

October 15, 2007

Mr. Neil Mohindra  
Acting Policy Manager  
**Joint Forum Project Office**  
5160 Yonge Street  
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North York, Ontario  
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Dear Sirs:

Thank you for this opportunity to provide the comments of Phillips, Hager & North with respect to the Proposed Framework for Point of Sale Disclosure for Mutual Funds and Segregated Funds ("Proposed Framework") developed by the Joint Forum of Financial Market Regulators ("Joint Forum").

Phillips, Hager & North ("PH&N") is the registered trade name for Phillips, Hager & North Investment Management Ltd. ("PH&NIM") and its wholly-owned subsidiary Phillips, Hager & North Investment Funds Ltd. ("PH&NIF"). PH&NIM is the manager and principal portfolio adviser for over twenty-five no-load mutual funds offered under simplified prospectus throughout Canada. PH&NIF is the principal distributor for these mutual funds and is a registered mutual fund dealer. PH&NIM has approximately \$67 billion in assets under management, of which approximately \$13 billion is invested in mutual funds, managed under discretionary and non-discretionary arrangements for private clients.

Since PH&N is involved in the mutual fund business, we will limit our comments to that industry, and not the segregated fund industry, and will focus only on three key areas of concern to investors: Receipt of the Disclosure Before Purchase; Nature of the Problem; and Potential for Product Arbitrage.

### **Receipt of the Disclosure Before Purchase**

The proposed Fund Facts document is a well-designed piece that summarizes key information about the mutual fund. Investors should be made aware that it is available and encouraged to read it before making a purchase decision. However, the Proposed Framework requires that the Fund Facts must be delivered before the initial and all subsequent purchases and the investor has no ability to waive this requirement. This will disadvantage, and potentially harm many of our clients.

When the Proposed Framework was being developed, there may have been a misperception that funds are always sold by registered mutual fund salespersons of a mutual fund dealer or registered representatives of an investment dealer ("Advisors") in person-to-person meetings. Handing over a disclosure document in such situations would not be particularly problematic.

However, at PH&N, almost 60,000 mutual fund investors have opened approximately 100,000 accounts with us, and these investors prefer to conduct approximately 75% of their trades in PH&N mutual funds over the telephone. Also, a significant percentage of retail unitholders in the PH&N mutual funds maintain their holdings at discount or full service brokerages, where we understand a significant percentage of transactions are also executed by telephone.

If the Proposed Framework is adopted, these clients will no longer be able to make an immediate mutual fund purchase or switch by phone (although they will be able to immediately transact in other securities and investment products, as discussed later in this letter).

The Proposed Framework seems to be based on an assumption that only naïve or unsophisticated investors invest in mutual funds. This is not the case. At PH&N our experience is that a significant percentage of clients have either undertaken significant and credible research based on ample information available, or have had a telephone discussion with an Advisor before making a purchase decision. When these investors decide to make an investment, they want to execute that decision promptly. In our view, investors should be allowed to waive the receipt of the disclosure document, and/or opt to have it delivered immediately after proceeding with their mutual fund investment decision. If not, and delays result, investors may suffer opportunity costs of not being invested, and more importantly, investors may suffer actual market losses if their ability to switch out of one asset class into another in a volatile market is delayed.

The Proposed Framework suggests the Fund Facts can be delivered by e-mail and therefore delays will be avoided for these telephone transactions. However, clients on the telephone do not always have ready access to their e-mail at the time of the call, and in some cases, do not have any access to e-mail.

Our recommendation is that the investor should have the option to receive the Fund Facts disclosure promptly after purchase for initial purchases and for subsequent purchases either waive receipt of the Fund Facts altogether or receive the Fund Facts disclosure promptly after the purchase.

### **Nature of the Problem**

PH&N fully supports the view that clients need to be fully informed, and should understand the risk that their investment portfolio will not meet their objectives. With regard to costs, PH&N has some of the lowest cost actively managed mutual funds available in Canada today. We are in complete agreement that the fees clients are paying within their investment portfolio should be plainly disclosed and transparent. To this end, we provide our clients with the weighted average management expense ratio ("MER") of their personal investment portfolio in each quarterly mutual fund statement, together with a plain English definition of the term MER.

It is our view that the proposed Fund Fact document will not adequately communicate the overall investment risk and costs the client will face when purchasing a fund. The true risk/reward of investing in a fund can only be evaluated in the context of the client's overall portfolio of investments. The fees a client will pay depend not only on MER's but also on the fee structures established by the Advisor's dealer. As a result, fees above and beyond those disclosed in the Fund Facts may be charged to the client. Accordingly, accurate information regarding benefits, risks and

costs of a particular investment decision is specific to that client's portfolio and the dealer fee structure, and has to be communicated by the Advisor, rather than having clients rely on a generic product disclosure document.

In our view, regulatory improvements to ensure clients better understand the risk and costs of their investment decisions have to be implemented at the overall portfolio level and in the context of the client's relationship with the dealer, and must incorporate all products within that portfolio, not just funds. Accordingly it seems to us that these regulatory improvements should be part of the work being done under the Client Relationship Model ("CRM") initiative.

In summary, rather than mandating the delivery of a generic prescribed product disclosure document before each purchase decision, it is our view that regulators should focus the CRM initiative towards implementing a principles-based requirement that holds Advisors responsible to explain and disclose the nature and extent of all compensation arrangements, and also holds the Advisor responsible to ensure that clients understand the potential investment benefits and risks of adding any investment product to their investment portfolio, before an investment decision is made.

### **Potential for Product Arbitrage**

Investors have a choice as to which investment product or security they purchase. Investment Dealers have a choice as to which investment products they choose to distribute. The proposed framework will serve to:

- ❑ Potentially delay an investor's decision to purchase mutual funds whereas the investor will face no delay in purchasing other securities;
- ❑ Increase costs and burden to the dealer (and the investor) to distribute mutual funds, whereas there will be no similar cost or burden to distribute other securities.

There is no similar point of sale disclosure required to be provided to help investors make a decision to invest in Separately Managed Accounts, even though these products have the same market risk and fee structures to mutual funds. Likewise, investors are not provided with point of sale disclosure before deciding to purchase exchange traded funds, individual stocks or bonds, or a principal protected note, nor before trading in options, futures or purchasing other types of derivatives. These financial products and securities are offered by Investment Dealers to investors without mandated point of sale disclosure even though their product offering documents are lengthy and it is difficult for investors to use the offering document to compare one investment to another, and it is likely that very few investors read the document in detail.

It is not clear from the Proposed Framework as to the basis of the Joint Forum's decision that point of sale disclosure should be applicable to mutual funds and segregated funds only. Comparing the underlying features of various securities and financial products, including Advisor compensation, fees, volatility and investment risk would not support such a distinction. It is a flawed assumption to believe that only unsophisticated or naïve investors invest in mutual funds and only sophisticated investors invest in all other securities.

We are not sure that mandating product disclosure rather than regulating the nature and scope of advice, will achieve the objective sought by regulators. However if we are wrong, and more concise product disclosure delivered before each purchase is what is required, then it seems incongruous to us that similar requirements are not being put in place for all securities. As mentioned above, PH&N has some of the lowest cost actively managed mutual funds available in Canada today and controlling costs is an important issue for us. The Proposed Framework will make the mutual fund a relatively more costly and more burdensome security to distribute compared to other securities. In that sense the proposal is not serving the interests of the investing public because those other securities which will be easier for dealers and investors to transact in, will often require investors to make more significant dollar investments, may not provide as much diversification, and may have significant market risk or fees.

If the intention is to introduce a fundamental change in how all securities are distributed in Canada, by requiring the delivery of point of sale disclosure before purchase, and changing investor withdrawal rights, then this vision should be articulated. We would respectfully suggest that if this is the case, then point of sale disclosure requirements should be introduced universally across all regulated products at the same time, because to do otherwise will result in product arbitrage with negative consequences to the Canadian investor and is not consistent with the regulator's mandate to protect public interest by fostering a securities market that is fair.

### **Concluding Comment**

In summary, we commend the Joint Forum for its development of the Fund Facts document but suggest that: investors are in the best position to determine whether they require the document before making a purchase or switch of a mutual fund; investment risk and compensation disclosure should not be at the product level but at the portfolio and advisory relationship level and addressed under the CRM initiative; and the investment risk and compensation disclosures should be applied to all investment products and advisory relationships.

Again, thank you for the opportunity to provide our comments.

Yours truly,

**PHILLIPS, HAGER & NORTH**  
**Investment Management Ltd.**

Original signed by "Larry Neilsen for John S. Montalbano"

John S. Montalbano  
President