March 12, 2014

British Columbia Securities Commission
Alberta Securities Commission
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
Financial and Consumer Services Commission (New Brunswick)
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
Superintendent of Securities, Nunavut

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

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FAIR Canada is pleased to offer comments on CSA Notice 81-324 and Request for Comment by the Canadian Securities Regulators ("**CSA**") regarding the proposed CSA mutual fund risk classification methodology for use in Fund Facts dated December 12, 2013 (the "**Notice**").

FAIR Canada is a national, non-profit organization dedicated to putting investors first. As a voice of Canadian investors, FAIR Canada is committed to advocating for stronger investor protections in securities regulation. Visit www.faircanada.ca for more information.

1. FAIR Canada Comments and Recommendations - Executive Summary

FAIR Canada Supports the CSA in Mandating a Standardized Methodology for the Risk Rating

1.1. FAIR Canada supports the introduction of a standardized risk classification methodology (the "**Proposed Methodology**") that would allow investors to compare the risks of different funds and would provide transparency as to how the risk classification is determined.

1.2. FAIR Canada recommends that the Proposed Methodology be mandated, rather than adopted as guidance. Otherwise, it may not facilitate comparability between funds.

Volatility Risk Does Not Equate with An Investor's KYC Risk Tolerance

1.3. The volatility risk classification of a given mutual fund (for example "medium risk volatility") does not necessarily mean that it is suitable for a given investor who has a "medium" risk tolerance. Investment fund risk should not equate with a consumer's "know-your-client" ("**KYC**") risk tolerance. This over-simplifies the KYC process and is an issue that needs to be addressed. This does not accord with modern portfolio theory where the overall mix of products in a client's portfolio should reflect the KYC of a particular investor.

1.4. Given that volatility risk does not necessarily reflect the overall risk of a given security, FAIR Canada recommends that the description of fund risk in the Fund Facts document not be limited to volatility risk. FAIR Canada supports the suggestion made by Kenmar Associates that instead of presenting volatility as the overall risk rating for the fund it be presented as the measure of the variability of returns.

FAIR Canada Recommends that the CSA Follow the Principles and Best Practices of IOSCO's Point of Sale Disclosure

1.5. Fund Facts for any type of investment fund should follow the principles and best practices of the International Organization of Securities Commissions ("**IOSCO**"), including IOSCO's Principle 1.[1] If a synthetic indicator such as volatility risk is used it should be supplemented by (a) a narrative explanation of the indicator and its main limitations, and (b) a narrative explanation of risks which are materially relevant to the mutual fund and

[1] IOSCO Principles on Point of Sale Disclosure, Final Report, February 2011, at page 28.

which are not adequately captured by the synthetic indicator. At present Fund Facts provides a narrative explanation of the indicator but does not mention its main limitations nor does it provide any narrative explanation of risks which are relevant to the mutual fund and which are not adequately captured by the synthetic indicator.

Material Risks Not Captured by Volatility Should be Presented to Investors

1.6. FAIR Canada recommends that the CSA prescribe the inclusion of other material risks that are not captured by volatility in order to alert investors to the other risks associated with the investment fund in order to ensure that investors are aware of such risks. To advise retail investors to reference the risk section of the simplified prospectus, especially when this is no longer delivered to them, is not an adequate solution. As the CSA has stated, "[w]e know that many investors do not use the information in the simplified prospectus because they have trouble finding and understanding the information they need."[2]

1.7. We note that the CSA's focus group investor testing found that investors generally did not understand the three to four main risks of the mutual fund that were listed and did not always understand the explanation of the risk scale and the relationship between risks and losses.[3] The testing found that half of all retail investors were not very or not at all clear about what other specific risks were and 83% of the investors wanted a brief explanation of other specific risks. In response, the CSA removed the list of specific risks from Fund Facts and made other changes to the risk section. FAIR Canada does not believe that removing the list of the three to four other material risks is the appropriate solution to the problem and believes that the IOSCO Principle 1 should be followed.

1.8. There is no one single descriptor of risk that exists and to only provide one such descriptor in the risk section of Fund Facts ignores this reality and will lead to the real possibility that investors will not understand the limitations of the risk measure or the ability to assess its relevance and significance given their particular circumstances and investment objectives, which may result in poor outcomes for investors.

Retail Investors' Understanding of Risk: Make the Risk Section Meaningful

1.9. Retail investors understand risk as the chance of losing money and want to know how much money they stand to lose.[4] This could include how often they could experience losses, how much they might lose and how long it will take to make up the loss (time to recover).

[2] CSA Implementation of Stage 2 of Point of Sale Disclosure for Mutual Funds – Delivery of Fund Facts, (2013) 36 OSCB 6001 at page 6003.

[3] *Ibid*. at page 6002.

[4] The criteria that drives mutual fund decisions is How much the fund earned in the past, followed by Performance compared to similar investments and then Chances of losing money and the strongest criterion for deciding not to buy is Chances of losing money. See Investor Education Fund, Investor behavior and beliefs: Advisor relationships and investor decision-making study, written by The Brondesbury Group, Toronto, ON, 2012 at page 23.

1.10. FAIR Canada recommends that in addition to providing a standardized, mandated risk classification methodology (including an explanation of the indicator, its limitations and the other material risks) the risk of loss needs to be provided in a way that is meaningful to investors.

1.11. The performance section of Fund Facts indicates to investors what the worst calendar year return was as a percentage, how often a loss occurred in the last 10 years, and what the worst 3-month return was as a percentage and in dollar terms. This is important information for retail investors. However, the investor testing found that retail investors see the bar graph as explaining performance only and not risk. The document states: "Investors need to be better directed to benefit fully from the information on Page 2 as a presentation of performance and risk." This may be achieved by, at a minimum, changing the heading of the section to indicate that the section is also about risk of loss or, better yet, including in the risk section summary information on the worst loss in the last 10 years (in dollars), the worst 3 month return (in dollars) and the number of years that the investment fund experienced an annual loss so that the information is brought to the attention of retail investors.

Losses Count More than Gains

1.12. Standard deviation does not differentiate between movements above or below an average. Risk-adverse investors (that is, most Canadian retail investors, and particularly seniors and retirees) feel the effects of negative movements more acutely than positive movements, but measures of standard deviation do not account for this. The time needed to recover from a loss, especially a large loss, is not captured by standard deviation and needs to be conveyed to investors. Otherwise, there is a serious risk that they may construe a one year gain of 30 percent as making up for a previous year's loss of 30 percent.

Volatility Risk Does not Capture the Impact of Fees which Increases Risk of Loss

1.13. FAIR Canada supports the submission of both Dan Hallett and Kenmar Associates that risk should be calculated and reported separately for different series of a fund's units (for example, D and F class series) given that the greater the fees, the greater the risk (of loss) while standard deviation does not change.[5]

[5] See comments of Ken Kivenko (December 20, 2013), available online at <http://www.osc.gov.on.ca/documents/en/Securities-Category8-Comments/com_20131220_81-324_kenmar-associates.pdf> at page 7 and comments of Dan Hallett (February 21, 2014), available online at <http://www.osc.gov.on.ca/documents/en/Securities-Category8-Comments/com_20140220_81-324_hallettd.pdf> at page 6.

1.14. Given investors' low understanding of the impact of fees on risk and returns, FAIR Canada recommends that the CSA consider how to include information regarding the impact of fees on risk, which is not captured by standard deviation.

1.15. FAIR Canada recommends that the CSA consider how any risk scale used in Fund Facts will allow retail investors to compare other types of investment funds, such as alternative funds, closed ended funds, exchange traded funds or structured products or other types of investment products such as GICs, equity securities, etc.

1.16. FAIR Canada comments on the specific questions posed in the consultation document at section 6 below.

2. FAIR Canada Supports the CSA in Mandating a Standardized Methodology for the Risk Rating

2.1. FAIR Canada commends the CSA for its efforts to correct the known deficiencies in the current risk rating disclosure regime. FAIR Canada and other investor advocates previously raised concerns about the lack of disclosure and transparency with respect to the risk rating methodology used by mutual fund companies, and the resulting problem of inconsistent evaluations of risk amongst funds which limit the use of Fund Facts for comparative purposes. These issues were raised in letters to securities regulators dated June 27, 2011[6], November 10, 2011[7] and September 6, 2012[8]. We acknowledge that the CSA has undertaken significant analytical work and research in order to issue the Notice.

2.2. FAIR Canada supports the introduction of a prescribed, standardized methodology developed through a public consultation process rather than allowing the methodology for risk disclosure to be determined by fund managers, which in practice has resulted in the majority of fund managers using the non-public methodology developed and recommended by the Investment Funds Institute of Canada ("**IFIC**") (the "**IFIC Methodology**"), the investment fund industry's lobbyist.

2.3. The IFIC Methodology was developed without public consultation, investor input, or regulatory oversight. The IFIC Methodology measures the standard deviation over three- and five-year periods (a time period we consider to be too short), fails to capture a full market cycle, and is inconsistent with investors' desire to invest for the long-term. It also

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6 FAIR Canada letter to Maureen Jensen, Executive Director and CAO, OSC dated June 27, 2011, available online at http://faircanada.ca/wp-content/uploads/2011/01/FAIR-Canada-letter-re-Investment-Risk-Classification-Methodology.pdf.

7 FAIR Canada letter to the CSA dated November 10, 2011 re Implementation of Stage 2 of Point of Sale, available online at http://faircanada.ca/wp-content/uploads/2011/01/111110-FAIR-Canada-submission-re-Implementation-of-Stage-2-of-POS-Discl-for-MFs.pdf.

8 FAIR Canada letter to the CSA dated September 6, 2012 re Implementation of Stage 2 of Point of Sale, available online at http://faircanada.ca/wp-content/uploads/2012/09/120906-FAIR-Canada-comments-re-Implementation-of-Stage-2-of-POS.pdf.

allows for a considerable amount of subjectivity, thereby preventing meaningful comparisons of different mutual funds' risk levels.

2.4. The Proposed Methodology features a 10-year annualized standard deviation using monthly total returns and does not allow for qualitative factors or investment fund managers' discretion to impact the risk ranking process. This is advantageous as discretion can lead to misleading ratings and defeat the goal of comparability. The Proposed Methodology will have six risk categories with their corresponding standard deviation bands. This may result in changes to the risk band classification for some funds, from the Medium rating to a Medium-High rating. The process for switching to the new methodology will need to be implemented in a coordinated fashion at one specified date so that comparability is maintained and confusion reduced. The need for some reclassification of funds into a different (and more accurate) risk bands is not a valid reason not to adopt a standardized methodology.

Volatility Risk Should Not Equate with An Investor's KYC Risk Tolerance

2.5. The volatility risk classification of a given mutual fund (for example "medium risk volatility") does not necessarily mean that it is suitable for a given investor who has a "medium" risk tolerance. Investment fund risk should not equate with a consumer's KYC risk tolerance. This over-simplifies the KYC process and is an issue that needs to be addressed. This does not accord with modern portfolio theory where the overall mix of products in a client's portfolio should reflect the KYC of a particular investor.

Mandate Methodology – Guidance Insufficient

2.6. FAIR Canada recommends that the Proposed Methodology be mandated, rather than adopted as guidance. Otherwise, it may not facilitate comparability between funds. It has been demonstrated that the IFIC methodology can be unreliable and inconsistent between funds that are otherwise very similar[9]. The Notice indicates that if a methodology is used that is shorter than 10 years, "… risk indicators (including standard deviation) tended to fluctuate too much. Over shorter time periods, risk indicators also have a tendency to be misleading – showing relatively low levels of Volatility Risk just before a market downturn and relatively high levels of volatility just after a market downturn."[10]

[9] See comments of Dan Hallett, CFA, CFP to the CSA dated February 21, 2014, *supra* note 5 at page 2.
[10] CSA Notice 81-324 at page 11856.

3. FAIR Canada Recommends that the CSA Follow the Principles and Best Practices of IOSCO's Point of Sale Disclosure

3.1. While the Proposed Methodology is a significant improvement over the status quo (and the IFIC Methodology as used by many fund managers today), volatility risk does not reflect the investment fund's risk in its entirety. Standard deviation measures volatility and is not necessarily a substitute for an overall risk assessment, nor is it a proxy for retail investors' use of the term 'risk' which we discuss further in section 4 below.

3.2. Given that volatility risk does not necessarily reflect the investment fund's overall level of risk, FAIR Canada recommends that the description of risk of the fund in Fund Facts not be limited to volatility risk. FAIR Canada supports the suggestion made by Ken Kivenko that instead of presenting volatility as the overall risk rating for the fund, that it be presented as the measure of the variability of returns.

3.3. FAIR Canada recommends that the Fund Facts document for any type of security follow the principles and best practices of the International Organization of Securities Commissions (IOSCO), including IOSCO's Principle 1:

> Key information should include disclosures that inform the investor of the fundamental benefits, risks, terms and costs of the product and the remuneration and conflicts associated with the intermediary through which the product is sold.
>
> …
>
> Key information in product disclosure could include:
>
> …
>
> Its risk and reward profile. Risk disclosures should include the material risks for the product. This may include performance risk/volatility, credit risk, liquidity risks and operational risks. In some jurisdictions, a scale may be considered appropriate to identify the overall risk measurement or classification of the product, rather than a list of specific product risks, and this may be accompanied by appropriate narrative explaining how to interpret the scale. This may assist with risk comparisons, although regulators and investors need to be aware of the inherent limitations in such measures.[footnote] Regulators might wish to include supporting information indicating minimum length of holding relative to short term volatility, what types of "targeted investors" the product is being marketed to and what commitment those investors need to make;…[11]

Footnote 31 provides:

> …in Europe, the "Risk and reward profile" section of the key investor information document shall contain a synthetic indicator, supplemented by: (a) a narrative explanation of the indicator and its main limitations; (b) a narrative explanation of risks which are materially relevant to the UCITS and which are not adequately captured by the synthetic indicator.[12]

[11] *Supra* note 1.
[12] *Ibid*.

3.4. If a synthetic indicator such as volatility risk, is used, it should be supplemented by (a) a narrative explanation of the indicator and its main limitations, and (b) a narrative explanation of risks which are materially relevant to the mutual fund and which are not adequately captured by the synthetic indicator. At present Fund Facts provides a narrative explanation of the indicator but does not mention its main limitations nor does it provide any narrative explanation of risks which are relevant to the mutual fund and which are not adequately captured by the synthetic indicator.

Material Risks Not Captured by Volatility Should be Presented to Investors

3.5. FAIR Canada recommends that the CSA prescribe the inclusion of other material risks that are not captured by volatility in order to alert investors to the other risks associated with the investment fund in order to ensure that investors are aware of such risks. To advise retail investors to reference the risk section of the simplified prospectus, especially when this is no longer delivered to them, is not an adequate solution. As the CSA has stated, "[w]e know that many investors do not use the information in the simplified prospectus because they have trouble finding and understanding the information they need."[13]

3.6. CSA focus group investor testing found that investors generally did not understand the three to four main risks of the mutual fund that were listed and did not always understand the explanation of the risk scale and the relationship between risks and losses.[14] The testing found that half of all retail investors were not very or not at all clear about what other specific risks were and 83% of the investors wanted a brief explanation of other specific risks. In response, the CSA removed the list of specific risks from Fund Facts and made other changes to the risk section. FAIR Canada does not believe that removing the list of the three to four other material risks is the appropriate solution to the problem and believes that the IOSCO Principle 1 should be followed.

3.7. There is no one single descriptor of risk that exists and to only provide one such descriptor in the risk section of Fund Facts ignores this reality and will lead to the real possibility that investors will not understand the limitations of the risk measure or the ability to assess its relevance and significance given their particular circumstances and investment objectives, which may result in poor outcomes for investors.

3.8. FAIR Canada suggests that one way risks could be presented to investors could be in the form of a matrix, as illustrated below.

[13] *Supra* note 2 at page 6003.
[14] *Ibid*. at page 6002.

	Low	Low to Medium	Medium	Medium to High	High	Very High
Volatility Risk				●		
Liquidity Risk					●	
Currency Risk					●	
Political Risk						●

4. Retail Investors' Understanding of Risk - Make the Risk Section Meaningful

4.1. Retail investors understand risk as the chance of losing money and want to know how much money they stand to lose.[15] This could include how often they could experience losses, how much of their investment they might lose, and how long it will take to make up the loss (time to recover).

4.2. Most Canadian investors self-identify as conservative when it comes to investment risk and "Canadians more often indicate a preference for investment options that involve a lower return and less downside risk than ones that carry a higher possible return, and higher downside risk."[16] Retail investors are worried primarily about the risk of loss of their capital, and secondarily about the risk that their investments may not perform as expected.

4.3. Standard deviation measures volatility, and is not necessarily a substitute for an overall risk assessment, nor is it a proxy for retail investors' use of the term 'risk'. According to a retail investor report prepared for the Investor Advisory Panel of the Ontario Securities Commission, "[t]he perception of risk appears more closely tied to the questions [retail investors] were asked for their KYC form, rather than to any underlying notion of investment volatility."[17] The strongest criterion for an investor deciding not to buy a particular investment "is simply the Chances of losing money."[18]

[15] The criteria that drives mutual fund decisions is How much the fund earned in the past, followed by Performance compared to similar investments and then Chances of losing money and the strongest criterion for deciding not to buy is Chances of losing money. See Investor Education Fund, Investor behavior and beliefs: Advisor relationships and investor decision-making study, written by The Brondesbury Group, Toronto, ON, 2012 at page 23.

[16] Ipsos Reid, "CSA Investor Index 2009", prepared for the Canadian Securities Administrators Investor Education Committee (October 5, 2009), online: <http://www.securities-administrators.ca/uploadedFiles/General/pdfs/CSA%20Investor%20Index%202009%20Final_EN.pdf?n=6519> at page 38.

[17] Lori Bottrell & Ed Weinstein, "Focus Groups with Retail Investors on Investor Rights and Protection" (April 7, 2011) prepared for the Investor Advisory Panel of the Ontario Securities Commission, at page 6, online: <https://www.osc.gov.on.ca/documents/en/Securities-Category1-Comments/com_20110427_11-765_ananda.pdf>.

[18] The Brondesbury Group, "Investor behaviour and beliefs: Advisor relationships and investor decision-making study" (2012), prepared for the Investor Education Fund, at page 23.

Losses Count More than Gains

4.4. Standard deviation does not differentiate between movements above or below an average. Risk-adverse investors (that is, most Canadian retail investors, and particularly seniors and retirees) feel the effects of negative movements more acutely than positive movements, but measures of standard deviation do not account for this. The time needed to recover from a loss, especially a large loss, is not captured by standard deviation and needs to be conveyed to investors. Otherwise, there is a serious risk that they may construe a one year gain of 30 percent as making up for a previous year's loss of 30 percent.

4.5. FAIR Canada recommends that in addition to providing a standardized, mandated risk classification methodology (including an explanation of the indicator, its limitations, and the other material risks) risk of loss needs to be provided in a way that is meaningful to investors.

4.6. The performance section of Fund Facts indicates to investors what the worst calendar year return was as a percentage, how often a loss occurred in the last 10 years, and what the worst 3-month return was as a percentage and in dollar terms. This is important information for retail investors. However, the investor testing found that retail investors see the bar graph as explaining performance only and not risk. The document states: "Investors need to be better directed to benefit fully from the information on Page 2 as a presentation of performance and risk."[19] This may be achieved by, at a minimum, changing the heading of the section to indicate that the section is also about risk of loss or, better yet, including in the risk section summary information on the worst loss in the last 10 years (in dollars), the worst 3 month return (in dollars), and the number of years that experienced an annual loss so that the information is brought to the attention of retail investors. We believe that this will enhance investors' understanding of risk and provide a more accurate picture of the overall risk.

5. Volatility Risk Does not Capture the Impact of Fees which Increases Risk of Loss

5.1. FAIR Canada supports the submission of both Dan Hallett and Kenmar Associates that risk should be calculated and reported separately for different series of a fund's units (for example, D and F class series) given that the greater the fees, the greater the risk (of loss) while standard deviation does not change.[20]

5.2. Given investors' low understanding of the impact of fees on risk and returns, FAIR Canada recommends that the CSA consider how to include information regarding the impact of fees on risk, which is not captured by standard deviation.

[19] CSA Point of Sale Disclosure Project: Fund Facts Document Testing Prepared by: Allen Research Corporation September 2012 at page 39.

[20] *Supra* note 5.

5.3. Investors must be sufficiently warned in the disclosure of the fund's performance that past performance is not a useful predictor of future returns. Morningstar has found that the best predictor of a fund's performance is its expense ratio rather than its past returns.[21] Right now Fund Facts informs investors that past performance "… does not tell you how the fund will perform in the future". FAIR Canada recommends that the CSA test whether this sufficiently alerts investors to the fact that past performance is not a useful predictor. It is well known that investors (and possibly advisors) place undue reliance on performance rankings as studies show that monies flow into funds that receive high rankings.

6. FAIR Canada's Response to the CSA's Questions for Comment on the Notice and Request for Comment

Question 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.*

6.1. FAIR Canada recommends mandating a standardized methodology and cautions against only implementing it as guidance. See sections 2.2 and 2.6 above. FAIR Canada suggests that research be undertaken by the CSA as to whether the Proposed Methodology will be very meaningful or appropriate for wrap mutual funds, target date funds, return of capital funds or those that use leverage or alternative strategies.

Question 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?*

6.2. FAIR Canada recommends that the CSA consider how any risk scale used in Fund Facts will be made comparable for retail investors to other types of investment funds, such as alternative funds, closed ended funds, exchange traded funds or structured products.

6.3. How will alternative funds, closed end funds, leveraged ETFs or structured products' risk scale be determined? If many funds come out as high risk from a volatility perspective,

[21] Russel Kinnel, "How Expense Ratios and Star Ratings Predict Success" (August 9, 2010), available online at: <http://news.morningstar.com/articlenet/article.aspx?id=347327>.

will comparisons by retail investors be meaningful or misleading? Will volatility be a relevant measure of risk for some types of investment funds? There may be high-risk mutual funds that are significantly less risky than a high-risk closed end fund or alternative fund but this may not be apparent. This may be true because the high-risk mutual fund has a significantly lower volatility risk as measured by a 10-year standard deviation and/or (more likely) because of other significant risks that the alternative fund has that the mutual fund does not (liquidity risk, counterparty risk, etc.) The limitations of volatility risk will likely become evident when trying to expand summary disclosure to other types of funds. This is another reason why FAIR Canada recommends that volatility risk should not be the only type of risk presented to investors in the risk section of Fund Facts.

Question 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.

6.4. We agree that a mandated standardized methodology will result in comparability between funds and greater transparency as to how the risk classification is determined.

6.5. FAIR Canada believes that the minimal costs anticipated by the CSA will be greatly outweighed by the benefits of providing consistency and transparency of disclosure and improved comparability of investment funds' risks.

Question 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?

6.6. The benefit of comparability and transparency will be lost if fund managers are provided discretion to override the calculation. If the volatility risk is not capturing the appropriate risk for a given fund and a fund manager wants to use his discretion to move to a different band, this indicates that volatility risk is not adequately capturing the risk of the fund. This demonstrates the need to follow IOSCO's principles and best practices for point of sale disclosure as discussed above.

Question 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 a basis for risk rating disclosure? Please explain your reasoning and supplement your recommendations with data/analysis wherever possible.

6.7. We note that CSA research has found that a 10- year standardization is less misleading than shorter time periods. However, we recognize that many funds do not have 10 years of data and that it is not uncommon for one fund's units to be merged into a newer series of the same fund. The CSA should consider whether for those funds without 10 years of data: (i) the monthly total return of a reference index should be used or whether returns of an older series (which is essentially the same fund) should be used instead where available, and (ii) an older fund's returns should be included when an older fund's units have merged into a newer series. Alternatively, the CSA should consider whether it is better to use a 7-year standard deviation if this presents much fewer incidences of needing to backfill the data with a reference index and will be therefore subject to less manipulation.

6.8. We also recommend that the CSA consider, if it has not done so, whether the reliability of the volatility risk measure is dependent on the inclusion of a significant market downturn in the time period utilized. Is it important to include a bear market in the time period rather than a set number of years to prevent the measure from being misleading?

<u>Question 9:</u> 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.

6.9. Please see section 5 above.

<u>Question 14:</u> 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.

6.10. See section 2.4 above.

We thank you for the opportunity to provide our comments and views in this submission. We welcome its public posting and would be pleased to discuss this letter with you at your convenience. Feel free to contact Neil Gross at 416-214-3408 (neil.gross@faircanada.ca) or Marian Passmore at 416-214-3441 (marian.passmore@faircanada.ca).

Sincerely,

Canadian Foundation for Advancement of Investor Rights