June 9, 2017

Response to CSA Consultation Paper 81-408 – *Consultation on the Option of Discontinuing Embedded Commissions – January 10, 2017*.

Dear Sirs,

The CSA Consultation Paper 81-408 advocates both a total, wholesale repeal of a fully accepted norm of commerce and the Canadian investment industry (the manufacturers' sales agency agreement), and a proposes to replace this norm that has operated in competitive market conditions for over 5 decades with a conjecture for a format of a payment-for-service contracting between investors and their registrant dealer that displays no understanding of the costs inherent to back office operational structures or transaction processing within the Canadian investment industry.

No Evidence of Harm or Advantage

CSA Consultation Paper 81-408 is a proposal that inherently maligns all Canadian registrants and regulators, openly and without offering any documentation or evidence.

It is a paper that does not undertake, nor provide sourcing from others, of any monetary analysis of the systemic harm and abuse to investors to substantiate its allegation, nor does it provide any data from enforcement actions on this alleged systemic abuse.

As to the allegations of asset managers gaining systemic advantage, CSA Consultation Paper 81-408 does not present even a single funds that has outperformed its peers in the accumulation of assets under administration (AUM) due to the cited conflict of interest of registrant dealers or advisors.

It is staggering that a 165 page paper shows no documented analysis of the value of the damage sustained by investors, nor offers any proof of an asset manager's profiting, from what the paper claims cannot be permitted to continue.

No Understanding of the Operational Costs in Back Offices

CSA Consultation Paper 81-408 does not investigate or detail the different costs structures that dealers encounter when their investors purchase and hold managed assets as opposed to those costs arising from transactions of any of security, whether exchange-traded or traded on the debt market.

CSA Consultation Paper 81-408's failure to appreciate and include references to the substantially higher cost inherent to managed assets, underpins Consultation Paper 81-408's advocacy for dealers to be required to openly and continually highlight a comparison of pricing, directly to investors, that places all mutual funds and managed funds at an enormous competitive disadvantage.

Advocating for massive competitive disadvantage to managed funds, inherent to the strict pricing in a new fee-per-service alternative will prove exceedingly costly, devastating to all mutual funds and asset management in Canada and structurally damaging to the Canadian investment industry.

Emotive Phrasing Shaping the Fate of the Canadian Investment Industry

Having highlighted the existence of a conflict of interest that is navigated by registered advisors at point of sale, Consultation Paper 81-408 claims, without providing any evidence, systemically investor abuse the CSA does not ask for public comment upon "Whether Fund Managers Are Being Allow to Pay Dealers Too Much" would elicit much less angst, but no less interest from the public, Consultation Paper 81-408 instead purposefully chooses the emotively charged, impugning phrasing, "Discontinuation of Embedded Commissions".

Choice of phrase has created a politicized environment that now threatens the existence of the mutual fund industry in Canada and the global stature and viability of Canadian exchanges and debt markets.

Repealing a Business Practice Honed Within Competitive, Highly Regulated Markets

The advocacy for repeal of a time-honoured, established by highly competitive conditions, and proven as an on-going business structure under Canadian regulation, is based upon unsupported conjecture.

Posing to resolve the inherent conflict of interest that faces any sales agency (they must always navigate the multitude of limitations within any product they represent between the desires of manufacturer and consumer), Consultation Paper 81-408 does not present any evidence to justify a need for its radical solution.

Even though this conflict of interest has been part of the investment industry for decades prior to being noted and discussed in the 1980s by the Stromberg Commission, a 165 consultation paper published in 2017 proclaims systemic investor abuse to have occurred and continues to occur, but cites no history of investor complaints and no enforcement actions.

Consultation Paper 81-408 should be enumerating those harmed, or specifically identify those individuals or corporations who have been found, publicly, to be perpetrators of harm, before undertaking to a public maligning of all Canadian regulators and registrants and advocating wholesale change to business practices.

Fee-Per-Service – No Definition; Multitude of Inherent Conflicts of Interest.

Worse still, after maligning regulator and registrant alike and advocating an immediate discontinuation of a norm, Consultation Paper 81-408 advocates an alternative does not exist, without any analysis of the present conditions that govern the cost of securities transactions and the holding of securities, let alone attempting to define in terms of the time, manpower, software systems and processes, or potential financial costs the implementing any version of its proposed solution/alternative.

It is entirely unprofessional for the authors of a 165 page paper, to back away and leave a required structure to replace a suddenly "discontinued" business practice to the investment industry to figure out, design, amass the resources for, and implement in time. Worse still, the paper proclaims this non-alternative, both unknown in scope and extent, and wholly unanalyzed - to be superior – even though fee-per-service is commonly accepted within the investment industry to have far more inherent conflicts of interest for an advisor than imbedded commissions.

No Analysis of Resources Require by Canadian Investment Industry

Even a brief survey of these requirements or a structured “fee-per-service” alternative (one is provided below) will establish as obvious that Consultation Paper 81-408’s recommendations are far beyond the resources of the Canadian investment industry.

Moreover, it was not demonstrated by Consultation Paper 81-408 that Canadian investors can reasonably expect an increase to their net investment performance as a result of the advocated changes.

Consultation Paper 81-408 advocates a “mandated redistribution” of fund management revenues; halting the forwarding of managed fund and managed account revenues that are presently being paid by the manager to a dealer to defray the higher costs involved in purchasing and owning mutual funds (including manual processing of purchases, withdrawals, and reinvestment, T3 tax forms, etc.).

Consultation Paper 81-408 envisions that these same dramatically higher costs will be presented to the investor by the dealer, in a posted schedule that openly contrasts each of these high costs against the low fees charged for the efficient, automated events for exchange traded and debt securities.

What is self-evident from Consultation Paper 81-408’s proposals is that investors will see more and higher charges from dealers and higher total costs towards maintaining their managed investments, without observing measurably superior investment results from these assets.

K-Y-C is a Factor at Point of Sale (POS)

Consultation Paper 81-408 also clearly avoids reference to K-Y-C when it issues its collectivizing statements about mutual fund commissions. The commission rates paid to dealers/advisors by managed funds rise in direct relationship to the risks inherent to the assets within the fund; moneymarket funds being the least expensive, equity and alternative asset management being the most expensive.

In every investor account, K-Y-C regiments the portfolio mix recommended and maintained by a dealer and advisor and K-Y-C inherently defaults towards the lower cost, lower risk alternatives. Also true is that investors seek professional management for their assets with a multi-year horizon. This allows the investor a longer amortization period for the higher purchase costs of professional management, thus over time this horizon reduces to insignificant the impact of any slightly higher commission that might be charged between two funds of the same asset class.

If one starts with the primacy of K-Y-C under Canadian regulation and the expected long term amortization of a fund’s purchase cost at Point of Sale (POS), it becomes exceedingly difficult to construct a scenario of systemic investor harm. However, Consultation Paper 81-408 cites neither; it simply repeats allegations of investor harm from a conflict of interest we know is already carefully circumscribed and restrained by an advisor’s regulatory obligations and the dealer’s compliance department.

Sales Commission Are Different From Trailer Fees

Consultation Paper 81-408 regularly obfuscates the two distinctive forms and structures of payments that occur between fund managers and dealers; sales commission and trailers fees. Consultation Paper

81-408 casually enlists any resulting confusion from its use of the emotive phrasing, “Embedded Commissions” to elicit support for the paper’s recommendations.

Investor Recollection

Consultation Paper 81-408 claims that investor interview surveys have shown that Canadian investors do not often recall the terms or percentages of the fund manager/dealer sharing of fund MERs for the assets they hold.

No mention is made in Consultation Paper 81-408 of the regulatory requirement that investors be apprised of this distribution at the time of purchase (POS). This is a glaring omission. It is the structural cornerstone to the paper’s core and fundamental allegation and “blanket statement” that the conflict of interest, inherent to the present commission payment structure income, is systemically resolved to the harm of the investor.

Specifically to this point, Consultation Paper 81-408 states because advisors are paid by commission asset managements “incent dealers and their representatives to sell funds that compensate them the best”.

It deserves to be repeated that no statistics, no documentation of complaints on this issue to regulators, or history of enforcement actions against such dealer or advisor non-compliant behaviour are provided in support of Consultation Paper 81-408’s existential allegation – there has been investor harm. Indeed, Consultation Paper 81-408 provides no evidence to demonstrate that investor harm results from differences in commission rates in a systemic fashion or even that is it a statistically significant problem in the Canadian investment industry.

Perhaps even more importantly, ignored and unstated by the Consultation Paper 81-408 is that the same Canadian consumer/investor who was surveyed would also not be aware that the exact same form of manufacturers’ sales agency agreement/contract was imbedded into the price of the blue jeans they are wearing, the groceries, articles of jewellery, telephones and telephone services (which are regulated industries), and the energy forms (including natural gas and electricity, which are regulated industries) they purchase or even within the financing they might obtain for costly products like homes, furniture, and recreational vehicles.

Clearly, as consumers, Canadian investors show themselves to have no problem with the conflict of interest arising from minor, less than ½%, differences in commissions rates between the alternative long-term investments they have been asked to choose between. This reality appears to be purposefully lost by Consultation Paper 81-408 as it clear, the paper does not entertain any alternative interpretation to the survey or potential for an alternative interpretation; only its own.

Maligning the Canadian Industry

Consultation Paper 81-408 does not make any reference Industry Regulations which require written and verbal disclosure of these agreements/contracts by registrants at point-of-sale (POS). It neither investigates whether registrants fail to meet obligations, nor raises the question whether Regulators have abjectly failed to monitor its registrants, which, of course is a systematic, wholesale failure of all Canadian regulators to perform their mandate of investor protection.

Consultation Paper 81-408 simply, in blanket statement fashion, maligns all Canadian regulators and registrants.

Costs of Process to Dealer Back Office

Consultation Paper 81-408, does not mention, take into consideration, nor does it analyze the highly significant, higher costs of mutual funds to dealer back-offices. There is no mention of costs, whether transaction related processes, safekeeping costs, tax form preparation costs, or otherwise. Nor does Consultation Paper 81-408 recognize there are a diversity of business practices between fund managers' back offices, creating different costs of process between fund managers and funds, even nearly identical mutual funds or funds from the same manager.

As a result of this oversight, Consultation Paper 81-408 fails either recognize or acknowledge that payments to dealers encompass more that the costs of investment selection.

Fee-for-Service – An Open-Ended, Unlimited Matrix

The cost, complexity, and openness to abuse of the proposed Fee-per-service model, as an alternative system to fund manager to dealer sales commissions and trailer fees advocated by Consultation Paper 81-408, is staggering.

To begin with, a strict relational fee-per-service at a dealer level represents an absolutely limitless number of security related event prices, levels of service, the product, activity, overhead, and compliance involved, back office practices, and more. None of these unique pricings can ever be directly compared by the investor or regulator at reasonable cost.

To create its own matrix, each dealer will have to begin with the operational differences between fund managers, operational costs in the dealer per account type come next, then a matrix of the vast and growing multitude of managed investment products and hundreds of different transaction types, all of which will need to be priced distinctly and separately Then there is the advisor conversation with the investor for which every service an advisor provides is to be billed for itself (be it one, two, three or more investments to consider; review of price history, percentage allocation to the portfolio, or relative income analyses of a portfolio; then whether the recommendation(s) pertain to one portfolio or a group of portfolios, etc.). There is no fashion by which Consultation Paper 81-408's advocacy of fee-per-service and its limitless matrices can be more easily understood and within the control of the investor, than the present POS advisor presentation of the costs to the mutual fund investor.

A schedule of charges that an investor will be subjected to an invoiced upon simply cannot be compared between dealers, or even advisors.

Consultation Paper 81-408 does not comment upon the costs to regulators for its alternative, fee-per-service; perhaps for good reason. The difference in regulatory cost between ensuring investor protection with the existing advisor payment system vs. the Consultation Paper 81-408's proposed "Fee-for-Service", presently appears to be beyond calculation.

Other Factors in Investor Decision-making

Within the Consultation Paper 81-408 there is no supporting evidence to justify the paper's attachment of an overriding importance to a differential of mere basis points between mutual funds' sales agency

commission rates, even when narrowed to nearly identical funds (e.g. same asset class, performance, strategy, risk profile)

Consultation Paper 81-408 cites investor harm but undertakes no investigation, nor does it list the many other factors within an investor's decision between funds. As a result, the paper also does not delve into what level of importance the investor has placed upon the marginal commission or trailer fee cost within his/her decision.

The paper fails to even discuss what the rate of commission offered by a fund relates to. This includes,

a. the difference in past performance between nearly identical funds within an asset category
b. the difference between the investment strategies pursued by fund managers
c. the inherent importance of non-volatile performance to the investor
d. the importance of fund manager name recognition to the investor
e. the expected holding period for the fund, thus the amortization period inherent to the sales commission

It is therefore difficult to accept Consultation Paper 81-408 allegations of systematic harm to investors is the result of modest differences in sales commission rates when Canadian regulations mandate that all of the above factors be considered by investors before they purchase a managed investment.

New Amounts to be Paid by the Canadian Investor – the impact of Fee-for-Service

Consultation Paper 81-408 will cause the immediate increase annual cost/fees to Canadian investors of between 0.5% and 2.0% or more for all fund/managed assets presently owned by Canadian investors ($1.5 trillion managed assets cited; between $7.5-30 billion/yr in additional costs to Canadian investors).

Because the Canadian investment industry presently does not charge annual fees or additional commissions on client assets invested in managed funds Consultation Paper 81-408 will require investors to immediately begin to pay their regular dealer account charges for these assets. For fee based accounts, managed products will become subject to what is commonly in full service dealers, a 2% annual fee.

Fund managers may or may not reduce their MER by the ½ % trailer for fee-based dealer accounts because they must immediately re-organize their sales, marketing and branding strategies to find new means to, and more directly engage, Canadian investors. (see below, fund managers must undertake and implement new, more expensive marketing costs).

The added investor expense of up to 2% will not change the performance of an asset, it will however, significantly reduce the investor's net investment performance.

If fee-based accounts are discontinued in favour of Consultation Paper 81-408 fee-per-service regime, the existing costs to buy or sell for mutual funds will remain unchanged, but they will be enumerated to the investor by the dealer. Since the up-front fund sales commission for managed assets are much higher than the trading costs investors prominently advertised for exchange traded securities, in all likelihood, the higher commission rate on fund trading slips and the constantly reporting of larger fees for fund holding and asset maintenance activities will inevitably dissuade most investors from buying non-exchange traded investments. (see below, unintended consequences)

The discontinuation of the present fund manager/dealer revenue sharing relationship as envisioned in Consultation Paper 81-408 will make fund investment appear significantly more costly to Canadian investors. The 37% of Canadian households who invest in funds will see between $ 7.5-30 billion drawn from their wealth annually, a charge to investor wealth that risks the survival of fund management in Canada.

Significant Additional Back Office and Compliance Costs

Consultation Paper 81-408 envisions that dealers will be allowed and expected to invoice fund managers to withdraw from the investor's assets under their management, for the activity related charges or structured fees owed to the dealer by that investor.

To meet the fee-per-service proposals of Consultation Paper 81-408's by both fund managers and dealers will have to purchase highly sophisticated invoicing and payment systems.

Dealers

Dealers do not presently possess an invoicing system or sufficiently sophisticated re-imbursement payment monitoring system(s) to address Consultation Paper 81-408's proposed alternative.

It is quite possible that invoicing systems capable of drawing the records of fees charged from the dealer's existing back office account management computerization, and shift them to or between fund managers have not yet been built. Nor are invoicing systems designed to parse an investor's total fees into invoices to be sent to one or more fund managers, identifying specific fund assets to be drawn down by the fund manager. Investor tend to want to draw down more from one fund than another.

While core to Consultant Paper 81-408 fee-per-service proposal is a system for tracking payments invoiced, a system to adjust holding of mutual fund units accordingly, it may not actually exist. Compliance demands and issues increase as well, in that the new balance of holdings may contravene the primacy of K-Y-C.

Certainly, if the dealer is expected by the investor to draw down from a fund that is actually held in another of investor's inter-related accounts at the dealer instead of in one where the fee(s) was generated, such a system does not exist.

If the simpler systems do exist, integrating it with dealer legacy systems and converting the existing system's format to account structures and pricing matrices within each dealer will be prohibitively expensive.

To attempt fund manager invoicing of this complexity using human resources is certainly not within the means of any Canadian dealer.

The cost of a dealer system (automated or human resource based) to fulfill the fee-per-service accuracy sought by Consultation Paper 81-408 is likely to be beyond the financial resources of a vast majority registrant dealers. It will certainly become a regulator-required barrier to entry within the Canadian investment industry.

Fund Managers

Fund managers do not possess the means or systems to handle Consultation Paper 81-408's envisioned a deluge of invoices, let alone invoices that request money from a fund to be transferred into more than one of an investor's related accounts at a dealer. The fund manager is not likely to be aware of the investor's related accounts at the dealer or the relationships. All of the relevant K-Y-C information is presently held by the dealer and fund managers do not possess systems to accommodate and keep current dealer held K-Y-C information.

Compliance at the Fund Manager Level

Consultation Paper 81-408 envisions the discontinuation of contractual arrangements between the fund manager and dealer, but each dealer account invoice inherently arrives at the fund managers back office with a legal obligation to the fund manager, as trustee, for each investor's assets; an obligation to protect those assets from wrongful disbursement.

Therefore the fund management industry will be confronted with the compliance problem of how to ensure that only the appropriate amount of money is being sent to the dealer. This is not Consultation Paper 81-408's simple proposal - fees can be drawn against the AUM under the fund manager – the industry to which it has been proposed faces tough realities for any request for fees from assets under management (AUM) from managed funds.

Designing and building such huge and sophisticated compliance and payment systems, quite probably, is beyond the resources of any fund manager. A required implementation certainly creates a barrier to entry into the Canadian investment industry.

It is safe to say, trailer fees have been the industry's means to avoid these costs and issues. Trailer fees are a proven, simple, and elegant way to deal with a dealer's costs arising from mutual fund investment. A discontinuations will create costs that will ultimately be borne by Canadian Investors, even though none of the costs will enhance net investment performance.

Dealer Compliance Departments

Compliance departments of dealers will have to monitor, test, and supervise fees paid within the expanded matrix of investor activities and account types within every dealer.

Dealers and fund managers will be required to monitor fees and investor costs for compliance purposes in more complex and intricate ways, including the attribution of fees to unrelated fund manager's AUM whose assets are in an investor's related dealer account and the potential need for K-Y-C related rebalancing of asset weightings after fund redemptions have been completed for the payment of fees.

Compliance departments will have to expand significantly in manpower and computerization.

The costs for the compliance systems needed to monitor, test and supervise the invoicing, payment and payment tracking systems to support Consultation Paper 81-408's are presently incalculable, but these too will ultimately have to borne by Canadian investors, who will derive no benefit to their net investment performance resulting from these costs.

Canadian Regulators

To fulfill their mandate to protect investors, all Canadian regulators will be required to monitor and review all fees paid by investors within the envisioned, vastly expanded matrix, including the pricing for all activities in dealers, funds, and managed accounts Regulators will also have to measure the efficiencies and inefficiencies of every fund management back office in order to evaluate "fair pricing" by a dealer.

To meet their investor protection mandate if Consultation Paper 81-408 is implemented, the audit departments of Canadian regulators must substantially expand beyond their present levels of human resources and computerization.

These increased regulation costs must ultimately be passed along to the registrants, who must then attribute these "operational/overhead" costs into the fees charged to the investor. None of these new costs advance Canadian investor wealth creation nor will they increase a fund management's net investment performance.

No Analysis of Regulatory Costs

Consultation Paper 81-408 does not include comment upon or provide insight into the increased cost of regulatory oversight inherent to its proposals. CSA certainly has the means to enumerate and quantify expected regulation costs (software, audit time, staffing, financial, etc.), therefore it is disturbing that Consultation Paper 81-408 omits this information.

Consultation Paper 81-408 proposes major structural change to the business practices and costs that underlie the marketing and sales of managed investment. The Canadian investors deserve a report, in dollar terms, of the both the benefits they can expect to receive and the costs they will bear, from Consultation Paper 81-408's proposal to replace existing fund manager/dealer sales agency agreements.

No Evidence to Support Allegations

Fund Manager's Benefit

Consultation Paper 81-408 cites no evidence, whether from industry analyses or internal CSA investigation, to demonstrate to what degree any specific mutual fund(s), ETF(s) or other managed account(s) gained observable marketing advantage over their direct competition and arose from a particular fund manager/dealer payment structure.

No evidence of Enforcement Actions or Naming of Victims

Although 165 pages in length, Consultation Paper 81-408 alleges that differences in advisor payouts have systemically harmed Canadian investors, but provides no facts, consultant presentations, or enforcement actions to provide the reader with specific offenders or victims (whether individuals or as an identifiable demographic of investors).

The underlying conflict of interest issue was publicly identified during the 1980's, certainly during the intervening three decades the industry should have produced ample fact-sets and records of enforcement that could have been referenced in Consultation Paper 81-408.

It appears appropriate to criticize the absence of enforcement records to support or contradict the point of sale, because in its place, Consultation Paper 81-408 provides a 24 page survey of the demographics of investment holdings and multiyear surveys of the change in holdings of managed product by Canadian investors. These 24 pages are entirely void of insight, or discussion, of point of sale issues, they are totally irrelevant to the issue and should not have been included.

Mischaracterization

Because Consultation Paper 81-408 does make any attempt to identify or reference any of these highly relevant sets of facts, the reader is left without appropriate scope regarding the issue of systemic investor harm, permitting Consultation Paper 81-408 to inherently mischaracterize the Canadian investor as someone who has always been victim, never seeing appropriate information regarding the costs of mutual fund ownership.

Maligning Regulators and Registrants

This mischaracterization maligns, dealers and advisors, as registrants, for failing to abide by regulatory POS requirements and all Canadian regulators who are inherently alleged to have totally and abjectly failed to fulfill their mandate of investor protection.

It is not clear why Consultation Paper 81-408 has issued such a broad maligning of all levels of the Canadian investment industry.

Role for Sales Commission When Investors Want to “Hold Managed Funds for the Long Term”

Sales commission act to motivate the advisor to recommend investors to undertake a regular review to consider culling their worst performing assets. This is a positive for investors as the advisor is seeking to enhance the investor’s net performance over both the near and long term. In these cases, trailer fees, even a differential in trailer fees, is highly unlikely to incent an advisor to not recommend a review of the portfolio, or to recommend an investor retain the higher trailer fee fund even though it is an underperforming asset.

Portfolio reviews

To replace the existing system that inherently promotes both investor review and timely review of their portfolio(s), which is what Consultation Paper 81-408 advocates, and replace it with a “sticker shock” type, “in your face”, barrage of fees, each unique to a specific service (including recommending and assisting with the portfolio review) should appear counter-productive.

Consultation Paper 81-408 does not address the fact that the exact same large commission payment that is not earned by suggesting a portfolio review, becomes new substantial cost to the investor after the investor agrees to first pay for a portfolio review.

Consultation Paper 81-408’s advocacy of precision item by item, fee-per-service, it will require investors to agree up-front to pay for regular and timely portfolio reviews, of costs that cannot be defined because it is inherently unknown as to how many services will be provided within the review, until after the review is completed.

Fee-per-Service, Incenting the Advisor

The above does to begin to address the dealer/investor relation complexities and brand new conflicts of interest regarding an advisor, who is tasked with proposing alternatives to under-performing assets under the advocated structure of fee-per-service in Consultation Paper 81-408. For example, each of the alternative investment proposed represents a separate services and thus its own fee. At what point is the advisor unduly incented by the number of fees he/she can charge for suggesting a further investment alternative or another overview service?

Unlike the proposal of fee-for-service, the present system of fund managers to dealer payments caps what investors pay. No matter how often there is a review, no matter how many alternatives are reviewed, the investor is in control. In the end, there will be one sales commission paid to the advisor, but only if the investor believes a change of assets will benefit his/her future net investment performance.

Unsubstantiated Conclusions and Recommendations

1. Reduction in fund series and in fund fee complexity

Fund series are a result of both a fund managements' attempts to disguise the extensive costs of their fund, designing new ways to present the same costs to an investor in a more palatable manner and a manager's need to innovate "brand extensions".

To an investor who continues to leave assets in the control of the fund manager, there are no differences between the funds in the present form of "series". It is only in a scenario of withdrawal from the fund that the investor must consider the different alternatives in a series.

Recognizing that consumers search for deals, fund managers will continue to seek new ways to make the investor feel that they have a "best" deal or the most "appropriate" alternative. For Consultation Paper 81-408 to pretend that fund managers will not innovate and implement means to appear to make an investor feel they better manage the costs of fee-per-service is either inappropriate or a failure to understand the marketing requirements facing fund managers.

Moreover, there is no limit to the marketing creativity of fund managements. For example, creating a "series" of funds to extend the brand of fund with successful performance, by designing variants to the initial fund's "strategy", permits the launching an entire "series" of funds based upon strategies, rather than amortization structures of advisor payments.

To expect a reduction in series is to misunderstand commerce.

Fee Complexity

Contrary to its conclusion that there will be a drop in fund fee complexity, Consultation Paper 81-408 requires that each dealer create their own payment-for-service matrix. Inherent to its requirement, dealers will have to enumerate reams of unique fees for

- each activity
- for every fund
- for every management back office

- by dealer account
- by product purchase or sale (not all funds at a manager may cost the same to process as a transaction)
- by investment product holdings within the account
- by formats for cash withdrawal or reinvestment
- by size and numbers of partial fund redemptions
- by number of and complexities of K-Y-C compliance supervision

And on and on.

We cannot comprehend how Consultation Paper 81-408 can possibly conclude that their recommendation to eliminate an established system of two-party agreements between fund managers and dealers to be replaced by an unlimited matrix of fees-per-service will decrease fee complexity.

2. New lower-cost product providers may enter the market

Consultation Paper 81-408's proposal for precise fee-for-service matrices will necessitate new, highly sophisticated invoicing and payment systems and will require enormous structural investments by fund managers and dealers alike.

Many registrants presently do not have the capital to undertake these new requirements, thus they will be forced to merge or close. All registrants will have to charge more per year to every investor to repay their required investment.

For new entrants the added costs, systems, relationships, and marketing procedures, all of which will have to be fully in place and operational on "Day one", will be even more prohibitive.

For fund managers, Consultation Paper 81-408's removal of their existing indirect access to investors through advisors will require asset and fund managers to find new, but far less efficient marketing procedures, driving their operating costs higher.

The cost of the fee-per-service matrices will increase the investment, operation and compliance costs of every dealer and make all fund management products appear very expensive. Rather than low-cost, all surviving registrants will be required to charge clients substantially more than they do presently.

It seems highly implausible that "lower-cost product providers may enter the market"

3. Increased price competition/decrease in fund management costs

Price Competition

Consultation Paper 81-408 requires fund managers to cease paying dealers. It is unclear how this promotes "price competition" between funds. At a dealer level, each will have to produce an overbearing schedule of unique fees that cannot be compared at reasonable cost. This too will not promote "price competition".

Decrease in Fund Manager Costs

Consultation Paper 81-408 mandates that fund managers make no payments to dealers except for reimbursements from investor funds. Marketing costs that presently pay for dealer/advisor participation in sales and product support may cease. But, to survive and grow, fund managers must continue to market their products.

Any basic understanding of commerce inherently recognizes that marketing budgets are existential to business; they cannot and will not diminish, if a commercial enterprise intends to sustain itself and grow. The operating cost structure of a fund is not reduced.

Under Consultation Paper 81-408 fund managers will have to investigate new forms of marketing and determine how to anticipate investor portfolio review. Their ability to act at the point of time when an investor will be undertaking a review his/her portfolio is crucial to successful and efficient marketing.

The costs for this will not diminish because of fee-per-service. Managers will have to find a means to entice investors to pay for their fund's inclusion within a portfolio review, then pay for the high purchase cost of the fund and the higher position maintenance costs.

In that Consultation Paper 81-408 only changes the recipient of a fund manager's presently paid marketing dollars, it is unclear how Consultation Paper 81-408 can perceive that operating and marketing costs will be diminished by having a new recipient for the marketing dollars.

Unintended Consequences

1. **Reduced trading on Canadian exchanges and Canadian Debt Markets**

Mutual funds are significant participants in the Canadian securities markets. Part of the trading volume they provide to Canadian markets is driven involuntarily by the purchases and redemptions of their fund units.

The fee-per-service envisioned within Consultation Paper 81-408 transforms the portfolio review into a new, distinct, and separately invoiced cost to investors, which will clearly reduce the number and frequency of reviews, thus portfolio changes. Ultimately this will reduces the trading volume within the Canadian markets, which are already finding themselves increasingly marginalized within the framework of global trading due to its less than significant volume of trade.

2. **Protection and perpetuation of non-performing funds and fund managers**

The fee-per-service envisioned within Consultation Paper 81-408 will clearly reduce the number and frequency of reviews, allowing non-performing funds and assets to remain within portfolios for longer periods. Consultation Paper 81-408 will also make the investor perceive as "costly", the replacing an underperforming mutual fund asset. This clearly protects the incompetent fund managers, who will be assisted by Consultation Paper 81-408's dissuading investors portfolio reviews and denying advisors opportunities to replace them. Inept performing managers will be allowed to continue to charge for their inept performances; to profit at the expense of the competent and to further deteriorate investor wealth.

3. **Creating barriers to entry to new fund managers and dealers**

As previously raised; the need for fee-per-service matrices, invoicing, payment and compliance systems, and the new alternative marketing strategies in all fund managers, each of which will be inherently required by Consultation Paper 81-408, will expand operating costs and skill needed by a registrant exponentially. To any potential, new dealer or fund manager Consultation Paper 81-408 embodies a huge barrier to entry.

Consultation Paper 81-408 might stimulate innovation, creativity, and new business for software companies, however, it will stifle entrepreneurialism within the Canadian securities industry.

4. Reduction of mutual fund investing in Canada

Investors, when regularly faced by the higher commission rates of managed product over the costs to purchase exchange traded or debt market securities, can logically be expected to gravitate to lower commission options. Virtually all investors can model diversification using exchange traded and debt market securities, thus reap immediate cost savings when rebalancing portfolios.

Faced with new costs and less efficiency within the fund manager's marketing and sales process, investors gravitation away from the higher mutual fund purchase commissions will become even more pronounced, even if the investor has asked that the fund be included in their portfolio review. Fund managers will find themselves perpetually at significant and growing disadvantage to exchange traded and debt market securities.

Such a major pertpetual disadvantage can only lead to a substantial reduction in managed fund investing and an inevitable consolidation within the managed fund sector of the Canadian securities industry.

Conclusion

Consultation Paper 81-408 does not cite investor complaints nor any records of enforcement to prove that the conflict of interest created by a fund managers paying dealers (a process renamed to incorporate emotive response; "Embedded Commissions") to prove that there has or is systemic harm to Canadian investors. In fact, there appears to be no evidence, no documents or studies to support Consultation Paper 81-408's claim of investor harm.

Consultation Paper 81-408 simply maligns all Canadian registrants and regulators, openly and without clear evidence.

The recommendations within Consultation Paper 81-408 will create enormous costs for the Canadian securities industry and ultimately the Canadian investor to absorb. It does not demonstrate how or whether the investor will find better net investment performances for their portfolios arising from its recommendations. In all likelihood net investment performance will be harmed.

It is also unknown whether the Canadian investment industry has the human talents, available time, and financial resources to build all of the systems that are inherently required by Consultation Paper 81-408. It is also clear that nothing in Consultation Paper 81-408 promotes more successful net investment performance in Canadian investor portfolios.

Consultation Paper 81-408 does not hold up to scrutiny and it advocates recommendations that will prove exceedingly costly and damaging to the Canadian investment industry.

“Robert Goldberg”