BY EMAIL: comments@osc.gov.on.ca; consultation-en-cours@lautorite.qc.ca

March 12, 2014

Ontario Securities Commission
Autorité des marchés financiers
British Columbia Securities Commission
Alberta Securities Commission
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Financial and Consumer Services Commission (New Brunswick)
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
Superintendent of Securities, Northwest Territories
Superintendent of Securities, Yukon
Superintendent of Securities, Nunavut

Attention: The Secretary
Ontario Securities Commission
20 Queen Street West
19th Floor, Box 55
Toronto ON, M5H 3S8

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 Sirs/Mesdames:

RE: CSA Notice 81-324 and Request for Comment – *Proposed CSA Mutual Funk Risk Classification Methodology for Use in Fund Facts*

AGF Investments Inc. ("**AGF**") is pleased to respond to the specific questions of the Canadian Securities Administrators ("**CSA**") relating to risk classification methodology, as specified in CSA Notice 81-324 (the "**Notice**").

AGF certainly supports the CSA's goal of providing consistent, comparable and transparent risk measurement disclosure for investors. AGF appreciates that there is presently a lack of standardization in risk classification methodology across fund managers, thereby resulting in inconsistencies in risk disclosure across the spectrum of publicly available mutual funds. For this reason, AGF submits to the CSA that a mandatory adoption of a risk classification methodology is a more valuable alternative than just adopting a methodology for "guidance" purposes only.

AGF is, however, concerned with certain aspects related to the CSA's "Proposed Methodology" (as defined in the Notice). Most notably, AGF believes that mandating the CSA's Proposed Methodology could prove unnecessarily disruptive to the mutual fund industry. In particular, AGF supports the argument that adopting the CSA's Proposed Methodology would result in fund manufacturers having to change risk classifications simply to capture changes in nomenclature, despite the lack of actual changes in risk. This, in effect, would have the unintended consequence of requiring dealers/advisors to realign their clients' portfolios to ensure continued compliance with suitability requirements.

As a result of the foregoing, AGF proposes to the CSA that the best course of action would be to mandate the use of the existing IFIC Risk Classification Methodology (the "**IFIC Methodology**"), as opposed to instituting a new methodology. This would be the least disruptive option for investors and industry participants alike. Further, the well researched, analyzed and developed IFIC Methodology has been widely used by fund manufacturers for many years. Ultimately, there is no real benefit to "reinventing the wheel" on an already proficient means of determining risk measurement for mutual funds.

The responses below pertain to the questions outlined in Annex B of the Notice. For ease of reference, the responses set forth below have been numbered so as to correspond with the questions outlined in Annex B.

1. **As a threshold question, should the CSA proceed with (i) mandating the Proposed Methodology or (ii) adopting the Proposed Methodology only as guidance for fund managers to identify the mutual fund's risk level on the prescribed scale in the Fund Facts? Are there other means of achieving the same objective than by mandating the Proposed Methodology, or by adopting it only as guidance? We request feedback from investment fund managers and dealers on what a reasonable transition period would be for this.**

   AGF Response:

As indicated in the preamble to these responses, AGF supports mandating IFIC's Methodology (but not the CSA's Proposed Methodology).

Voluntarily allowing firms to adopt a risk classification methodology as "guidance" would have a minimal impact on achieving the overarching objective of standardizing risk classification across the mutual fund industry.

Since all fund manufacturers have varying prospectus and Fund Facts annual renewal periods, it would be AGF's recommendation that a grace period of one year be granted, in order for all firms to be able to transition their current risk rating systems to comply with the IFIC Methodology.

2. **We seek feedback on whether the Proposed Methodology could be used in similar documents to Fund Facts for other types of publicly-offered investment funds, particularly ETFs. For ETFs, what, if any, adjustments would we need to make to the Proposed Methodology? For instance should standard deviation be calculated with returns based on market price or net asset value per unit?**

   AGF Response:

   While AGF does not offer ETFs, we do advocate that the CSA Proposed Methodology should apply equally to ETFs. A risk classification methodology should be agnostic to the investment vehicle (trust fund, corporate class, ETF structure, etc.) and investment style (active vs. passive). All "investment fund" (i.e. not just mutual fund) risk classifications should utilize the same methodology.

3. **We seek feedback on whether you agree or disagree with our perspective of the benefits of having a standard methodology, as well as whether you agree or disagree with our perspective on the cost of implementing the Proposed Methodology.**

   AGF Response:

   AGF agrees that having universal application of a risk classification methodology for all funds is very important for both the investor and the fund manufacturer. Providing investors with consistent risk ratings allows for an "apples to apples" comparison that will give investors more confidence in their product selection; and ensures that fund manufacturers are aligned in their product representation to investors.

   AGF believes that the cost of incorporating the CSA's Proposed Methodology could be material, as this methodology has a notable impact to the risk classification bands currently used by most fund manufacturers.

The cost to fund manufacturers and dealers would be minimized if the IFIC Methodology is adopted, since most firms (like AGF) already have resources in place today to regularly calculate and review the risks associated with their product suite in accordance with this already well-defined methodology.

4. **We do not currently propose to allow fund managers discretion to override the quantitative calculation for risk classification purposes. Do you agree with this approach? Should we allow discretion for fund managers to move their risk classification higher only?**

   AGF Response:

   AGF has made certain discretionary adjustments to its fund risk ratings in the past. In certain cases, risk ratings were raised or lowered depending on subjective rationale such as manager turnover, geopolitical risk, etc. These adjustments were generally made to funds that had risk ratings on the cusp of either a higher or lower rating. Further, AGF made these adjustments to provide more fulsome risk disclosure to investors – embedding the essential "qualitative" aspects of measuring risk.

   Based on our experience, AGF believes that the discretion currently afforded fund manufacturers to classify funds either higher or lower from the volatility category indicated under the IFIC Methodology is an acceptable standard. AGF does, however, appreciate that the current IFIC Methodology does not suggest if, where and how much discretion should be applied. Consequently, without this clarity, AGF recognizes that risk ratings could deviate from the intended standardization. To this end, AGF recommends that discretion could be limited, without limitation, to new funds, funds that have undergone portfolio manager changes, funds that hover between two risk band classifications, and any other category deemed necessary for discretion by necessary stakeholders.

5. **Keeping the criteria outlined in the introduction above in mind, would you recommend other risk indicators? If yes, please explain and supplement your recommendations with data/analysis wherever possible.**

   AGF Response:

   Since AGF currently uses the IFIC Methodology, we inherently use standard deviation as the risk indicator. We agree with the CSA that this is the most common and suitable risk indicator, particularly given the simplicity and richness that this data point represents.

6. **We believe that standard deviation can be applied to a range of fund types (asset class exposures, fund structures, manager strategies, etc.). Keeping the**

criteria outlined in the introduction above in mind, would you recommend a different Volatility Risk measure for any specific fund products? Please supplement your recommendations with data/analysis wherever possible.

AGF Response:

Having reviewed our data, AGF does not feel there is a need to apply separate or different volatility measures for specific funds or fund types – i.e. standard deviation is the best application across all funds. While AGF acknowledges that standard deviation is not the only measure of risk, we feel that it is the simplest and most widely understood measure of volatility. And, as previously indicated, AGF submits that risk measurement should apply equally regardless of fund type or asset class since *consistent* expression of volatility is the objective.

7. **We understand that it is industry practice (for investment fund managers and third party data providers) to use monthly returns to calculate standard deviation. Keeping the criteria outlined in the introduction above in mind, would you suggest that an alternative frequency be used? Please specifically state how a different frequency would improve fund risk disclosure and be of benefit to investors. Please supplement your recommendations with data/analysis wherever possible.**

AGF Response:

AGF concurs with the industry practice of using monthly returns to calculate standard deviation. Monthly data is a traditional frequency used to view risk and return data in the fund industry. Further, fund manufacturer use of monthly data is consistent with third party data providers like Morningstar (relied upon by many advisors and investors), who also use monthly returns.

AGF also suggests that the use of yearly intervals ensures that no one month unnecessarily skews the results.

8. **Keeping the criteria outlined in the introduction above in mind, should we consider a different time period than the proposed 10 year period as the basis for risk rating disclosure? Please explain your reasoning and supplement your recommendations with data/analysis wherever possible.**

AGF Response:

While AGF agrees that using a 10-year annualized standard deviation strikes the appropriate level of data required to remove the "noise" of tail events, AGF does not believe that this time horizon provides any more information than the 3 or 5 year annualized standard deviation presently prescribed under the IFIC

Methodology. AGF appreciates that it is best to use a data set large enough to soften the impact of low probability and high deviation future events; however, AGF believes that the time period should not be too long as to be irrelevant to the investor. Consequently, AGF proposes maintaining the status quo with the time period already embedded within the IFIC Methodology.

9. **Keeping the criteria outlined in the introduction above in mind, should we consider an alternative approach to the calculation by series/class? Please supplement your recommendations with data/analysis wherever possible.**

   AGF Response:

   AGF does not feel that this level of analysis and disclosure is required given that the underlying mandate is the same across the series/class of the fund, irrespective of fund structure or cost/price. AGF does not feel that an alternative approach is required.

10. **Keeping the criteria outlined in the introduction above in mind, do you agree with the criteria we have proposed for the use of a reference index for funds that do not have sufficient historical performance data? Are there any other factors we should take into account when selecting a reference index? Please supplement your recommendations with data/analysis wherever possible.**

    AGF Response:

    While there are inherent drawbacks to the use of a reference index (see discussion below), AGF believes that use of a reference index is still the most logical solution. AGF submits that current practices of allowing fund manufacturers discretion to select an appropriate reference index is the most reasonable alternative for funds that do not have sufficient historical performance data.

    AGF does, however, want to draw the CSA’s attention to the fact that a reference index may not always adequately represent the experience an investor can expect from a mandate. For example, there are no rules or regulatory oversight which manage how closely a mandate should remain within a prescribed index.

    Further, CIFSC categories, in certain cases, can be agnostic to benchmarks. Using the CSA's proposed risk rating categories and standard deviation bands, for the S&P 500 and S&P/TSX, standard deviation over ten years is enough to rank the former as a Medium to High and the latter as a Medium (see table below). This anomaly can be extended to other categories where CIFSC rules do not closely align to fund benchmarks.

Index	Risk Date (Mo-End)	Std Dev 1 Yr (Mo-End)	Std Dev 3 Yr (Mo-End)	Std Dev 5 Yr (Mo-End)	Std Dev 10 Yr (Mo-End)	Std Dev 15 Yr (Mo-End)
S&P 500 TR (Bank of Canada) CAD	30/11/2013	7.91	8.66	11.26	11.42	12.83
S&P/TSX Composite TR	30/11/2013	7.82	10.43	12.86	13.98	15.06

Notwithstanding these anomalies, AGF does still continue to believe the use of a reference index is the most logical proxy for funds that do not have sufficient performance history.

11. **Keeping the criteria outlined in the introduction above in mind,**

    i. **Do you agree with the proposed number of risk bands, the risk band break-points, and nomenclature used for risk band categories?**

    ii. **Do the proposed break points allow for sufficient distinction between funds with varying asset class exposures/risk factors?**

If not, please propose an alternative, and indicate why your proposal would be more meaningful to investors. Please supplement your recommendations with data/analysis wherever possible.

AGF Response:

AGF does not agree with the number of risk bands and the break-points suggested under the CSA's Proposed Methodology. The nomenclature presents the greatest concern. The bias in the proposed nomenclature given the break-points places greater emphasis on more risk than is currently expressed by the bands under the IFIC Methodology.

For example, the IFIC Methodology uses a “Very Low” category, whereas the CSA's Proposed Methodology begins with “Low"; and on the high end, the CSA's Proposed Methodology ends the scale with “Very High” whereas the IFIC Methodology ends with “High". If an investor has an investment risk threshold of “Average” (using the existing IFIC nomenclature and risk bands), transitioning to the CSA's Proposed Methodology may reclassify the investor's holdings to “Medium to High", and may thus cause a significant yet unnecessary reallocation of assets.

It is AGF's understanding that most dealers only operate on a three band risk rating system. Therefore, while we currently use mid-point nomenclature (i.e. "Low to Medium", "Medium to High"), dealers round up the ratings we provide such that "Low to Medium" is given a "Medium" risk rating and "Medium to High" results in a "High" risk rating.

Based on our analysis, implementing the CSA's Proposed Methodology would result in more than half of the AGF funds moving up one risk rating notch. 27% of our funds move one notch to a split rating going from "Medium" to "Medium to High" or from "Low" to "Low to Medium". Given the aforementioned dealers' use of a three-band risk rating system, this would effectively result in 37% of our funds moving up two risk rating notches. This level of risk rating change, assuming other fund manufacturers are in a similar position, may cause considerable confusion with dealers given current suitability requirements with clients.

With respect to the break-points under the CSA's Proposed Methodology, although similar to those in the IFIC Methodology, AGF believes them to be unnecessarily more conservative. Applying the break-points, we found that the level of granularity at the lower end of the spectrum would not be of value to the investor, and the greater conservatism at the higher end of the spectrum creates, what we believe to be, misleading risk classifications.

12. **Do you agree with the proposed process for monitoring risk ratings? Keeping the criteria outlined in the introduction above in mind, would you propose a different set of parameters or different frequency for monitoring risk rating changes? If yes, please explain your reasoning. Please supplement your recommendations with data/analysis wherever possible.**

AGF Response:

AGF does not believe that it is necessary to monitor risk with the frequency suggested under the CSA's Proposed Methodology. AGF feels that monitoring any more frequently than annually is not required. Further, the current annual frequency aligns with dealers' annual suitability discussions with clients.

Based on back-testing of our own funds, AGF believes it to be unlikely that one month of data would move a fund into another risk classification. And, even if there was a shift, AGF suggests that that the shift would likely be temporary in any event. In addition, adoption of the IFIC Methodology would imply the use of the 3-year and 5-year rolling standard deviation, which AGF believes would not be materially impacted by even 6 months of data.

13. **Is a 10 year record retention period too long? If yes, what period would you suggest instead and why?**

AGF Response:

Given the CSA's requirements to retain records for 7 years from the funds' date of creation, we believe that this period should be sufficient for risk classification as well. There does not appear to be a compelling rationale for a 10 year record retention period.

14. **Please comment on any transition issues that you think might arise as a result of risk classification changes that are likely to occur upon the initial application of the Proposed Methodology. How would fund managers and dealers propose to minimize the impact of these issues?**

    AGF Response:

    Given our analysis, incorporating the nomenclature under the CSA's Proposed Methodology would needlessly cause greater than 50% of our funds to be rated one or two notches higher. Assuming many fund manufacturers would be similarly affected, this seems unnecessarily disruptive to the fund industry. Adopting the CSA’s Proposed Methodology would unnecessarily require excessive man hours and costs to incorporate these changes.

    Further, the CSA’s Proposed Methodology would result in investors having to either switch products or increase their stated risk tolerance with their dealer/advisor. AGF proposes that this is would be a costly and disruptive unintended consequence for those stakeholders.

    AGF strongly reiterates that in order to minimize the impact and costs to fund manufacturers, dealers and investors alike, the CSA should mandate the already existing IFIC Methodology.

We thank you for the opportunity to respond to the above issues with you. We look forward to continued constructive dialogue to ensure that the proposals with respect to potentially mandating a risk classification methodology lead to rules that are beneficial for investors.

Yours very truly,

Mark Adams
Senior Vice President, General Counsel & Corporate Secretary
AGF Investments Inc.