[ROYAL BANK OF CANADA LETTERHEAD]

September 27, 2002

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

Dear Sirs:

Re: Ontario Securities Commission Rule 13-502 - Fees

I am internal counsel for Royal Bank of Canada and its wealth management affiliates. I am writing on behalf of RBC Funds Inc. ("RBCFI"), the manager of the Royal Mutual Funds and the RBC Advisor Funds (the Royal Mutual Funds and the RBC Advisor Funds are, collectively, the "Funds"), RBC Global Investment Management Inc. ("RBCGIM"), the portfolio advisor to those same funds, and Royal Mutual Funds Inc., the principal distributor of the Royal Mutual Funds, to provide you with our comments on proposed Rule 13-502 – Fees (the "Proposed Rule").

We are pleased to have the opportunity to comment on the Proposed Rule. We previously submitted comments on the March 2001 Concept Proposal for revising the fee schedule (the "Concept Proposal"). We have also participated in the development of the comment letter submitted by the Investment Funds Institute of Canada ("IFIC") and support those comments.

General

We are supportive of the general objective of the Ontario Securities Commission (the "OSC") to allocate the costs of regulation of the Ontario capital markets to the largest consumers of regulatory resources and to those who derive the greatest benefit from participation in those markets. We are also supportive of the OSC's specific objective of reducing fees paid by the mutual funds industry. However, we believe the Proposed Rule, as currently drafted, would effect an inappropriately large shift in regulatory costs from the Funds to RBCFI and RBCGIM.

By our internal calculations, the combined fees paid by RBCFI and RBCGIM would increase from $29,300 paid in 2001 to $500,000. In addition, while we recognize that the fees payable by RMFI to the OSC would be reduced from approximately $1 million to approximately $700,000, the total regulatory cost to RMFI includes fees levied by the Mutual Fund Dealers' Association (the "MFDA") which are approximately $1.6 million.

In summary, by our calculations, the total regulatory cost to these three entities, including MFDA fees, would increase from just over $1 million in 2001 to approximately $2.8 million. Conversely, the fees payable by the Funds would be reduced from approximately $980,000 paid in 2001 to $30,000.

In the notice accompanying the publication of the Proposed Rule, in response to comments received on the Concept Proposal, OSC staff suggested that mutual fund managers and investment managers could offset the increased fees by seeking securityholder approval to increase management fees. In our view, this suggestion is impractical and unrealistic. IFIC and other mutual fund industry participants have indicated in other contexts the very high cost to mutual funds of holding meetings and the very low securityholder participation in those meetings.

Our comments below are intended to identify and suggest changes to those provisions of the Proposed Rule that we feel effect significant inequities.

Calculation of Gross Revenues

A. Deductions from Gross Revenues

Each of RBCFI and RBCGIM would pay fees based on the calculation of gross revenues under s. 3.6 of the Proposed Rule.

Subsection 3.6(1)(a) would permit an entity to deduct from the gross revenues reported in its audited financial statements the items set out in subsections 3.6(2) and (3). While we have no concerns with respect to the items set out in subsection 3.6(2), we have the following concerns with respect to the deductions contemplated by subsection 3.6(3).

(i) ***"Sub-advisory fees":*** RBCFI and RBCGIM are currently structured as separate legal entities. Accordingly, RBCFI earns a management fee in respect of each of the Funds and pays an "advisory fee" to RBCGIM.

We assume that the use of the term "sub-advisory fees" in this subsection was predicated on an assumption that a single legal entity acts as both the manager and portfolio advisor to all mutual funds. In other words, we assume the OSC does not intend to preclude RBCFI, and other managers who are structured as separate legal entities from their funds' portfolio advisers, from deducting "advisory fee" payments from their gross revenues.

Accordingly, we suggest that subsection 3.6(3)(a) be amended to refer to "advisory fees or sub-advisory fees paid by the person or company".

(ii) ***"…paid by the person or company to another registrant firm in Ontario":*** We strongly object to this deduction being limited to payments to advisors or sub-advisors in Ontario. Like many primary portfolio advisors, RBCGIM engages non-Ontario-based sub-advisors ("non-resident sub-advisors") for

certain of the Funds, where it does not have sufficient expertise in-house and it believes that to do so is in the best interests of securityholders.

We assume that this limitation is intended to reflect the fact that most primary portfolio advisors who engage non-resident sub-advisors do so in reliance on the registration exemption set out in section 7.3 of OSC Rule 35-502 ("Rule 35-502"), which requires a registered Ontario-based advisor to take responsibility for investment advice provided by the non-resident sub-advisor. The amount deducted by a primary portfolio advisor in respect of sub-advisory fees paid to an Ontario-based sub-advisor would be included in that entity's gross revenues and would, therefore, be subject to fees under the Proposed Rule, while a similar amount paid to a non-resident sub-advisor engaged under Rule 35-502 would not be subject to fees, notwithstanding that liability for the non-resident sub-advisor's advice rests with the Ontario-based primary portfolio advisor.

We submit that (a) sub-advisory fees paid to a non-resident sub-advisor are a legitimate cost of doing business that should be deductible by primary portfolio advisors and (b) the cost of regulating a primary portfolio advisor who engages non-resident sub-advisors should be no greater than the cost of regulating a primary portfolio advisor who engages Ontario-based subadvisors. We would point out that whether a sub-advisor pays fees in Ontario has no impact on the liability of the sub-advisor to the primary portfolio advisor or the securityholders of a fund nor on the likelihood that the primary portfolio advisor will be able to successfully assert a claim against a non-resident sub-advisor for a breach of the contractual obligations to the primary portfolio advisor and a fund's securityholders contemplated by s. 7.3(1)(b) of Rule 35-502.

Accordingly, we suggest that subsection 3.6(3)(a) be amended to permit the deduction from gross revenues of all advisory or sub-advisory fees, whether they are paid to a non-resident sub-advisor or to an Ontario-based sub-advisor.

(iii) ***"Trailing Commissions"***: RBCFI is the manager of four funds-of-funds, known as the Royal Select Choices Portfolios (the "Portfolios"), which include underlying funds managed and investment managed by entities (the "Third Party Managers") unrelated to RBCFI. In order to comply with the prohibition against duplication of fees that is contained in the discretionary relief upon which the Portfolios are based, RBCFI has negotiated certain payments to be made by certain of the Third Party Managers to RBCFI. These payments are described in the contractual arrangements between RBCFI and the Third Party Managers as "trailing commissions" and are used by RBCFI to fund its obligation to pay trailing commissions to RMFI, the principal distributor, and to other distributors of the Portfolios. The "trailing commissions" payable to RBCFI are contemplated in the discretionary relief

applicable to the Portfolios (an applicable extract of which is attached as Appendix 'A') and are disclosed in the Portfolios' simplified prospectus under the heading "Fees and expenses paid by the manager of the underlying funds" (attached as Appendix 'B').[1]

Since RBCFI is not a registrant, subsection 3.6(3)(b) would preclude the Third Party Managers from deducting from their gross revenues the "trailing commissions" payable to RBCFI. We submit that underlying fund managers who have this type of arrangement in respect of fund-of-fund structures should not be precluded from deducting the applicable amount from their gross revenues, since the "trailing commissions" ultimately accrue to a mutual fund dealer or an investment dealer who will include these amounts in their gross revenues, where they are not deductible and, therefore, on which they will pay to the OSC a participation fee. In other words, we submit that if these amounts are not deductible by the underlying funds' managers, the OSC will ultimately earn a fee twice on these amounts: once while it is in the hands of the underlying fund manager and once while it is in the hands of the mutual fund dealers or investment dealers who distribute funds-of-funds.

Accordingly, we suggest that s. 3.6 be amended to permit managers of underlying funds in fund-of-fund structures to deduct from their gross revenues "trailing commissions", even if such payments are made to an entity that is not a registrant.

(iv) ***Other: Management Fee Rebates***: In addition to the "trailing commissions" described above, the Third Party Managers of certain of the Portfolios' underlying funds rebate a portion of their management fees directly to the Portfolios. Management fee rebates are a common attribute of fund-of-fund structures where the underlying funds do not have an "I" class or "O" class with a reduced, institutional management fee. In respect of the Portfolios, management fee rebates are contemplated in the contractual arrangements between RBCFI and the Third Party Managers and in the discretionary relief on which the Portfolios are based and are described in the Portfolios' simplified prospectus. We would also point out that this type of rebate is specifically contemplated by the proposed fund-of-funds amendments to National Instruments 81-101 and 81-102.

We submit that management fee rebates payable by an underlying fund manager to a top fund in a fund-of-fund structure should be deductible from the underlying fund manager's gross revenues, since management fee rebates are intended to achieve the same result as an offering of "I" or "O" classes or series of securities with a lower, institutional management fee. The inability to deduct management fee rebates would disadvantage those underlying fund

[1] We recognize that the existence of these "trailer fees" is also impacted by the proposed fund-of-funds amendments to National Instruments 81-101 and 81-102 on which we will also be submitting comments.

managers whose funds do not offer classes or series of securities that carry a lower, institutional management fee.

Accordingly, we suggest that s. 3.6 be amended to permit managers of underlying funds in fund-of-funds structures to deduct from their gross revenues all management fee rebates.

B. "Ontario Percentage" and "Specified Ontario Revenues"

We strongly object to the proposed method for determining an entity's "Ontario percentage" and, accordingly, its "Specified Ontario Revenues" in respect of entities that have a permanent establishment in Ontario.

Each of RBCFI, RBCGIM and RMFI has a permanent establishment in Ontario. Accordingly, 100% of the each of those entities' income is allocated to Ontario in their corporate tax filings under the *Income Tax Act.* As a result, each of them has an Ontario Percentage of 100% and their Specified Ontario Revenues are equal to 100% of their revenues calculated under subsection 3.6(1)(a).

We do not accept as fair or reasonable OSC staff's suggestion in the responses to comments received on the Concept Proposal that entities are free to structure their corporate affairs such that their Ontario Percentage more accurately reflects their Ontario capital markets activities. The OSC is charged with protecting Ontario investors from unfair, improper or fraudulent practices and to foster fair and efficient capital markets and confidence in capital markets in Ontario. We submit that it is inappropriate for the OSC to attempt to collect fees in respect of that portion of an entity's business that is not derived from Ontario investors and that does not relate to Ontario's capital markets. Each of RBCFI, RBCGIM and RMFI currently derives approximately 40% of its revenues from Ontario residents. Since each of them pays fees to the securities regulatory authorities of the other provinces and territories, it is our view that the fees that would be collected by the OSC on the remaining 60% of each entity's revenues is duplicative, not within the OSC's jurisdiction and, therefore, unacceptable.

We submit that the appropriate method for determining an entity's "Ontario percentage", regardless of whether the entity has a permanent establishment in Ontario or not, is set out in the second branch of the definition, i.e. "the percentage of the total revenues of the person or company attributable to capital markets activities in Ontario".

Accordingly, we strongly suggest that the definition of "Ontario percentage" be amended to remove the first branch of the definition and to make the second branch of the definition applicable to all entities carrying on business in Ontario.

C. Fixed, Tiered Capital Markets Participation Fees

We strongly object to the fixed, tiered fee schedule that is set out as "Appendix B – Capital Markets Participation Fees" ("Appendix 'B') to the Proposed Rule.

We do not believe that an entity whose Specified Ontario Revenues are $49 million should pay fees of $75,000, while an entity whose Specified Ontario Revenues are $51 million would pay $150,000. Similarly, we do not think it justifiable that two entities would each pay a fee of $500,000 where one had Specified Ontario Revenues of $200 million and the other $499 million.

Virtually all management fees, investment management fees, trailing commissions and sales commissions levied and paid in the mutual funds industry are expressed as a percentage of the value of the assets under management or adminstration or the value of the securities sold. As a result, participants in Ontario's capital markets experience fluctuations (sometimes dramatic fluctuations) in revenues from year to year. However, under the Proposed Rule, an entity whose Specified Ontario Revenues fluctuates within one of the tiers will not experience a corresponding decrease or increase in the participation fees payable.

We submit that the fixed, tiered participation fees contemplated by Appendix 'B' are inequitable as between two entities whose Specified Ontario Revenues are at extreme ends of the tiers and in respect of the extreme fluctuations that a single entity may experience in its Specified Ontario Revenues from year to year within the tiers.

Given that virtually all other fees in the mutual funds industry are expressed as a percentage of the value of assets under management or administration, we strongly urge that Appendix 'B' be amended such that participation fees applicable to the tiers are also expressed as a percentage of an entity's Specified Ontario Revenues, rather than a fixed amount.

D. Activity Fees Payable by Funds

We are very supportive of the intention of the OSC to reduce fees paid directly by mutual funds. However, we believe that the $600 Activity Fee proposed for the filing of a preliminary or pro forma prospectus and annual information form is not reflective of the true cost of regulation of a mutual fund.

Corporate issuers would be subject to certain Corporate Finance Participation Fees set out in Appendix 'A' to the Proposed Rule. Those fees are intended to replace the fees currently payable in respect of certain timely and continuous disclosure filings and are, in effect, indirectly paid by a corporate issuer's shareholders. Presumably, the OSC's rationale for levying these fees is that corporate issuers, and by extension their shareholders, benefit from the ongoing reporting obligations and the ongoing regulation of corporations by the OSC. In a sense, the corporate finance participation fees treat shareholders as indirect "participants" in Ontario's capital markets who are bearing their share of the regulatory costs.

We submit that mutual funds and their securityholders should be treated similarly. In other words, mutual funds and their securityholders are also "participants" in the Ontario

capital markets and should bear a greater portion of the cost of regulation than is contemplated by the Proposed Rule. Like corporate issuers, mutual funds are subject to timely and continuous disclosure filings, as well as requirements to file prospectus amendments upon the occurrence of "significant changes", in respect of which the OSC currently levies fees. Accordingly, we submit that mutual funds should be subject to fees that are more reflective of the true cost of continuous disclosure and ongoing regulation.

Accordingly, we suggest either that the activity fee levied in respect of the filing of a preliminary or pro forma prospectus under Appendix 'C' to the Proposed Rule be amended to more accurately reflect the true cost of regulation by the OSC on behalf of a fund's unitholders or that funds be subject to a participation fee similar to those set out in Appendix 'A' to the Proposed Rule.

We appreciate the opportunity to provide you with our comments on the Proposed Rule. We recognize that our comments are significant and detailed and we would be pleased to discuss them further with you at your convenience.

If you have any questions regarding our comments, please feel free to contact the undersigned.

Yours truly,

Mark D. Pratt
Senior Counsel
RBC Financial Group

cc: George Lewis, CEO, RBC Global Asset Management
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