Capital International
Asset Management (Canada), Inc.
BCE Place, Bay [illegible] Tower
181 Bay Street [illegible]
Toronto, ON M[illegible]

(800) 42[illegible]

June 5, 2002

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

Denise Brousseau, Secretary
Commission des valeurs mobilieres du Quebec
800 Victoria Square, Stock Exchange Tower
P.O. Box 246, 22nd Floor
Montreal, Quebec H4Z 1G3

<u>Re: Concept Proposal 81-402</u>

Capital International Asset Management (Canada), Inc. ("CIAMC") is pleased to have this opportunity to provide comments on Concept Proposal 81-402 (the "Proposal") of the Canadian Securities Administrators ("CSA"). For your information, CIAMC is a registered investment adviser in Ontario and British Columbia, and serves as the investment adviser to the Capital International mutual funds registered throughout Canada. CIAMC is part of The Capital Group Companies organization, a global investment management firm, established in 1931. The Capital Group Companies organization, through its separate investment management subsidiaries, managed in excess of $900 billion as of March 31, 2002.

CIAMC's sister company, Capital Research and Management Company ("CRMC"), serves as the investment adviser to The American Funds Group of mutual funds in the United States. Total assets in the American Funds Group of funds were in excess of $580 billion as of March 31, 2002. CRMC has had a great deal of experience with mutual fund governance in the U.S. under the Investment Company Act of 1940 (the "1940 Act"). While we recognize that the governance standards under the 1940 Act are different than those proffered under the Proposal, we nonetheless believe that they may provide a valuable reference point in considering the potential benefits and burdens associated with a fund governance agency.

We have chosen to not to address all of the CSA's points of inquiry in the Proposal, as we think that the most prominent point is the CSA's flawed cost benefit analysis which undermines the entire set of recommendations. In sum, we believe that any fund governance regime or standards that might be established should ultimately be designed to (1) serve the interests of the investing public, and (2) strengthen confidence in the Canadian financial markets. However, we believe any such regime or standards must also reflect a reasonable balance between increased investor protection on the one hand, and the costs and complexity of administration on the other. While many of the specific points in the Proposal are laudable, given that the proposed capital requirements and extent of the governance requirements will impose significant costs, we believe that there may be better, more cost effective ways to achieve these two primary goals.

As further discussed below, based on our organization's experience with fund governance in the U.S., we believe that the Proposal materially underestimates the true cost and commitment required to maintain a fund governance agency. These costs ultimately will be borne by fund investors, and thus, we would strongly urge that alternative approaches be pursued so that a more cost effective solution will be available for the funds and their unitholder.

The Proposal states that the OSC's chief economist has estimated the costs of creating and operating a governance agency will represent no more than 0.016 percent of total industry assets under management. Based on that underlying assumption, the Proposal concludes that the proposed fund governance regime would not place an undue burden on mutual fund managers or mutual funds, and thus the costs of the proposals will be more than offset by the benefits.

However, we note from the "Explanation of our cost analysis" in the accompanying Concept Proposal Research Report, that in deriving the 0.016 percent figure the CSA used a survey of historic costs from fund groups already using governance agencies. We believe that the survey greatly understates the true costs, as explained further below, especially given that these historic costs would not reflect the new and expanded duties and responsibilities that the fund directors would have under the Proposal. Also, the method used does not reflect the cost of staff internal to the mutual fund manager to organize and support the governance agency, which in our case, at least in the U.S., is not insignificant (see further below). Additionally, the estimate used for director's liability insurance would not necessarily reflect (1) providing coverage for unlimited director liability under the Proposal (i.e., while it is our understanding that firms will not be able to obtain insurance for unlimited liability, they will most likely need to increase their existing policy amounts if that provision is effected); or (2) increasing coverage in the current unfavorable insurance market. Furthermore, the average cost cited for director compensation would not likely be realistic going forward in an environment where demand for qualified directors skyrockets due to the new requirements instituted under the Proposal. We further question the estimate for legal fees given that (1) the directors will have many new and expanded duties and responsibilities under the Proposal; and (2) with unlimited director liability we would expect more consulting resources on decisions would be utilized. Finally, it should not be overlooked that all of these costs will be

incurred regardless of the market; when assets under management decline during inevitable down markets, these costs will rise as a percent of assets under management.

Additionally, while the estimate separately acknowledges that the actual costs will be disproportionately higher for smaller mutual fund managers (estimated at 0.178 percent of assets under management compared to 0.016 percent for the overall industry), we do not agree with the summary conclusion that this "should not present an insurmountable obstacle for these managers." There will be a certain fixed cost involved to attract and compensate qualified board members, deploy additional staff to organize and support the governance agency, as well as pay for the additional costs such as insurance and administration, all of which we believe will have an undue impact on smaller firms.

The proposed minimum capital requirement will likewise increase the costs of doing business for mutual fund managers. We do not understand the CSA's rationale for this, and as there did not seem to be any empirical data in the Research Reports to support the recommendations, we are unsure how this proposal fits within the framework of the CSA's overall cost benefit analysis on this matter. In our opinion, tying the capital level to assets under management does not capture the level of risk involved if this is the premise of the CSA's proposal. Further, the recommendations appear to provide for a variable level of capital, which would seem to allow managers to reduce their capital commitment when assets under management decline during down markets. We think that insurance requirements would be a more appropriate measure to address potential managerial default which the CSA has noted as being a specific concern.

We believe that combining the extent of the proposed fund governance requirements with the proposed minimum capital requirements will impose undue burdens, especially on smaller managers who will find themselves at a competitive disadvantage. With smaller firms being burdened disproportionately, the likely result over time will be fewer firms managing funds, thus reducing investor choice. We say this recognizing that our organization might perhaps directly benefit as such, but we cannot in good conscience espouse this, as we believe that investors would ultimately suffer.

For an illustration of the internal manager costs to organize and fully support a governance agency, please consider the experience of CRMC in managing the 29 funds within the American Funds Group in the U.S. CRMC has 14 full time employees (including two senior managers and four fund secretaries) dedicated to supporting fund board governance activities. Additionally, many other employees from other departments, such as portfolio compliance, legal, accounting and statistics, spend a significant amount of time throughout the year producing information for fund board meetings. While we recognize that our infrastructure is tailored to the specific requirements under the 1940 Act in the U.S., it is nonetheless indicative of what level of commitment is required.

Thus, if, as we believe, the Proposal's initial cost assumption is erroneous, then the CSA's entire cost benefit analysis in the Proposal would likewise be flawed. The main theme of the Proposal, and in instituting a sea change in the current regulatory structure,

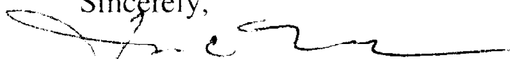
is "Striking a New Balance". We would assert that this proposed balance is in fact tilting toward over-regulation. The fund industry is already heavily regulated. However, if the CSA continues to espouse all of the recommendations under the Proposal, we believe it must concurrently address the current prescriptive rules governing funds as well as the lack of harmonization between provincial securities commissions so as to strike a reasonable balance. As the CSA has an obligation under the provincial securities laws to ensure that the costs of proposed restrictions on the business and investment activities of market participants are proportionate to the significance of the regulatory objectives sought, we believe that it is imperative that it first re-examine its proposals in light of more realistic cost estimates. We recognize that it is perhaps difficult to quantify exactly the cost and benefit of these specific proposals for improving fund governance. Recognizing that such an imprecise calculation may benefit from a measure for the margin of error involved, perhaps the CSA should consider whether the extent of these proposals would be justified if the estimated costs were in fact double, or even triple, what is used in the analysis.

We believe that upon such re-examination, the CSA will find that the alternatives it considered, as well as others, may look more viable. We note that the alternatives cited in the Proposal do not include use of a self-regulatory organization which might also be explored. We also take note of the recent BCSC Concept Proposal, many elements of which we think provide a practical approach to strike a new balance, but overall looks to lessen the regulatory burden on market participants. Certainly, as a regulator, the BCSC actively promotes measures for investor protection, but has found alternative approaches to be viable which we believe address many of the same issues that the CSA is considering. Given the date of the BCSC Concept Proposal (February 18, 2002), we are not certain how much time or consideration the CSA was able to give to this in drafting the CSA Proposal. In light of the above comments on cost benefit measures, we would urge the CSA to more closely examine the balance proposed by the BCSC Concept Proposal as well.

Please note that in addition to the above, we have had the benefit of reviewing the comment letter submitted by The Investment Funds Institute of Canada, and we generally support their positions.

Again, we appreciate this opportunity to submit our views on the Proposal, and your reconsideration of the cost benefit analysis of these specific proposals. As mentioned, we are not certain that the benefits which fund unitholders and potential investors would receive under the proposals as drafted are justified by the true costs involved. We would be happy to discuss further these matters should you find that useful.

Sincerely,



J.C. Massar,
President

cc: Thomas A. Hockin, Investment Funds Institute of Canada