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

Attn: The Secretary
Ontario Securities Commission
E-mail: comments@osc.gov.on.ca

Dear Sirs:

Reference: CSA Discussion Paper and RFC 81-407 Mutual Fund Fees

I would first like to thank the CSA for studying issues related to mutual fund fees in the Canadian financial industry, and for the opportunity for the public to comment.

As background, I am a retail investor with no professional training in the financial industry, nor any beneficial interest in any individuals or firms in the financial industry. I began investing in a significant way circa 1990 and went through a series of Investment Advisors with full service brokerage firms over the next 10-12 years, eventually becoming dissatisfied with each one in turn. As the Internet took off, online information became more readily available, and discount brokerages started to appear, I eventually educated myself through online financially oriented websites and discussion forums to migrate methodically to 100% DIY investing with online discount brokerage(s).

My comments herein are primarily based on my experiences with investment dealers (full service brokerages), online/discount brokerages, and anecdotal information from fellow investors, family and friends.

Investor Understanding of Fund Costs and Advisor Compensation

While the prospectus of each mutual fund discloses (MER) fund costs and the distribution of these costs, only the most patient and courageous investor dares to wade into primarily pages and pages of legal and regulatory boilerplate. In other words, few investors read them and that is likely to become more prevalent as the pace of life increases and younger investors operate in a world of sound bites. The Fund Facts sheet has become the 'go to' tool for most investors (if they even go that far) and it does not yet disclose the breakdown and allocation of the cost components. At best, most Fund Facts sheets now say what the

MER is for that particular series of fund and that there are trailing commissions/fees (if they exist).

I never had an Investment Advisor voluntarily advise me to read the prospectus and/or Fund Facts sheet before committing to a mutual fund investment. In addition, I never had an Advisor offer to disclose how s/he gets paid in any mutual fund purchase. The few times I asked, I was typically brushed off by comments such as 'why do you care as it is not costing you anything'. None of my account statements have ever disclosed inherent costs, nor how the Advisor was compensated for mutual funds.

As a minimum, the mandatory disclosure of fund costs and the allocations of same in the Fund Facts sheet (including compensation to the Advisor) would go part way to full disclosure and transparency. It would be no extra effort for the mutual fund manufacturer to put this cost allocation data on the Fund Facts sheet for each series of funds.

Further, it is not unreasonable (as part of Advisor services rendered) to insist on mandatory disclosure of Advisor compensation on investor account statements summarizing the revenue stream that is accruing to the investment dealer (and/or the Advisor). Only then can investors have a meaningful discussion with his/her Advisor on the value received for that revenue stream. It may additionally clear out the 'less than forthright' Advisors and improve the image of the industry.

These two things would likely have the most positive effect for investor advocacy of anything presented in the discussion paper. That information may also act as a catalyst to resolve some of the other issues described in the discussion paper.

<u>Potential Conflicts of Interest</u>
With respect to automatic conversion potential conflict of interest, no such conversion should be permitted without the investor's consent. This issue would/could also be solved through transparency and disclosure of advisor compensation. In that case though, the pressure/burden would be on the investor to question the proposed switch, or any attempt by the advisor to steer the investor into a new DSC fund once the DSC schedule had matured. However, putting the onus on the investor may not result in the intended results since many retail investors feel intimidated by their investment advisors, i.e. a reluctance to question their advisor's recommendations since 'advisors know it all'.

That said, if advisor compensation was fully transparent and disclosed in enough detail, there would likely be less incentive for an advisor to exercise conflicts of interest, and less reason for an investor to suspect conflicts of interest.

<u>Alignment of Advisor Compensation and Services</u>
From my viewpoint, there is no logical reason for trailing commissions to vary on the basis of type of fund, e.g. equity, balanced, fixed income. If it does not take the investor any material difference in time and effort to research and make a decision on any one of those types of funds, it surely cannot take the advisor any difference in time or effort to make a recommendation either. Mandating no difference would eliminate any incentives for an advisor to favour one type of fund over the over, leaving the sole deciding factor being the investor's risk tolerance and asset allocation needs.

<u>Discount broker/online Issues</u>
I will restrict my comments to online discount brokerages since I have no personal experience with direct sellers. Investors, like myself, who became disenchanted with full

service brokerages have educated themselves sufficiently to migrate partially, or completely, to DIY investing, primarily with discount brokerages, or in some cases (usually those with smaller accounts) e-series funds. In essence, DIYers have become their own advisors, either completely solo, or in combination with financial advice provided by, for example, a Fee Only Planner.

More investors are becoming DIYers as evidenced by the number of people that continue to join and participate in financially based Discussion Forums such as http://www.financialwebring.org/forum/index.php and its companion financial Wiki http://www.finiki.org/wiki/Main_Page . That particular forum has been one of my primary 'go to' places for generally trustworthy financial information since its inception in 2005.

One of, if not the major, pet peeves by the DIYers is the inability of investors, who are de facto their own advisors, to access F series mutual funds through discount brokerages. Discount brokerages, by definition are order takers only, i.e. they do not provide financial advice. Why then do they not provide investor (self-advisors) access to the same F series mutual funds (without trailer fees) they provide to licensed Financial Advisors? At least one intrepid discount brokerage did provide, for a short period of time pre-2000, investor access to F series funds, but that was shut down. It is rumoured the mutual fund companies threatened to pull the availability of their funds from the discount brokerage(s) to shut that concept down, either on their own initiative, or under pressure from the full service industry.

If this is true, the mutual fund manufacturers may be short sighted. They will continue to lose potential sales to ETFs, their new competition. While the number of ETFs has gotten out of hand with a proliferation of slice and dice products, the primary index ETFs typically have MERs well under 50 basis points, sometimes in the 10-15 bp range making them the 'go to' choice of DIY investors. Sharp investors learn that costs matter as evidenced by studies that show most actively managed mutual funds, especially Series A and B with their comparatively high MERs, cannot beat their respective market indices on a longer term basis. So what are the alternatives?

DIY investors recognize there are transaction and custodial costs associated with mutual funds, and the distribution channels need to cover costs and make a profit. There are really two main choices in this regard: 1) Mandate the availability of zero trailer F series mutual funds and DIY investors accept a sales/purchase commission to the investor as they currently do for stocks and ETFs, or 2) create a new series of mutual funds with a small administrative operating fee of perhaps 10-15 bp p.a. of the holding's market value to cover transactional and custodial costs and make a small profit.

Conclusion

The Canadian mutual fund industry needs to change significantly if it wishes to maintain its share of the business. It needs to eradicate the inequities and potential conflicts of interest in the system that the CSA discussion paper has highlighted, but if nothing else, the cloak must be removed on fees and advisor compensation. Informed investors will otherwise continue to be suspicious and go elsewhere. Perception is reality until proven otherwise. Thank you for the opportunity to comment.

Yours truly,

W S Kubasek

Wayne S. Kubasek, P. Eng.