Via email

September 23, 2011

John Stevenson, Secretary
Ontario Securities Commission
20 Queen Street West, Suite 1903, Box 55
Toronto, ON M5H 3S8

and

Me Anne-Marie Beaudoin, Corporate Secretary
Autorité des marchés financiers
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Dear Mr. Stevenson and Ms. Beaudoin,

Re: Notice and Request for Comment – Proposed Amendments to National Instrument 31-103 *Registration Requirements and Exemptions* – Cost Disclosure and Performance Reporting

This comment letter is being submitted on behalf of the following entities within RBC: RBC Dominion Securities Inc.; RBC Direct Investing Inc.; Royal Mutual Funds Inc.; RBC Global Asset Management Inc.; RBC Phillips, Hager & North Investment Counsel Inc.; Phillips, Hager & North Investment Funds Ltd; and Commission Direct Inc. We are writing in response to the Canadian Securities Administrators' ("CSA") request for comment on the proposed amendments to National Instrument 31-103 *Registration Requirements and Exemptions* ("NI 31-103") regarding cost disclosure and performance reporting ("Proposed Amendments" or "Proposal") published on June 22, 2011 ("Notice"). We appreciate the opportunity to provide comments on this important initiative.

We have participated in the industry working groups organized by the Investment Industry Association of Canada ("IIAC"), Investment Funds Institute of Canada ("IFIC") and Canadian Bankers Association ("CBA"), and contributed to the comments in their submissions. In this regard, we support and endorse the comments submitted by the named industry associations. That being said, we would like to provide further comments on certain issues where we have significant concerns.

1. Application of Cost Disclosure and Performance Reporting Requirements

We appreciate the efforts of the CSA, Mutual Fund Dealers Association ("MFDA") and Investment Industry Regulatory Organization of Canada ("IIROC") to date to address requirements for cost disclosure and performance reporting. While the Proposal seeks to impose standardized requirements across various types of registered firms, there is clear evidence suggesting that a "one size fits all" approach may not be appropriate when it comes to cost disclosure and performance reporting rules. In practice, different distribution channels deal with different products and serve different segments of clients with diverse needs, expectations and levels of experience related to financial instruments.

As stated in the Notice, the CSA has considered the findings from the investor research conducted by The Brondesbury Group and Allen Research Corporation in developing this Proposal. According to the

report of The Brondesbury Group, entitled *Performance Reporting and Cost Disclosure* ("Brondesbury Research"), the objective of the investor research was "to obtain information on *retail*[1] investors' understanding and expectations in the areas of cost disclosure and performance reporting by registrants". The results provided under the Brondesbury Research are "based on a representative sample of some 2,000 Canadian households that currently invest". Further, the report *Canadian Securities Administrators Performance Report Testing,* prepared by Allen Research Corporation ("Allen Research"), was prepared based on 18 one-on-one "document interviews" with individual investors and 15 one-on-one interviews with various registrants.

The Allen Research has cautioned that "because of the exploratory nature of the technique and the small sample size, [its] findings may not be generalizable to the target populations as a whole. Rather they constitute hypotheses to be used as a guide to judgement or as the basis for further quantitative research." Given that the goal of this Proposal is to address concerns of clients of *all* registered firms, we are concerned whether the findings provide relevant, adequate and sufficient data for the CSA to develop this Proposal. For example, it is not clear to us whether the needs and expectations of self-directed (discount brokerage) clients have been distinguished from the needs of clients who have full service advisory accounts. Similarly, the expectations of a typical high net worth client or institutional pension plan client of a portfolio management firm can vary quite significantly from those of an in-branch mutual fund investor. The Allen Research supports the view that the type of advisor relationship and levels of investment shape the nature and source of information used. As well, the Brondesbury Research strongly supports the notion of different tiers of investors based on the amount invested, expressed in investor knowledge and sophistication; it is shown that more than half of those wanting more detailed information are willing to pay for it, most notably among more sophisticated investors. In our view, these findings clearly demonstrate the need for a flexible approach to cost disclosure and performance reporting, depending on the type of clients registrants serve and types of investment they sell or manage.

As also acknowledged in the Allen Research, the proposed changes will be difficult and expensive for registered firms to implement. One of the industry suggestions is to establish a minimum portfolio size reporting threshold (i.e. $100,000) for which performance reporting would not be mandated by the CSA. In our view, a flexible approach appropriate to the types of clients who make use of various distribution channels would be a more prudent and effective approach so that any additional costs, which are ultimately borne by investors, are only passed on to the clients who need to receive more detailed reporting. For example, the Brondesbury Research states that small investors, those with no more than $50,000 in investments and savings, lack a good understanding of investment and performance terms and would therefore benefit from highly simplified information that is easy to understand. On the other hand, it is stated that more sophisticated investors are willing to pay a bit more than most others for enhanced information. Given the significant economic effect of the proposed amendments, it is very important to strike the right balance between the perceived benefits and increased costs of investing.

With this in mind, we urge the CSA to revisit the uniform application of the Proposal and to work with the MFDA and IIROC to take into account the characteristics of various client segments and distribution channels. In this regard, we recommend the following:

(i) Non-Retail Accounts

We respectfully submit that the proposed cost disclosure and performance reporting requirements should not apply to non-retail accounts for two reasons: (1) accounts for institutional clients are generally "cash on delivery" ("COD") accounts meaning that cost disclosure and performance reporting is not practically possible for these types of accounts; and (2) institutional clients are generally sophisticated clients and do not require prescribed cost disclosure and performance reporting.

[1] Emphasis added.

a. *COD accounts*

Generally, registered firms do not provide custodial services for institutional clients; rather, accounts for institutional customers are generally COD accounts. Proposed subsection 14.14(5.2) requires the account statement to include the original cost of each security position. This requirement is challenging for COD accounts since cost information for the securities in COD accounts is not available to the registered firms, rendering the cost/performance reporting meaningless for both the dealer and, more importantly, the client as there is no information on which to base the reporting. Consequently, we request that COD accounts be exempted from the proposed sections 14.14(5.1) and (5.2), 14.15 and 14.16.

b. *"Institutional" clients*

The Proposed Amendments recognize that a number of sophisticated investors do not require certain reporting by providing exemptions from proposed sections 14.2(2)-(4.1), 14.15 and 14.16 to accounts of registered firms, Canadian financial institutions, Schedule III banks and permitted clients (subject to conditions). We note that investment dealers have processes in place to meet IIROC's requirements for "institutional customers", as defined under IIROC Rules. In practice, the incomplete overlap of clients that meet the definitions of "Canadian financial institutions", "permitted clients" and/or "institutional customers" poses significant challenges for investment dealers in identifying the applicable requirements for any one client. Since the objective is to provide protection to clients who need it, we would suggest that accounts of clients that meet the definition of "institutional customer" under IIROC Rules should be exempted from the stated provisions or, alternatively, the exemptions should be granted to IIROC members.

Further, since the investor research noted above was conducted from the perspective of retail investors, we are concerned whether the findings adequately represent the needs and expectations of sophisticated and/or non-individual clients. Pending further research, we are of the view that the benefits of the requirement to provide cost disclosure, under proposed sections 14.14(5.1) and (5.2), and the requirement related to benchmarks, under proposed sections 14.2(2)(m) and 14.17, would not apply to "institutional customers" as defined under IIROC Rules. Consequently, we request that exemptions from the stated provisions be granted to accounts of clients that meet the definition of "institutional customer" under IIROC Rules or, alternatively, to IIROC members.

Lastly, for discretionary portfolio managers, their institutional clients engage third parties such as custodians or independent consultants that perform a number of additional services for them including valuation of assets, reconciliation and performance reporting. The imposition of additional reporting requirements on portfolio managers for the purpose of benefiting their highly sophisticated clients would seem to be unnecessary and duplicative.

(ii) *Order execution only accounts*

The objective of performance reporting is to allow clients to assess the value of the investment advice/ investment management services that registrants have provided to them. Due to the nature of order execution only accounts, clients of registrants who have such accounts do not receive investment advice/investment management services. As such, we request that an exemption from proposed sections 14.15 and 14.16 be provided to such accounts.

(iii) *Investment Management Fees accounts*

Proposed subsections 14.2(4.1)(b) and (c) would require a registered firm to deliver to its clients, on an annual basis, information relating to operating charges and transaction charges. For fee based accounts, such as managed accounts provided by IIROC members and discretionary accounts offered by portfolio managers, the management fees typically include the operating and, where applicable, transaction charges. Clients with these types of accounts are made aware of and consent in advance to the extent of the investment management fees that they will pay; this occurs through various discussions with registered individuals/firms and is reduced to writing via written and signed account documentation. An

attempt to break down the charges related to each service provided to these clients would not offer value-added information. For example, it is customary for clients with discretionary managed accounts of portfolio management firms to incur brokerage commissions on trades at institutional rates. Unbundling of trading costs would be an extremely cumbersome process with little, if any, real benefits to clients. Similarly, unbundling of trading charges involved in the pool fund investments would require significant effort by the registrants. We are of the view that complexity of such undertaking would far outweigh the perceived benefits to clients. In this regard, we request that managed accounts be exempted from these sections.

(iv) *Accounts subject to MFDA Rules*

The MFDA addressed the principles of the Client Relationship Model ("CRM") through recent amendments to the MFDA Rules related to client accounts, account supervision, client reporting and communications including performance reporting. These rules were the subject of an extensive consultation process, approval by the CSA and ratification by the MFDA Board. Currently, mutual fund dealers are planning and making significant process and system changes to meet the June 2012 implementation date of the MFDA's performance reporting rule. It is our view that, in the absence of a meaningful analysis of the costs and benefits of the Proposal, the CSA should not introduce any further changes at this time for MFDA members in order to allow them to complete the orderly implementation of these significant developments.

2. Point of Sale Disclosure of Charges

Proposed section 14.2(3.1) is mandating point of sale disclosure of charges relating to all investment products for non-managed accounts. We note that clients (will) have access to information relating to charges through various sources, including relationship disclosure documents, the prospectus for a fund and/or the Fund Facts document. With respect to mutual funds, we reiterate the concerns highlighted in IFIC's submission dated September 7, 2011, that there is a significant overlap between this aspect of the Proposal and CSA's unfinalized Point of Sale disclosure framework for mutual funds ("Framework"). Following the implementation of Stage 1 of the Framework on January 1, 2011, the CSA recently released the Stage 2 proposal for comment. The industry is now preparing for and anticipating the publication for comment of Stage 3, which addresses the point of sale delivery for mutual funds. In this regard, we support IFIC's view that the proposed point of sale disclosure of charges for mutual funds should be effected through the implementation of Stage 3 of the Framework and not through this Proposal.

Disclosure of charges regarding mutual funds alone has been the subject of numerous consultations and request for comments, and recognizing the complexity of the issue has called for a three-stage implementation. Likewise, we strongly believe that the extent and significance of the proposed point of sale disclosure of charges requirement, being applicable to transactions in mutual funds and all other investment products, warrants a separate industry consultation.

Further, registered firms that offer order execution only accounts are challenged by the point of sale disclosure of charges requirement. Clients who have such accounts trade in reliance on their own strategies, not pursuant to recommendations of registered firms; they do not consult or inform registered firms prior to entering the trade, especially when related information is available in product materials (e.g. a prospectus). Notwithstanding the above two paragraphs, we request that an exemption from proposed section 14.2(3.1) be provided to order execution only accounts.

3. Mutual Funds - Operational Challenges

In several instances, the Proposed Amendments mandate registered firms to report on certain fees and/or charges information that are not within the domain of the registered firms but are controlled by third parties such as fund managers, trustees and custodians:

(i) *Deferred Sales Charges ("DSC")*

As part of a proposed annual reporting requirement to clients, proposed subsection 14.2(4.1)(f) mandates an identification of any securities that may be subject to DSC. In practice, it is difficult to identify DSC funds where the schedule has expired.

Proposed subsection 14.12(1)(c) requires trade confirmations to include the DSC charged in respect of the transaction(s) in question. At this time, some registered firms' trade confirmations disclose redemption fees, but do not distinguish between DSC and short term trading fees.

In light of the CSA's mutual funds point of sale framework, we recommend that the Proposed Amendments should remove the references to the disclosure of DSC to take into account that registered firms would be able to rely on the Fund Facts document for disclosure of mutual funds related fees and charges once the new framework is implemented.

(ii) *Trailing Commissions*

Proposed subsection 14.2(4.1)(g) mandates the annual reporting of the dollar amount of trailing commissions on a per account basis. We note that this information is not readily available for registered firms. Currently fund companies provide registered firms with reporting of trailer fees attributable to representatives at the fund company level only; they do not report the dollar amounts received at an account and/or fund level. Therefore, we support IFIC's recommendation that the proposed section should be revised to mandate uniform disclosure be made to clients explaining trailing commissions and referring to the Fund Facts document for the percentage amount of commission for a specific product.

4. Use of Benchmarks

We support the CSA's decision not to impose delivery of benchmark information in the Rule, and agree that the use of benchmarks has its challenges. For example, we note that the use of benchmarks that are based on widely recognized and available indices and/or broad-based securities market indices may not always be appropriate. For clients' investment portfolios that have identified the nominal rates of return in the financial plan, the objectives of these portfolios are to meet the nominal rate of return, not an index return. In addition, the indices may be based on portfolios of securities that do not represent prudent portfolio management investing. While the index may be conventionally accepted as 'the market', it does not represent prudent diversification as it is not 'managed'.

On the discretionary institutional side of the business it is important to note that sophisticated clients often dictate the manner in which benchmarks will be used by the portfolio manager in the management of an account. In this regard, the guidance set out in the Companion Policy does not seem relevant in the context of institutional clients. There is no clear indication why exemptions otherwise applicable to sophisticated clients have not been extended to benchmark information reporting.

In light of the above, we recommend that proposed sections 14.2(2)(m) and 14.17 be removed until the subject of benchmarking is researched further.

5. Cost disclosure

Notwithstanding part 1 of this letter, with respect to the proposed requirement for registered firms to include in the account statement the original cost information of each security position, we support IIAC's recommendation that registered firms should be given flexibility to disclose either book cost or original cost of the security in question, for reasons outlined in IIAC's submission dated September 20, 2011. Where the Proposal must mandate one method, registered firms should be required to disclose book costs instead of original costs.

6. Level of Cost Disclosure and Performance Reporting

Notwithstanding part 1 of this letter, registered firms should be provided with flexibility as to whether performance reporting, cost disclosure and/or benchmarks are reported at the account or portfolio level. The Proposed Amendments must recognize the distinction between “account level” and “portfolio level”. In many cases, the accounts of one client are components of that client’s portfolio. The requirement to provide clients with performance and/or benchmark information at the account level is counter productive to 'transparency' and may cause confusion to the clients. For instance, if a client has a balanced portfolio constructed of a 'fixed income' account and an 'equity account', providing the client with account level performance information would not offer a full picture on how his/her overall portfolio is performing.

7. Timing of Implementation and Transition Periods

The implementation of performance reporting and cost disclosure requirements will subject registered firms to significant and costly system and information technology developments. While registered firms strive to dedicate the required resources to promote the goal of enhancing client reporting, alignment of the CSA, MFDA and IIROC’s development and implementation timelines for such initiatives would be of great assistance. In order to ensure that meaningful disclosure is available for clients, we support IFIC and IIAC’s recommendations that a 3-year transition period be provided for the proposed amendments to section 14.2(2), 14.12 and 14.14 and for proposed sections 14.15 and 14.16 (except 14.16(3)(c),(d)).

We would welcome the opportunity to discuss the foregoing with you in further detail. In particular, we would recommend that the CSA continue dialogue with various industry participants and would be pleased to play a role in such a process. If you have any questions or require further information, please do not hesitate to contact the undersigned.

Sincerely,

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David Agnew
Chief Executive Officer
RBC Dominion Securities Inc.

“Doug Coulter”

Doug Coulter
President
RBC Global Asset Management Inc.
Phillips, Hager & North Investment Funds Ltd.

“Wayne Bossert”

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cc. Russell Purre, Chief Compliance Officer, RBC Dominion Securities Inc. (Retail)
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