please supplement your recommendations with data/analysis wherever possible.

    No comment.

11. Keeping the criteria outlined in the introduction above in mind,

    i. Do you agree with the proposed number of risk bands, the risk band break-points, and nomenclature used for risk band categories?

    We are not certain that there is any tangible benefit with the proposed number of risk bands, the risk band break-points, and the nomenclature used for risk band categories. Changes to 'risk bank' classifications we believe has far-reaching implications. It appears CSA recognizes this and implies that a number of products will be classified in or at a risk band / level that differs from what is or would be shown /disclosed in the

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Fund Facts. It should be noted, this should not be interpreted as meaning that the fund has any greater degree of risk than previously.

ii. Do the proposed break points allow for sufficient distinction between funds with varying asset class exposures / risk factors? If not, please propose an alternative, and indicate why your proposal would be more meaningful to investors. Please supplement your recommendations with data/analysis wherever possible.

We believe the 'existing' break points are sufficient to distinguish between funds with varying asset class exposures / risk factors.

11. Do you agree with the proposed process for monitoring risk ratings? Keeping the criteria outlined in the introduction above in mind, would you propose a different set of parameters or different frequency for monitoring risk rating changes? If yes, please explain your reasoning. Please supplement your recommendations with data/analysis wherever possible.

Yes.

13. Is a 10 year record retention period too long? If yes, what period would you suggest instead and why?

See 8.

14. Please comment on any transition issues that you think might arise as a result of risk classification changes that are likely to occur upon the initial application of the Proposed Methodology. How would fund managers and dealers propose to minimize the impact of these issues?

Transition issues; we believe it too soon to make a reasonable assessment on transition. Consider costs, impending legislation, industry appetite, etc.

We appreciate the opportunity to comment. Should you have any questions do not hesitate to contact the undersigned.

Regards,

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