Via email

September 14, 2012

John Stevenson, Secretary
Ontario Securities Commission
20 Queen Street West, 19th Floor, Box 55
Toronto, ON M5H 3S8

and

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

Dear Mr. Stevenson and Ms. Beaudoin,

Re: Second Request for Comment – Proposed Amendments to National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* ("NI 31-103") – Cost Disclosure, Performance Reporting and Client Statements

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.; and Phillips, Hager & North Investment Funds Ltd. We are writing in response to the Canadian Securities Administrators' ("CSA") second request for comment on the proposed amendments to NI 31-103 regarding cost disclosure, performance reporting and client statements ("Proposal") published on June 14, 2012 ("Notice").

We are pleased to note that the Proposal contains certain welcome revisions to the June 2011 proposal which address a number of industry concerns. Specifically, this includes the proposed amendments to: exempt non-individual permitted clients from various requirements; require that investment fund managers provide dealers and advisers with the information necessary for them to comply with certain disclosure requirements; mandate the disclosure of the "book cost" instead of "original cost" of securities on client statements; and clarify that the all-in fee charged by registered firms is the "operating charge".

The fact that CSA would consider the applicability of the Proposal to order execution only accounts when the Investment Industry Regulatory Organization of Canada ("IIROC") takes steps to materially harmonize its rules with the amended NI 31-103 is also a positive development. On a similar note, IIROC's approved Client Relationship Model related performance reporting requirements specifically exclude the accounts of "institutional customers", as defined under IIROC rules. While the Proposal provides certain exemptions for non-individual permitted clients, in practice, the differences in the definitions of "permitted clients" and "institutional customers" would pose significant challenges for investment dealers in identifying the applicable requirements for any one client. In this regard, we support IIROC's approach and continue to suggest that accounts of clients that meet the definition of "institutional customer" under IIROC rules be exempted from the Proposal or, alternatively, the exemptions should be granted to IIROC members.

We have participated in the industry working groups organized by the Investment Industry Association of Canada ("IIAC") and Investment Funds Institute of Canada ("IFIC"); we contributed to and support the comments in their submissions. That being said, we would like to provide further comments on certain issues where we have significant concerns:

1. Client Statements

(i) Reporting on client name securities

The Proposal requires that client statements and investment performance reports include reporting on certain securities owned by a client that is held by a party other than the dealer or adviser ("client name securities"). While it is a common practice for mutual fund dealers and portfolio managers, investment dealers do not usually include client name securities in their account statements. Our comments in this section will focus on issues primarily related to investment dealers.

For the reasons outlined below, we do not support the proposed mandatory inclusion of client name securities on client statements and investment performance reports. It appears that the anticipated costs to investment dealers of complying with this requirement would outweigh the potential benefits to clients:

- An investment dealer's client name securities primarily consist of assets held at fund companies. These clients receive client statements directly from the fund companies, whereas investment dealers would be required to build complex systems in order to capture information relating to client name securities on client statements.
- Clients may find it confusing to have reporting on client name securities included in separate clients statements provided by both the investment dealer and fund company, especially if there are differences in the content and/or presentation of the reporting.
- Where a client statement includes a section on client name securities, clients may be misled that the client name securities are also covered under an investor protection fund. IIAC's submission points out that IIROC member firms are required to include the official Canadian Investor Protection Fund ("CIPF") symbol and an explanatory statement on the client statements to warrant that the securities presented on the client statement are covered by CIPF. As client name securities are not covered by CIPF, their inclusion on an IIROC firm's client statements would result in clients incorrectly inferring there is CIPF coverage for those securities. Even if firms take additional steps by including an explanatory or legal disclosure note, client may still be confused.
- Currently, investment dealers do not have all the information required to provide accurate and comprehensive reporting on client name securities. Though fund companies provide some information to investment dealers regarding client name securities in the form of a Position Reconciliation File ("PS file"), additional information would be required from fund companies to meet the requirements under section 14.14(6.2). In addition, only fund companies who offer funds through FundSERV provide investment dealers with the PS file; fund companies who do not offer their funds through FundSERV do not provide this information.
- Generally, client name securities are not a significant portion of a client's holdings, hence the requirement may not result in significant benefit to clients.

Exemptions

In the event that registered firms would be required to report on client name securities as drafted, it should be noted that there may be potential timing and coordination issues as registered firms would need to rely on information from external sources in order to produce such reporting. By way of illustration, consider a situation where both a dealer and a fund company are to provide a client with client statements as at July 31st. FundSERV standards currently mandate delivery of the PS file by 11:59 pm on month end +3 days; this can be shortened to +2 days, but not all fund companies may be able to meet this timeline. The dealer would require the necessary information on the first or second calendar day after the last business day of the month in order to arrange for the client name securities positions to be reflected on its month end client statements. If the necessary information is not received on time, the

dealer would be left with two inadequate options: either to reflect July month end client name account balances on its August month end client statement, or to delay standard client statement production. Hence, we submit that the proposed requirement to report on client name securities should be subject to registered firms receiving information necessary to comply with the applicable provisions from the relevant fund companies or other persons in a timely manner.

To avoid duplication in client reporting and client confusion, where another person (including third party, such as a custodian or issuer) is providing reporting on client name securities to clients directly, registered firms should be exempted from this requirement.

Further, the CSA's request for comment on proposed amendments to NI 31-103 published on June 25, 2010 notes that if client name securities were required in account statements, the CSA would expect to exempt client name securities held in certificate form by the client and in Delivery against Payment ("DAP")/Receipt against Payment ("RAP") accounts. As per RBC's submission dated September 30, 2010, we continue to support this approach:

- With respect to client name securities held in certificate form by the client, in practice, registered firms would not generally know whether a client still has physical possession of a certificate unless informed by the client, and clients do not have any obligations to do so. When applying the test under proposed section 14.14(6.1), we note that registered firms would not have trading authority over the security in question nor receive any relevant dividends. If proposed subsection 14.14(6.3)(b)(iv) would be adopted as drafted, we would appreciate if the CSA could provide examples where a registered firm would be required to provide reporting under proposed section 14.14(6.2) for a security held by client in certificate form.
- For DAP/RAP accounts, providing book cost information for positions in DAP/RAP accounts would be challenging since such information may not be available to registered firms. We seek confirmation that DAP/RAP accounts are exempted from section 14.14.

Transition Period

Should the proposed requirement to include client name securities on client statements and investment performance reports be implemented, registered firms would be required to invest significant time and costs to implement the changes. We anticipate that registered firms would need to develop complex systems to be able to capture information relating to client name securities on client statements and investment performance reports; find a source to obtain data on the client name securities held by the client; and identify all clients who hold client name securities. Consequently, we request that the transition period for section 14.14 be extended from two years to a minimum of three years. In addition, we support IIAC's recommendation that the requirement be implemented on a going forward basis only, due to concerns regarding the accuracy of information for historical transactions or legacy accounts.

(ii) Provision of client statements

Under section 14.14, registered firms are only required to provide client statements to "clients". We suggest that it should be clarified that registered firms are not required to provide clients with client statements where the client relationship has ended. In our view, a client's relationship with a registered firm has ended when the client closes their account with the firm or the account is inactive for a certain period and the firm is unable to contact the client in accordance with unclaimed property legislation.

(iii) Transaction Reporting

Proposed subsection 14.14(5)(g) requires that, if the transaction was a purchase for the client, the client statement identify the party that held the security when the transaction was completed and how it was held. Notwithstanding our comments under section 1(i) of this letter, we seek clarification on whether this proposed requirement applies to both nominee and client name securities; if so, how this information should be presented.

(iv) Cost of Securities

Client statements would be required to include the book cost of each security position; where the information required to calculate the book cost of a position is unavailable, registered firms may elect to substitute market value information as at a certain point in time as the book cost going forward. We find that the proposed requirement to default to market value where a book cost is not known may be problematic and would not further the objective of providing clients with an accurate view of capital appreciation or depreciation of each security position. In the case where book cost information is not available, we suggest that registered firms should be provided with an option to suppress or create a blank for book cost where market value has been applied to a security. This would highlight to the client that the correct book cost has not been provided to the registered firm and action needs to be undertaken by both the client and registered firm to update the book cost.

The proposed provisions also require that, for each security position for which the registered firm does not reasonably believe it can determine a reliable book cost, a disclosure of that fact be included in the client statements. We seek confirmation that a general notification could be included in the footnote of all client statements.

2. Fixed-Income Transactions

(i) Definition of "Fixed income security"

The Proposal includes proposed disclosure of fixed income commissions on trade confirmations and reports on charges. From the perspective of investment dealers, IIROC's rule amendments mandating fixed income security yield disclosure and remuneration disclosure statement to retail clients on trade confirmations have just become effective in September 2012. As clients are now provided with such disclosures and investment dealers have recently completed operational changes to implement these requirements, we recommend that the proposed fixed income related disclosures should take into account the scope of IIROC rules. In this regard, we agree with IIAC's suggestion that the Proposal should provide a definition of "fixed income security" that is consistent with IIROC's requirements and clarify the types of securities that would not be considered as a "fixed income security". We would also appreciate confirmation as to whether primary market transactions are excluded, as well as guidance on how step-up fixed income securities should be treated under the rules.

(ii) Disclosure of annual yield of fixed income security

Proposed subsection 14.12(b.1) provides that trade confirmation must include, in the case of a purchase of a fixed income security, the security's annual yield. It should be noted that the proposed requirement contrasts with the above-mentioned IIROC rule, which requires disclosure of the fixed income security's yield to maturity. We seek guidance on whether the annual yield could be calculated in a manner consistent with market conventions for the security traded (which is in line with approach taken by IIROC).

(iii) Disclosure of the amount of fixed-income commissions

The CSA is inviting comments on whether it is feasible and appropriate to mandate the disclosure of all of the compensation and/or income earned by registered firms from fixed-income transactions; this would include disclosure of commissions earned by dealing representatives as well as profits earned by dealers on the desk spread and through any other means.

We support regulatory initiatives that aim to offer retail clients transparency in fixed-income transactions. However, any such information to be provided to retail clients should be reliable in order to avoid client confusion and misunderstanding regarding the fixed income world. In 2009 and 2010, IIROC staff considered the possibility of requiring the disclosure to retail clients of the gross amount of mark-up or mark-downs, commissions and other service charges applied by IIROC firms to over-the-counter fixed income security transactions. As concluded by IIROC, we agree that "there are structural impediments to determining the actual, dollar amount of remuneration received by [an IIROC firm] with respect to a

transaction involving an OTC debt security." By way of example, the calculations to quantify any mark-up/mark-down at the wholesale level on a trade-by-trade basis would need to account for the length of time each bond has been warehoused in inventory (which could be anywhere from seconds, to months or years); the cost of carry/funding costs associated with holding positions; the borrowing costs associated with short selling to facilitate client transactions; and the potential market movements. In addition, most institutional bond trades are not outright for cash and have more than one leg associated with the transaction, such as hedges or switch/spread trades. Due to the challenges in arriving at an accurate amount of "all of the compensation and/or income earned by registered firms", we are of the view that the proposition would neither be feasible nor appropriate as it is not in the interest of clients to receive inaccurate, unreliable information.

Likewise, disclosure of fixed income related commissions paid to dealing representatives only may also be misleading to retail clients. When a registered firm that acts for retail clients or a retail division of an integrated registered firm conducts fixed income transactions for its client, it sources fixed income securities for the client and charges a commission on the wholesale marked-up/marked-down price at which it acquired the security (for the purposes of this letter, "Gross Retail Commission"). The dealing representative's compensation would be allocated from the Gross Retail Commission.

To enhance transparency in fixed income transactions, we suggest that trade confirmations and report on charges should disclose the Gross Retail Commission. For the reasons outlined above, Gross Retail Commission should exclude the mark-up/mark-down at the wholesale level and should be defined in NI 31-103 or explained in the Companion Policy. The disclosure of the Gross Retail Commission, as opposed to the proposed disclosure of compensation paid to dealing representatives, is preferable as it is consistent with the commissions reported on trade confirmations for other products (such as listed equity, options). Also, the Gross Retail Commission is a readily available information, whereas service providers do not currently support the disclosure of compensation of dealing representative; to extract this amount from the Gross Retail Commission would be operationally overwhelming and may have an adverse affect on existing service delivery commitments pertaining to the delivery of electronic and paper trade confirms. Should this approach be adopted, we note that the notifications under proposed subsections 14.12(1)(c.1) and (c.2) may no longer be applicable.

(iv) Notification concerning fixed-income related compensation

If the notifications under proposed subsection 14.12(1)(c.1) and (c.2) would still apply, we suggest that the notifications should be allowed to be combined into one notification. This is to address circumstance where a registered firm's system for producing trade confirmations does not recognize whether remuneration is made from a buy or sell transaction and minimize the possibility of disclosing incorrect notification to clients. In line with the notification under proposed subsection 14.15(1)(e), the notification could be revised to read as follows:

> *"Dealer firm compensation may have been included in the price of this security (in the case of a purchase) or deducted from the price of this security (in the case of a sale). These amounts were in addition to any commissions this trade confirmation shows was paid to individual dealing representatives."*

3. Investment Performance Report - Percentage Return Calculation Method

The CSA is inviting comments on the benefits and constraints of the proposal to mandate the use of dollar-weighted method in calculating the percentage return on a client's account or portfolio. To begin with, we are concerned that the proposal creates a localized regulation that is contradictory to the CFA Global Investment Performance Standards that have been used by registered firms for the past 20 years in lieu of regulatory standards. Since most registered firms have historically been providing time weighted rate of returns to their clients, it is likely that clients will lose the historical performance that has been provided. Also, it is anticipated that it may not be possible for registered firms to go back and restate historic returns based on a dollar-weighted method; even if it is possible, it would be extremely costly and difficult.

The Notice explains that dollar-weighted method is mandated because it most accurately tells a client how an account has performed. We note that as part of the proposed investment performance report, registered firms would be required to provide the opening market value of an account, plus deposits into the account, less withdrawals from the account (at market value) to determine the change in the market value of their account over the reporting period. Compared with the dollar-weighted rate of return, we believe this is a more meaningful representation for the gains and losses of the account for clients.

Given that clients would have the means of evaluating the actual return of their accounts, the annualized total percentage return information should be used as a supplementary indicator to show how their accounts are managed. However, a dollar-weighted rated of return would offer minimal value to clients in this case as it cannot be compared to industry standard benchmarks. In contrast, a time-weighted rate of return would allow the client to view a fair representation of both questions: What was my gain/loss? How well has my account been managed?

Although the Proposal allows registered firms to provide time-weighted rate of returns in addition to mandatory dollar-weighted rate of return, the Notice has correctly pointed out the two calculation methods can produce significantly different results. Providing clients with both dollar-weighted and time-weighted rate of return would cause client confusion. To link the time-weighted rate of return with dollar-weighted rate of return would also be inappropriate as they are two separate and distinct performance metrics.

Consistent with IIAC and IFIC's recommendations, we are of the view that the Proposal should not impose one method of calculating percentage return. Mandating a uniform performance reporting methodology across all types of registered firms disregards the fact that performance reporting should serve the varying needs of investors. Instead, registered firms should have the option of using a recognized time-weighted or dollar-weighted calculation method as appropriate. Should it be determined that one methodology must be mandated, based on the above considerations, the time-weighted method would be more suitable as it would provide clients with more meaningful information to assess their investments.

4. Trade Confirmation

Proposed subsection 14.12(1)(c) provides that trade confirmations must disclose the transaction charge, deferred sales charge or other charge in respect of the transaction. To assist registered firms in determining the types of charges that should be disclosed under this proposed provision, we request further guidance on the items that would be interpreted as "transaction charge" and "other charge". For greater clarity, please confirm that third party payments to a registered firm or any of its registered individuals in relation to a transaction (such as spreads from new issues, back-end commissions paid from fund managers, GIC related fees) are not required to be reported on trade confirmations.

To comply with the proposed requirement to disclose the "total amount of all charges in respect of the transaction" on trade confirmations, registered firms would need to rely on data from third party service providers. It is our understanding that currently, not all service providers support the summation of charges.

Due to the significance of the proposed changes being made to the existing trade confirmation requirements, we request that a transition period of a minimum of two years be provided to subsections 14.12(1)(b.1), (c), (c.1) and (c.2) to allow registered firms and third party service providers (as applicable) to develop the necessary system changes to implement these enhanced disclosures.

5. Information from Investment Fund Managers

With respect to proposed subsection 14.1(2), we share the same concerns described by IFIC in their comment letter dated August 29, 2012 regarding the proposed disclosure of trailing commissions. We are also concerned whether investment fund managers would always be able to provide dealers or advisors with information relating to charges deducted from the net asset value of securities upon their redemption

and trailing commissions in timely manner. As the ability of dealers and advisers to comply with proposed subsections 14.12(1)(c) and 14.15(1)(h) depends on the coordination with investment fund managers, we would appreciate clarification that the proposed requirements are subject to the registered firms receiving the necessary information from investment fund managers in a timely manner.

6. Foreign Exchange Spreads

IIAC's submission highlights that the proposed requirement to disclose the dollar amount of foreign-exchange spread as a transaction charge is an example of a disclosure that provides minimal value to the client, while being extremely costly and complicated to registered firms from a technical perspective to determine an accurate amount. Instead of disclosing the dollar amount of foreign-exchange spread, we support IIAC's recommendation that registered firms be required to provide a general notification in all trade confirmations and applicable client reports that the registered firms may have received remuneration from a foreign exchange transaction.

7. Determining market value

Proposed subsection 14.11.1(2) provides that if the market value of a security is determined in accordance with a valuation policy, a prescribed notification be included in the client statements. Currently, registered firms and service providers generally do not track nor have the means to track in their systems whether the market value of a security is determined using a valuation policy. Hence, to comply with this requirement would require additional system build for both registered firms and service providers, while the benefits to clients are not significant. With the goal of providing clients with more understanding of the pricing of their securities, we suggest that a more general notification could be included in the footnote of client statements:

"Where there is no active market for a security, the value of the security is estimated."

If a registered firm cannot reasonably determine a reliable market value for a security, proposed subsection 14.11.1(3) requires that the market value of the security be reported in client reports as not determinable. For client statements, we seek guidance on how this information should be expressed; for example should such security position be assigned a value of zero; if so, is additional notification in the footnote of the client statements required? For investment performance reports, we seek confirmation that the required explanation to clients under subsection 14.17(7) may be included in the report as a footnote.

8. Consolidated Reports

Proposed subsections 14.15(2) and 14.16(3) allow registered firms to provide a consolidated report on charges and a consolidated investment performance report for more than one of a client's accounts instead of account-by-account reports, if the client consents in writing. The proposed amendments recognize that in many cases, the accounts of one client are components of that client's portfolio and providing clients with such reporting at the account level may cause confusion to the clients. As it is anticipated that a significant number of clients would be in favour of receiving consolidated reports as opposed to account-by-account reports, we suggest that the CSA could introduce ways to facilitate smooth transitions for both clients and the registered firms. Specifically, we recommend that the CSA could introduce flexibility in the way that client consent is evidenced by allowing registered firms to obtain negative consent or other means of client acknowledgement.

9. Point of Sale Disclosure of Charges

Proposed section 14.2.1 is mandating point of sale disclosure of charges relating to all investment products for non-managed accounts. As noted in IFIC's submission, there is significant overlap with the CSA's Point of Sale Framework for mutual funds, which requires the disclosure of mutual fund costs, charges and commissions to be included in Fund Facts. We support IFIC's view that the proposed point of sale disclosure of charges for mutual funds should be effected through amendments to National Instrument 81-101 *Mutual Fund Prospectus Disclosure* only.

10. Implementation of the Proposal; Competing Regulatory Priorities

The securities industry is embracing a number of significant regulatory developments that are or will be effective shortly; to name a few, these include IIROC Client Relationship Model (in particular, Relationship Disclosure, Enhanced Suitability requirements), CSA's Point of Sale Framework for mutual funds (preparation and delivery of Fund Facts), exchange traded funds prospectus offering and the U.S. *Foreign Account Tax Compliance Act*.

We support IIAC's conclusion that the proposed transition periods for a number of aspects of this Proposal must be revisited as they are likely unattainable. The CSA must recognize that the implementation of the proposed requirements would require registered firms to undergo significant project and budget planning while managing existing competing priorities, and would require registered firms, fund companies and/or third party service providers to coordinate and agree on multiple infrastructures to facilitate the necessary information gathering and sharing process. To this end, we strongly encourage the CSA to consider the phased implementation timeline proposed by IIAC.

We appreciate the opportunity to provide comments on this important initiative and welcome the opportunity to discuss the foregoing with you in further detail. If you have any questions or require further information, please do not hesitate to contact the undersigned.

Sincerely,

"David Agnew"

David Agnew
Chief Executive Officer
RBC Dominion Securities Inc.

"Mark Neill"

Mark Neill
President
Phillips, Hager & North Investment Funds Ltd.

"Wayne Bossert"

Wayne Bossert
President and Chief Executive Officer
Royal Mutual Funds Inc.

cc. Russell Purre, Chief Compliance Officer, RBC Dominion Securities Inc. (Retail)
Shaine Pollock, Chief Compliance Officer, RBC Dominion Securities Inc. (Institutional)
Greg Nowakowski, Chief Compliance Officer, RBC Directing Investing Inc.
Ann David, Chief Compliance Officer, Royal Mutual Funds Inc.
Larry Neilsen, Chief Compliance Officer, RBC Global Asset Management Inc.; Phillips, Hager & North Investment Funds Ltd.
Martha Rafuse, Chief Compliance Officer, RBC Phillips, Hager & North Investment Counsel Inc.