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TO: **Purdy Crawford** FAX: 862-6666
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August 30, 2002

Five Year Review Committee
c/o Purdy Crawford, Chair
Osler, Hoskin & Harcourt LLP
Barristers & Solicitors
Box 50, 1 First Canadian Place
Toronto, Ontario M5X 1B8

Dear Mr. Crawford:

Re: Five Year Review of Securities Legislation in Ontario

We appreciate the opportunity to provide our comments on the Draft Report of the Five Year Review Committee ("the Draft Report") on behalf of the Royal Bank of Canada and its wealth management division, RBC Investments ("RBCI"). The following business units are included under the RBCI umbrella: Royal Mutual Funds Inc. ("RMFI"), the principal distributor of the Royal Mutual Funds, registered as a Mutual Fund Dealer or its equivalent across Canada, RBC Funds Inc., the manager of the Royal Mutual Funds and the RBC Advisor Funds, RBC Dominion Securities Inc. ("RBC DS"), registered as an Investment Dealer/Broker or its equivalent across Canada, Royal Bank Action Direct Inc. ("Action Direct"), also registered as an Investment Dealer – Equities & Options, RBC Global Investment Management Inc. ("RBC GIM"), registered as an Adviser in the category of Investment Counsel and Portfolio Manager, as well as a Limited Market Dealer (Conditional) and a Commodity Trading Manager under the *Commodity Futures Act* and RBC Private Counsel Inc., which is registered in the categories of Investment Counsel and Portfolio Manager and Limited Market Dealer.

General Comments

The Draft Report is comprehensive in its scope and contains 85 recommendations. We do not propose to comment on each recommendation and have focused instead on those that are of particular concern to the Royal Bank of Canada and RBCI. We have

organized our comments in a manner that corresponds to the recommendations as set out in the Executive Summary to the Draft Report.

We have read the submission prepared by the Canadian Bankers Association ("CBA") in response to this initiative and are generally supportive of the views reflected therein.

We note that there are several significant regulatory initiatives currently underway relating to securities regulation in Canada proposed by the securities regulatory authorities and the Canadian Securities Administrators ("the CSA"). Some of these initiatives include the British Columbia Securities Commission's "New Proposals for Securities Regulation", the Ontario Securities Commission's ("OSC") Fair Dealing initiative, the release of the CSA's Concept Proposal 81-402 outlining a new vision for mutual fund governance in Canada, as well as the CSA's proposals for harmonized continuous disclosure and uniform securities laws. The recommendations in the Draft Report must be considered in light of these other concurrent regulatory initiatives.

Part 1: The Role of the Commission in Capital Markets Regulation

Recommendations 1 and 2 - Single Securities Regulator / Harmonization

We support the Committee's recommendation that the provinces, territories and federal government work toward the creation of a single securities regulator with responsibility for the capital markets across Canada. We believe that the current fragmented system of regulation with separate overlapping provincial/territorial securities regulators and financial services regulators is not only costly, but also duplicative and highly inefficient.

Recognizing that divergent views exist on whether or not a single national regulator is the appropriate model or form of national regulation, we believe that it is critical that steps be taken in the short term, such as mutual reliance among jurisdictions, with a view towards moving to a single national regulator. Accordingly, we support the Committee's recommendation to incorporate delegation authority into the *Securities Act* (Ontario) ("the Act") to enable securities regulators to delegate authority amongst themselves.

We also support the recommendation for continued harmonization of securities laws across Canada and the efforts of the CSA's Uniform Securities Act project. As the Draft Report states, harmonizing provincial/territorial securities laws would significantly simplify securities regulation in Canada. We also endorse the recommendation that securities legislation across the country be amended to provide for "mutual recognition" – that a securities regulator may deem that compliance by a market participant with securities laws in another specified Canadian jurisdiction constitutes compliance with securities laws in the regulator's own jurisdiction.

Recommendation 3 – U.S. GAAP

We agree with the recommendation to permit both foreign and Canadian companies to prepare their financial statements in accordance with U.S. GAAP. However, we believe

there should be an ongoing requirement to reconcile the statements to Canadian GAAP until the adoption of International Accounting Standards.

Recommendation 4 – International Accounting Standards

We agree with the recommendation to move to International Accounting Standards, however, such a move should be coordinated with the Canadian Institute of Chartered Accountants ("CICA"), the Canadian standard setter. Ideally, the timing of such a move should also coincide with such a move by the U.S. standard setter, the Financial Accounting Standards Board, so that no new U.S./ Canadian GAAP differences are created.

Recommendation 7 – Harmonized Functional Regulation

The Draft Report recommends that the CSA, provincial and territorial governments and the federal government move to adopt a system of harmonized functional regulation across Canada, whereby all Canadian capital market activities, products and conduct are regulated by a single market conduct regulator and fiscal solvency matters are regulated by a single prudential regulator.

We support the position taken in the CBA's response to this recommendation and reiterate that while attempts to streamline the regulatory structure for the securities industry are important, care must be taken that these attempts do not interfere with the national regulatory structures for banks and other financial institutions.

Part 2: Flexible Regulation

Recommendation 11 – Basket Rulemaking Authority

We agree with the recommendation to give the Commission "basket" rulemaking authority similar to that granted the Lieutenant Governor in Council under clause 143(2)(b) of the Act, so that the Commission may make rules respecting any matter that, in the opinion of the Commission, is "necessary or advisable for carrying out the purposes of the Act".

Recommendations 12, 13 and 14 – The Need to Streamline the Rulemaking Process – Length of Comment Period

Recommendations 12, 13 and 14, which provide for shorter comment periods on proposed rules and policies were prompted by concerns that the rulemaking process in Ontario needs to be more streamlined. The Draft Report notes that Ontario prescribes a 90 day initial comment period for rules and a 60 day initial comment period for policies, which is longer than any other Canadian jurisdiction. The Committee recommends that these timeframes be reduced to 60 days and 30 days respectively.

We strongly disagree with this recommendation and do not believe that the reduction in the length of the comment periods for rules and policies will achieve the aim of streamlining the regulatory process. All it would accomplish is a reduction in the amount of time that interested parties have to review and comment on new or amended rules or policies. We submit that the proposed reduced timeframes would not provide adequate time to solicit meaningful comments from market participants.

The regulators should be careful to ensure that these proposed changes to the initial comment periods and the requirement for republication do not result in the adoption of significant rules and policies, or in the adoption of significant changes without giving affected parties a reasonable opportunity to comment. The submission of informed and detailed comments is important at every step of the development process of a proposed regulatory initiative. This is particularly true with respect to comments that are submitted at the preliminary stages. We suggest that one way to expedite the regulatory process is to increase the amount of consultation with the industry prior to publication, rather than reduce the comment period after publication.

The Committee believes that the Commission should have more flexibility and discretion in deciding when republication of a proposed rule or policy is warranted. In our view, the recommendation that proposed rules should be republished "only if the Commission proposes changes to a rule that the Commission considers to be material" is too narrow. It would permit the Commission to rely solely on its own view of the materiality of proposed changes and arguably could result in some changes which market participants consider material not being republished for comment.

For the above reasons, we submit that Ontario's 90 day comment period for rules and 60 day comment period for policies should be preserved and that the period for Ministerial approval of rules remain at 60 days.

Recommendation 16 – Cost-Benefit Analysis

We agree with the recommendation that the Commission should undertake cost-benefit analyses to assess the effectiveness of proposed regulations and that such analyses should be made public. Any cost-benefit analysis should be undertaken well in advance of the release of any proposed regulatory initiatives. Where no cost-benefit analysis is undertaken, the Commission should give reasons why this is the case.

Recommendation 17 – Blanket Rulings and Orders

The Draft Report recommends that the Commission be allowed to issue blanket rulings and orders that provide exemptive relief, subject to a sunset clause. We agree with this recommendation and the suggestion that blanket orders and rulings should be used as an interim measure and that the substance of the relief should be incorporated into proposed rules and published for comment.

The ability to issue blanket orders and rulings as an interim measure would allow the Commission to respond to concerns of market participants quickly and at the same time provide the Commission with sufficient time to develop and promulgate comprehensive rules.

Recommendation 18 – Publication of Exemption Orders

We support this recommendation and are of the view that it would be extremely helpful if the Commission published exemption orders granted from the requirements of securities rules. We also urge the Commission to provide notice when an exemptive relief application has not been granted, and of the reasons for the refusal. On this latter point, we assume that the identity of the parties involved would not be disclosed in cases where confidentiality has been requested and granted.

Recommendation 21 – Registrant Involvement in Internet Offerings

We agree that from an investor protection perspective it would be prudent to retain the involvement of registrants in Internet offerings.

Recommendation 22 – Alternative Methods of Delivery of Documents

While we fully support a move toward electronic delivery of documents, the business reality is that clients want documents both electronically and in paper format. As a result, while we have incurred significant costs in building an electronic delivery infrastructure, we have not enjoyed the benefit of corresponding cost savings in reduced mailing costs to clients. In order to encourage clients to move away from paper copies, we submit that it should be permissible to pass on the costs of mailing to those clients who request hard copies of documents. We would then be in a position to pass on these cost savings to those clients that request electronic delivery. The current rules relating to electronic delivery in Canada do not contemplate this and consequently the advantages of electronic delivery have not been fully realized.

We are generally supportive of the recommendation to consider alternative models for delivery of documents by electronic means and a move towards an "access-equals-delivery" model. To the extent that certain documents are excluded from the "access – equals-delivery" model, we assume that issuers would still be permitted to rely on National Policy 11-201, which provides guidance regarding the electronic delivery of documents under securities laws. In addition, certain corporate statutes, including the *Bank Act* (Canada) ("the Bank Act"), impose requirements concerning the method of delivery of certain documents, which may include "access-equals-delivery" without further communications. We encourage harmonization of the delivery requirements in such statutes with any "access-equals-delivery" alternative model that is adopted.

Regulation of Market Participants

Recommendation 24 – Registration Requirements Related to Trading

The Draft Report recommends that the registration requirement related to trading be moved to a model requiring the person or company to be "in the business of trading", provided this change is adopted on a national basis. The Draft Report suggests that one of the purposes of the recommendation is to reduce the number of exemptions from the registration requirement.

We concur with this recommendation as long as exemptions that have historically been accorded to trust companies (for fully managed accounts) and to banks in recognition of the powers that are conferred on the business of banking under the Bank Act are maintained (such as the exemption for issuing guaranteed investment certificates and taking a pledge of securities from a control block). The Bank Act authorizes banks to engage in a broad array of activities in the ordinary course of conducting the business of banking. These activities are under the exclusive regulation of the federal government and it is important that securities laws provide for appropriate exemptions so that such activities are not inadvertently brought under the ambit of provincial securities regulation.

Recommendation 25 – Registration Requirements and "ancillary advice"

The Draft Report recommends that the current requirements in the Act to be registered either as an adviser or to trade in a security be retained. It further recommends that the Commission and the CSA carefully review the proficiency, experience and suitability requirements applicable to dealers and their employees to ensure that they are sufficiently rigorous to match the increasingly important role of "ancillary advice" delivered by dealers and their employees.

Before we can support this recommendation in principle, we require clarification as to what the proficiency requirements will be across the trading spectrum (i.e. from order execution to managed accounts) to ensure that the bar is set where we believe it is appropriate. Further, we assume that the additional proficiency, experience and suitability requirements would not apply to discount brokers and other dealers who do not provide advice and simply execute trades.

We are also of the view that the exemption for giving incidental advice should not be eliminated and should be available where the advice is truly incidental and we see no policy reason why this exemption should not be maintained. Accordingly, we recommend that clear guidance be given regarding what will amount to incidental advice and therefore come within the exemption, and what will entail more vigorous registration requirements.

Recommendation 27 – Universal Registration Requirements

We support the proposed amendment to the Act to eliminate the universal registration requirements. We believe that any benefits to investor protection are nominal at best and significantly outweighed by the system's complexity. Moreover, since the concept of universal registration has only been adopted in Ontario and Newfoundland to date, it is a significant impediment to regulatory harmonization.

Recommendation 32 – SROs

The Committee is of the view that there is considerable potential for conflict between an SRO's role as a trade association and its responsibilities as an SRO. It therefore recommends that the trade association and SRO functions be carried out by two separate bodies with distinct governance structures.

The current SRO model, of which the Investment Dealers Association is an example, provides the benefit of industry experience and direct involvement with market participants. While we are not necessarily opposed to splitting the trade association and regulatory functions of an SRO, we are concerned that this would undermine the primary premise behind the SRO model – that the SRO has industry specific knowledge and expertise that allows it to more effectively regulate. We believe that separating a SROs regulatory and trade association functions may be an impediment to simplifying our current regulatory structure. Alternatively, we suggest that the current SRO model could be maintained and that the Commission can address the potential for conflict through appropriate governance and effective oversight. If the decision is ultimately made to split the trade association and regulatory functions of an SRO, it may be preferable to return to a single regulator (e.g. the securities commissions) and a separate trade association.

Part 4: The Closed System and Secondary Markets

Recommendation 34 – Continuous Disclosure Requirements

We agree with the Committee's recommendation that the CSA harmonize basic continuous disclosure requirements so that they are uniform across Canada.

Recommendation 35 – A Statutory Civil Liability Regime for Continuous Disclosure

The Committee supports the CSA's proposal to create a statutory civil liability regime for continuous disclosure and urges the Government of Ontario to move forward as soon as possible to adopt such a regime by legislative amendment. The Committee also encourages the governments of the other CSA jurisdictions to adopt the regime.

We continue to have substantial concerns regarding a proposal for a limited statutory civil liability regime in connection with continuous disclosure in the secondary market. We have expressed our concerns to the CSA through the CBA, noting the need for more analysis concerning the increased personal liability of directors of public companies and

the need for uniformity. We are of the view that extensive industry consultation is still necessary and that this initiative should be part of a larger national initiative and should not be proceeded with by Ontario acting unilaterally.

Recommendation 36 – Prospectus Exemptions and the Closed System

We agree that the closed system is overly inclusive, inefficient and complex and cries out for simplification. We support the recommendation of the Committee to encourage the CSA to proceed with further reforms to the prospectus exemptions and the closed system, with greater convergence of requirements across the country and simplification as twin goals.

Recommendation 42 – "Material Information"

We agree that the timely disclosure requirements in the Act should not be amended to require disclosure of "material information" as opposed to a "material change," for the reasons noted by the Committee. Not only would it be more difficult for issuers to determine when material information would need to be disclosed, but as a practical matter it would also impose a significant burden on issuers.

Recommendation 43 – Standard for Materiality

We have concerns about the proposed recommendation to change the materiality standard under securities legislation to a "reasonable investor" standard, similar to the standard that is in place in the U.S. We believe that the current "market impact" test works well and is a more objective test than the reasonable investor test.

Recommendation 45 – Financial Statement Disclosure

The Draft Report recommends that the periods for filing annual financial statements be reduced to 90 days after the fiscal year end and that the time periods for filing interim financial statements be reduced to 45 days after the end of each quarter.

We have no objection to the recommendation to abbreviate the time periods for filing annual and quarterly financial statements, provided that this requirement is implemented concurrently with the proposal to allow issuers to deliver their financial statements to shareholders at a later date than the date they are filed.

Recommendation 46 – Review of Quarterly Financial Statements by External Auditor

We support the CBA's response to this recommendation and are of the view that the review of quarterly financial statements by the issuer's external auditor may be desirable, however, we do not believe that it should be mandatory. Any such requirement should not preclude the release of unaudited quarterly results prior to the completion of a review by the external auditor. In addition, it should be made clear that a review engagement report need not be attached to interim financial statements.

Recommendation 47 – Earnings Press Releases Filed on SEDAR

We do not agree with the recommendation to amend Ontario securities legislation to require that press releases containing financial or earnings information be filed on SEDAR. We submit that the CSA's approach in National Policy 51-201 – Disclosure Standards is more appropriate since it provides guidance to issuers on best practices, including their recommendation that earnings releases be filed through SEDAR.

Recommendation 48 – GAAP Exemption

We agree with the recommendation to remove the GAAP exemption available to banks in subsection 2(3) of the Regulation to the Act. We are in favour of transparency and of having only one source of GAAP in Canada, namely the CICA. Canadian banks that are Securities and Exchange Commission ("SEC") registrants cannot file financial statements with the SEC if the financial statements have exemptions from GAAP.

Part 5: Enhancing Fundamental Shareholder Rights

Recommendations 56 – 61 – Mutual Fund Governance

We submitted detailed comments to the CSA in response to the publication of Concept Proposal 81-402 on mutual fund governance. We are very supportive of a mandated fund governance regime, however, in order for the industry and unitholders to derive any concrete benefits from having a governance agency in place, we submit that it must be coupled with removal of the existing product regulation provisions, (including those pertaining to related parties), in National Instrument 81-102 and under applicable securities legislation. In our view, a mandated governance regime that does not provide relief from these provisions simply adds another layer of bureaucracy and regulation to an already highly regulated industry. We suggest that this is not in the interest of unitholders, who will ultimately bear the costs of further regulation.

Fund Manager Termination

We strongly disagree with the recommendation that the independent governance agency should have the right to terminate the mutual fund manager for cause.

We are of the view that the independent governance agency should not have the ability to terminate the fund manager under any circumstances. As the Committee correctly notes, this would amount to an expropriation of the property rights of the manager. Further, this recommendation fails to properly take into consideration the fact that there is an existing fiduciary relationship between the mutual fund manager and its unitholders. Dismissing the fund manager would not only subvert the wishes of unitholders who arguably chose to invest in the mutual fund based on its manager, but it could also leave a mutual fund without management. We maintain that if unitholders lose confidence in the manager they can always "vote with their feet " and leave the fund. Where there is an unresolved

dispute between the fund manager and the governance agency, unitholders should be entitled to full disclosure of any such unresolved dispute and can act accordingly.

Recruiting Qualified Mutual Fund Directors

As the Draft Report indicates, there are currently in excess of 1,700 mutual funds and 70 mutual fund management companies in Canada. Under the circumstances, finding sufficient suitably qualified people to serve as directors of an independent governance agency could prove challenging.

We agree with the recommendation that the process by which potential directors of mutual fund governance agencies are identified and nominated should be expanded so as to include a broader range of potential directors. Mutual funds and their nominating committees should expand the pool of talent they will consider to include individuals below the ranks of CEOs, as well as retired professionals and members from non-profit organizations.

Regardless of the available talent pool, we believe that the prospect of unlimited liability will be a significant deterrent to the recruitment of appropriately qualified individuals and we therefore recommend that director liability be appropriately capped.

We also agree that a majority of the governance agency members should be independent of the management company. Having said that, we are also of the view that in order to be effective in its role, the governance agency should also be comprised of certain members who possess detailed knowledge of the fund manager's business. We assume that any test for determining a member's independence should be reasonable and intended to address real conflicts of interest.

Governance Agency Member Compensation

We disagree with the recommendation that one of the characteristics that a mutual fund governance agency should have is the right to set its own compensation. We do not believe that governance agency members should set their own compensation. In our opinion, it is entirely appropriate for the mutual fund manager to set the compensation of governance agency members, since the manager is responsible for the funds' management expense ratios and other costs that will be charged to the funds. Our experience with the Royal Mutual Funds" Board of Governors suggests that the independence of the governance agency members will not be compromised if the mutual fund manager sets the compensation of the agency members directly. We believe that given the relatively small and specialized talent pool available for governance agency members, market forces will quickly establish appropriate benchmark compensation.

We are of the view, however, that the independence of the governance agency members could be compromised if the fund manager paid the compensation directly, instead of the funds. Since the governance agency is in place to protect unitholders and represent their

interests, it is appropriate that compensation of governance agency members be a fund expense that will be borne by unitholders.

The Right to Retain Counsel and Independent Advisers

The Draft Report recommends that the independent mutual fund governance agency should have the right to retain counsel, independent of counsel of the fund manager, as well as the right to hire other independent advisers. We submit that it is inevitable that governance agency members will seek to retain multiple independent experts, such as accountants and lawyers, in view of the prospect of unlimited liability. It should be noted that these costs will not be insignificant and will ultimately be borne by unitholders.

Capping the Number of Funds for which a Governance Agency is Responsible

The Draft Report recommends a cap on the number of funds for which any one independent governance agency is responsible. We concede that there may be a practical limit to the number of funds that one governance agency can effectively oversee. The primary factor in determining this limit will be the roles and responsibilities of members of the governance agency. Until such roles and responsibilities are clarified, it will be very difficult to assess in any definitive way what this limit will be. In addition, the potential liability to which agency members are exposed may also be a factor that influences this limit.

Subject to the foregoing, we are of the strong view that mutual funds within the same fund family or funds that are managed by the same mutual fund manager would only need one governance agency to oversee all related mutual funds.

Review of Manager's Performance

One of the Committee's recommendations is that the independent governance agency should review the performance of the manager on a regular basis.

We submit that the role of a governance agency should be to provide general oversight of the mutual fund manager's actions in managing its mutual funds to ensure that it acts in the best interests of unitholders and not to micro-manage the day-to-day management of the mutual funds. The independent governance agency should focus on areas where its members can add value to the unitholders they represent, such as ensuring that management is properly qualified, has access to sufficient capital and has appropriate processes and controls in place with respect to the funds' investment objectives and strategies and regulatory reporting requirements.

Functions of a Governance Body

One of the listed recommended functions of a governance agency outlined in the Draft Report is "ensuring compliance with investment goals and strategies".

We believe that it is inappropriate to have the governance agency ensure that the mutual funds are managed according to their stated investment objectives and strategies. In our view, there is nothing more fundamental to the manager's role than ensuring that funds are operated in accordance with their objectives and strategies. Managers should report to the governance agency on their processes and controls to ensure compliance with mandates and any action required where there has been a deviation from the funds' objectives and strategies.

Recommendation 67 – Establishment of a National Complaint-Handling System

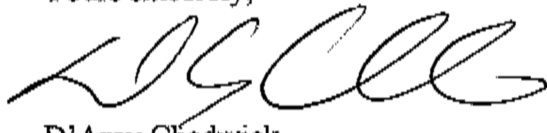
The Draft Report recommends the establishment of a national complaint-handling system in which participation by financial service providers is mandatory.

We are of the view that the Committee's recommendations in this respect are redundant and note that the Draft Report references the creation of, and indicates its general support for, the Financial Services OmbudsNetwork ("FSON"). FSON provides a "single window" for consumers of financial services to access the industry's complaint-handling and dispute resolution mechanisms. From our perspective, FSON generally meets the criteria that the Draft Report indicates should be found in a complaint-handling system. We therefore do not see the need for the establishment of another complaint-handling system.

Concluding Remarks

We would be pleased to discuss our submission further with the Committee and encourage you to contact D'Arcy Chadwick, Assistant General Counsel, at (416) 955-3592 (darcy.chadwick@rbc.com), or Lori Lalonde, Senior Counsel, at (416) 955-7826 (lori.lalonde@rbc.com) in this regard.

Yours sincerely,



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