



INVESTMENT INDUSTRY ASSOCIATION OF CANADA
ASSOCIATION CANADIENNE DU COMMERCE DES VALEURS MOBILIÈRES

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President & Chief Executive Officer

September 20, 2011

British Columbia Securities Commission
Alberta Securities Commission
Saskatchewan Financial Services Commission
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
New Brunswick Securities Commission
Superintendent of Securities, Prince Edward Island
Nova Scotia Securities Commission
Superintendent of Securities, Newfoundland and Labrador
Superintendent of Securities, Northwest Territories
Superintendent of Securities, Yukon Territory
Superintendent of Securities, Nunavut

Attention:

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- And -

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Dear Sirs and Mesdames:

RE: Canadian Securities Administrators Notice and Request for Comments on Proposed Amendments to NI 31-103 regarding Cost Disclosure and Performance Reporting (the Notice)

The Investment Industry Association of Canada (IIAC) is writing on behalf of our membership to respond to the request for comments issued on June 22, 2011 by the Canadian Securities Administrators (CSA) on the proposals to implement cost disclosure and performance reporting requirements in NI 31-103 (the Proposed Rules).

This comment letter has been drafted with the assistance of the IIAC CRM Performance Reporting Working Group (the Working Group or we), which consists of numerous members from across Canada, representing a broad cross-section of firms. The industry professionals on this Working Group are knowledgeable and experienced in the wealth management business, and many of them have been involved for numerous years in the rule-making process.

The IIAC has commented extensively on earlier versions of the IIROC Client Relationship Model (CRM) proposals. Most recently, IIAC submitted comments by letter dated March 7, 2011 on the IIROC CRM proposal released for comment on January 7, 2011 (collectively, IIROC submissions) which contains substantially similar provisions with respect to cost disclosure and performance reporting to those in the Proposed Rules. To the extent that the comments in the March 2011 IIAC submission are relevant to the Proposed Rules, they have been reiterated in this submission.

This submission is organized into the following parts:

- Part 1 – Overview
- Part 2 – Questions posed by the CSA
- Part 3 – Comments on the Proposed Rules
- Part 4 – Conclusion

Part 1 - Overview

As the IIAC stated in their IIROC submissions, the members of the Working Group fully support the objective of providing clients with meaningful information regarding the performance of, and costs associated with, their accounts. However, it is necessary to balance the desire to enhance disclosure currently provided to investors with the cost, operational impact and the client experience resulting from making the proposed changes.

To this end, we encourage you to implement the Proposed Rules in a way that allows firms sufficient time to make the necessary changes to their systems – recognizing that both technology and operations will need to be changed – and to manage the client education and communication that will be required upon implementation. In order to

manage this process the Working Group makes the following recommendations.

- That the CSA provide a lengthy transition period - at a minimum, 3 years from the effective date of the Proposed Rules. The CSA may consider a phase-in system with milestones for firms to ensure that rules can be met.
- That the CSA harmonize the implementation timelines that will apply to both the CSA rules and SRO rules. In this regard, we encourage you to work with the SROs to ensure that any required changes to fully implement cost disclosure and performance reporting will only need to be made once. This approach will be both cost efficient as firms will be able to focus resources on implementing the final solutions rather than interim “phases” and, more importantly, result in a better client experience as client statements and materials will not be changing through the process leading to possible client confusion and concern.
- That the SROs should be exempt from the Proposed Rules as they are in the best position to regulate their own members. In the case of the MFDA, they have regulated their members, and in the case of IIROC, they are in the process of regulating their members in the areas of cost and performance reporting. We refer you to paragraph 6 of the Notice and Request for Comment dated June 23, 2011, which refers to the efforts of the CSA to work with the SROs to achieve harmonization in this area. It states that, subject to final approval of the SRO rules, exemptions would be available where the SROs have provided for substantially similar requirements.
- That the efforts of the CSA to achieve harmonization include ensuring that the requirements of the CSA, IIROC and MFDA are not contradictory. This would allow firms who have registrations in more than one category to elect one set of requirements to comply with, resulting in possible over compliance in one or more registration categories, but at least achieving the objective of minimizing the cost of developing and implementing multiple systems.

We have explained these points in greater detail in our comments in Parts 2 and 3 below.

We note that the research which was conducted by the CSA with respect to the Proposed Rules targeted retail investors. We would suggest that the research findings are not necessarily applicable to institutional investors who are more sophisticated and are unlikely to require or rely upon the cost disclosure and performance reporting information contemplated by the Proposed Rules. For example, institutional accounts typically deal with more than one firm and are typically custodial accounts where the registrants do not maintain control over the investment assets. As a result, the firm does not have the same access to the cost information upon which the cost disclosure and performance reporting is based. Accordingly, we suggest that institutional/COD accounts be exempted from the cost disclosure requirements contained in the proposed sections 14.14(5.1), 14.14(5.2), 14.15 and 14.16 of NI 31.103.

Part 2 - Questions posed by CSA

Set out below are our answers to the questions posed by the CSA in the Notice in relation to performance reporting. We have set out the CSA's issue for comment in bold. Our response follows.

2.1 Cost information - the Proposed Rules requires original cost information for each position in an account statement

We have considered the option of permitting the use of tax cost (book value) as an alternative to original cost. We invite comments on the benefits and constraints of each approach to cost reporting, in particular as they relate to providing meaningful information to investors and their usefulness as a comparator to market value for assessing performance.

The Working Group does not believe that the CSA should mandate which form of cost should be used to value securities in account statements. Rather, each firm should be allowed to decide whether to value securities on account statements using original cost or tax cost (otherwise referred to as book value). Allowing firms to choose their own methodology and provide the appropriate disclosure to clients will benefit clients and firms alike as disclosure can be customized to suit the particular client/circumstance. However, a firm should be expected to adequately disclose to their clients how they determine and report cost base. In the event that the CSA does not adopt a flexible approach to reporting, we are of the opinion that tax cost is a more appropriate measure than original cost for the reasons discussed below.

Tax cost is the historical cost being provided to clients by many firms. While it is not insurmountable to ask service providers to develop the methodology to track and populate original cost data in their systems, it will require significantly more lead time to prepare for than the mandated reporting of original cost. Since the Proposed Rules also require members to disclose the cumulative realized and unrealized capital gains/losses on the client's account as an element of the account activity disclosure reporting, tax cost will be needed to calculate these positions. The requirement to also report original cost will actually result in the requirement to track and report two costs and could be confusing to clients to see different costs on different reports.

The primary protocol for transferring positions via ATON is to transfer at tax cost where available. There has been a significant investment made by many of our members to integrate the account transfer applications with CDS-ATON functionality. Tax cost fields in most systems report tax cost to ATON. Therefore, firms do not provide original cost when transferring a retail account from one firm to another. Inability to properly track original cost on securities held in accounts transferred between firms will limit the ability of the industry to comply with original cost base reporting requirements. As noted above, the cost and development time for firms and/or CDS to add original cost on firm to firm transfers is expected to be significant.

At present, not all firms consistently provide cost information on non-registered accounts. With no mandatory requirement for IIROC members to provide cost information on all

external transfers, it will be difficult for firms to report original cost on all accounts unless information is provided by the client.

Furthermore, there are products where original cost may not be appropriate or relevant information to the account holder. NHA mortgage backed securities that pay a portion of the investor's original principal each month or mutual funds that pay a return of capital regularly or periodically are examples, and are described below.

Example 1: NHA mortgage backed securities

NHA MORTGAGE BACKED SECURITY BANK OF N.S. POOL #97010698

CUSIP: 62922ZLB1

Issue Date: 03/01/2009

Maturity Date: 08/01/2011

Assuming an initial investment of \$10,000.00, this becomes the original cost amount. The security's current market value as at 02/07/2011 would be \$2,836.50 based on a price of 28.365. With each month's payment, the system marks down the cost of the investment by the principal portion of the monthly payment. In this example, displaying original cost alongside market value may give a less sophisticated investor the impression their investment had performed poorly whereas tax cost reflects the monthly reduction in principal paid since the bond was issued.

Example 2: Mutual Funds

While mutual funds are typically an investment commonly referenced where original cost is the most appropriate value to display to an investor, many fund managers supplement fund generated income and/or capital gains with return of capital to meet their distribution requirements. Any amounts paid out as return of capital should be offset against the investor's original cost base (and provides consistency with their tax reporting). There is no known process for firms to do this other than reporting the fund's cost base. Canadian mutual fund manufacturers universally report tax cost today.

To conclude, it should be noted that clients will be receiving information with respect to net amount invested in the performance report. As a result, it is of more benefit to the client to use a figure which is consistent with their tax reporting, rather than introduce a new cost figure for which it is necessary to explain why it is different than the cost figure used for tax reporting. As such, we suggest that if an approach is mandated, the preferred approach would be tax cost as opposed to original cost when reporting cost information for each position in a client account statement.

2.2 Cost information - guidance on determining market value

Is the guidance provided on determining the market value of securities in section 14.14 [client statements] of the Companion Policy useful and sufficient? Please indicate if there is additional or different guidance needed. We are particularly interested in your comments on the guidance related to the valuation of exempt or illiquid securities where there are no quoted values available.

The Working Group supports the guidance that where the market value of a security is not quoted on a recognized exchange or marketplace and cannot be determined by reference to quotes that are available through brokers, the CSA would expect firms to have a valuation policy that is consistently applied and based on reasonable measures. We note that the CSA has provided guidance only in the case where market value of a security is not quoted on an exchange. There are concerns that the minimal guidance provided does not contemplate other instances where securities cannot be valued such as illiquid securities. As such it would be more helpful to provide additional guidance, for example, a reference to real estate trusts which are valued quarterly and illiquid securities, to name a few examples. If more guidance is not provided, then a minimalist approach is recommended i.e. only a requirement that firms have a valuation policy applied consistently, so that firms are not restricted in establishing their own valuation policies.

The second and third paragraph of the Companion Policy describes the process for when market value cannot be determined. It should be made clearer that those securities for which market value is determined through the firm's valuation policy are not required to be noted as having no value.

2.3 Performance reports

We acknowledge that there are unique features to group plans offered by scholarship plan firms (group scholarship plans). We invite comments on whether the proposed account performance reporting requirements should apply to accounts invested in group scholarship plans or what other types of performance reporting would be useful to clients of group scholarship plans in lieu of the proposal outlined in the Rule.

We are not aware of any reason to exclude clients of scholarship plan firms from receiving cost disclosure and performance reporting information.

Part 3 - Comments on the Proposed Rules

3.1 Charges

Pursuant to section 14.2 (4.1), a firm would be required to deliver a report describing the total amount of operating and transaction charges, separated by type and in aggregate every 12 months for each account. We believe that a better approach would be for the rules to permit a firm to present the information, both here and under sections 14.15 and 14.16– Performance Reports, either by account or by client portfolio. In many cases, client accounts represent discreet, but complementary investment strategies. For example, a client's RRSP account may contain primarily fixed income securities while that client's cash account may contain blue chip equities, and the performance of these two accounts will be different. In our view, the information that the client will be interested in receiving is the overall performance of their portfolio rather than the performance of the individual accounts.

We note that in the Notice the CSA states that they have not made any changes to section 14.14 [*client statements*] of the Proposed Rules in this publication as a result of the comments made in response to a previous CSA Notice. Specifically, the CSA request for feedback on what securities should be reported in account statements included in the June 25, 2010 Notice and request for comments on proposed amendments to NI 31-103. We appreciate that the CSA is continuing to consider what securities should be included in the reporting requirements and we would be happy to continue to work with the CSA on this issue. Having said that, it would be difficult to incorporate into the reporting model that is being proposed information that is not contained on the firm's book and records such as information on client name holdings or other off-book transactions.

3.2 Definition of “original cost” - section 1.1

This definition of original cost incorporates the definition of operating charges which includes all charges to the account, regardless of whether they are directly applicable to a security. For example, a client may be charged an annual custody fee for an RRSP, which is paid out of the cash account not the RRSP account. To incorporate these items into original cost would require constant readjustments to the original cost of each security. Moreover, it would be necessary to estimate the charge that should be attributed to the security as each charge arises. This would not allow clients to maintain their own records as they would be unable to reconcile the confirmation slip of the trade with the original cost data the firm provides. Further, since section 14.2 (4.1) includes the requirement that the firm provide information to the client of what “charges” are paid out of the account, the goal of providing this information to the client is achieved without including it in the original cost information. If the CSA feels it necessary that all charges be included in a performance analysis, then this could be treated as a separate item.

We would also request clarification on whether “charges” includes those items prescribed by a governing body such as U.S. withholding taxes, and if so whether they would be considered to be "transaction charges"? In our view, to avoid confusion to the clients, it would be more appropriate to include charges such as withholding taxes in the annual tax summary, rather than as a line item in this report.

3.3 Definition of “transaction charges” - section 1.1

We would like confirmation that items such as foreign exchange spreads are not transaction charges or operating charges.

3.4 Disclosure of charges - section.14.2 (CP) and section 14.2(3.1) (NI)

Timing of disclosure

In reference to disclosure of charges, the Companion Policy states that "While general information on the charges is appropriate at account opening, a firm must provide more specific information as to the nature and amount of the actual charges when it provides services or advises on a trade."

While we are supportive of disclosing charges to clients, we query the need to add this point of sale disclosure requirement in light of the existence of a current strong disclosure

and suitability regulatory regime. For example, for mutual funds, clients already receive a prospectus, a fund facts documents and a trade confirmation. All of these documents already provide the charges disclosure. Furthermore, the CSA is already working on dealing with mutual funds fund facts disclosure at point of sale which has been and continues to be subject to strong industry consultation. We urge the CSA to continue following that fund facts consultation process for point of sale disclosure of charges on mutual funds and refrain from dealing with point of sale disclosure on mutual funds in the Proposed Rules.

In addition, while the Working Group agrees that disclosure is a suitable objective and recognizes that the Companion Policy allows for the pre-trade charges to be disclosed orally by the representative, we are concerned about the viability of setting up appropriate compliance procedures to audit that this disclosure has been provided to the client.

It would seem that further deliberation is required to avoid establishing a requirement that we cannot audit appropriately and we would welcome guidance on how this requirement is expected to be met. We appreciate that representatives are required to document suitability and other discussions with the client and we strongly believe that a suitability analysis should be sufficient without the need to add further more detailed charges disclosure. The client will have received the firm's fee schedule upon the opening of the account, which provides information on what the charges will be. As well, the client receives the confirmation slip after a trade, which clearly indicates the charges that applied to the trade. In addition, the client will get the annual cost report contemplated by the Proposed Rules. In the event that the client has an issue with the general information provided initially and the specific information provided on the trade confirmation, the client has the opportunity to discuss this with the representative. We feel that this combination of disclosure satisfies the intent of the Proposed Rules.

Deferred sales charges (DSCs)

With respect to the special attention that DSCs are given, it should be noted that it is particularly difficult to disclose what the actual DSC will be before a mutual fund security is sold to a client and that there is no automated method of determining the DSC. Moreover, DSCs are variable and may not be paid if the client only redeems that portion of the fund which is DSC exempt (typically 10% redemption annually is permitted). Given the strong existing disclosure framework for DSCs in prospectuses and in fund facts, we question the need to require disclosure of the DSC a third time

Nonetheless, if the CSA would still like to see this disclosure made then we suggest that section 14.2 (3.1)(b) be revised to require disclosing to clients that there may be a DSC charge and providing disclosure in percentage terms of the approximate amount of the deferred charge that would apply to all types of mutual funds. This would avoid some of the complexity of providing specific disclosure (e.g. the DSC would be different if a client holds a mutual fund for 1, 3, 5 or 10 years.) We believe that the CSA already contemplates this type of a proposal in the Companion Policy but would like clearer confirmation to this effect.

Trailing commissions

The Working Group notes that the requirement to disclose trailing commissions at the point of sale is equally problematic as the requirement to disclose DSCs. As with DSCs, trailing commissions are equally variable and unknown at the client level as fund companies only generate trailing commission reports based on a representative code. As with DSCs, disclosure of trailing commissions is provided to each investor in the fund facts document which is sent with the trade confirmation and the CSA will deal with point of sale delivery of fund facts in its phase 3 of the point of sale for fund facts proposal which is subject to public consultation. For other products, a notation on the trade confirmation that a trailing commission is payable by the fund company should suffice. We have concern that the CSA suggestion of providing an estimate when the dollar value is unavailable may cause further confusion as it will be difficult to ensure that the estimate is reasonably accurate, given the variables in charges, products and the length of time the product is held by the client. In addition, as discussed above, there is the problem of the availability of sufficient space on the confirmation to provide detailed information. Nonetheless, if the CSA would still like to see this disclosure made then we suggest that section 14.2 (3.1)(b) be revised to require disclosing to clients that there may be a trailing commission charge and providing disclosure in percentage terms of the approximate amount of the trailing commission that would apply to all types of mutual funds.

Further, clients of order execution only accounts trade in reliance on their own strategies, not pursuant to recommendations of registered firms. They do not consult or inform registered firms prior to entering the trade, especially when related information is available in product materials (e.g. prospectus, fund facts). Therefore, while execution only firms use trailing commissions to cover costs such as operational costs, trading fees, maintenance of the account etc., we request that an exemption from this section be provided to order execution only accounts as we do not believe that such firms have an obligation to disclose trailing commissions charges on products solely selected by the client.

3.5 Benchmarks - sections 14.2(2)(m) and 14.17 (NI) and section 14.16 (CP)

The Working Group agrees that the use of benchmarks should not be prescribed. For a benchmark to be meaningful to a client's individual account, a firm would be required to group accounts into specific categories, (as managed accounts tend to be) and to find a benchmark appropriate to reflect that category. This would make it difficult to account for an investment which might fall outside of the broad categories, but is still suitable for the client, or originates from the investor, or is an investment which the client wishes to maintain, or reflects appropriate changes to the account due to a change in the client's objectives. The possibility of variation from benchmarks is to be expected; as a result the Companion Policy states that only widely available benchmarks should be utilized. Further, for clients' investment portfolios that have identified the nominal rates of return in the financial plan, the objectives of these portfolios are to meet the nominate rate of return, not an index return. Investors who are interested in benchmarks would already know how to access them and would be aware of their limitations. Non-managed retail investors will question why the performance of their investments varies from a widely available benchmark which could lead to advisors attempting to explain how a

benchmark established by an independent rating agency does not relate to the client's portfolio objectives. Furthermore, determining meaningful benchmarks that could apply across a broad spectrum of non-managed accounts, with changing positions and objectives, and storing and auditing the standards and accuracy under which they are created, is a daunting task for firms to administer.

Additionally, indices and the type of index, do not represent prudent portfolio management investing. While the index may be conventionally accepted as “the market”, it does not represent prudent diversification as it is not “managed”.

While acknowledging that the use of benchmarks is not being prescribed, the Working Group is concerned that including a discussion of what must be disclosed when benchmarks are used within the Proposed Rules represents a view by the regulator that benchmarks should eventually be prescribed. Accordingly, the Working Group suggests that the reference to benchmarks be deleted. However, if the provisions are maintained, there should be exclusion in section 14.17 for managed accounts and permitted clients who consent, consistent with the provisions of section 14.15.

As a drafting comment, please note that the section on benchmarks in the Companion Policy should be removed from section 14.16 and included as a new section 14.17.

3.6 Trade confirmation – deferred sales charge - section 14.12(1)(c)

Pursuant to section 14.12(1)(c), the DSC must be shown on the trade confirmation for a security with a DSC feature. Currently trade confirmations disclose redemption fees, but may not distinguish between DSC and short term trading fees. It is difficult to ascertain the amount of DSC since this amount cannot be known at the time of the purchase as the DSC is determined by the timing and quantity of redemption of the investment. Please clarify in the drafting if it is sufficient that the security be identified as “DSC” or whether further information would be required.

3.7 Information to be delivered to clients - section 14.2(4.1)

We note that the Proposed Rules addresses the issue of charges by reference to charges relating to an account, rather than to a client. As stated earlier, sometimes the fees are paid outside of that specific account, for example RRSP fees. Tracking these fees when they are paid in a different account than the one to which the fee is applicable would be extremely difficult, if not impossible. In our view, the Proposed Rules should permit these charges to be aggregated for the client across all of the client's accounts.

Section 14.2(4.1)(a)

We do not believe that disclosing the operating charges that a client *may* have to pay is appropriate in a cost disclosure statement. This statement should be reserved for charges that are actually incurred. Furthermore, disclosing operating charges that a client may pay is already required to be disclosed under section 14.2(2)(f) and we believe that the duplication is unnecessary and may be confusing to clients.

Section 14.2(4.1)(b)

This proposed section requires disclosure of operating charges relating to the account paid by the client. We have a number of concerns with this proposal. It should be noted that certain operating charges that relate to the account that are paid by the client may not be levied by the registrant but by a third party that may or may not be a related party to the registrant. For example, custodian fees may be charged and invoiced by a third party custodian. In such a case, while the fee may be debited from the client's account with the registrant, we do not believe it is appropriate to require the registrant to disclose this operating charge on their cost disclosure statement to the client. This is because the client would have already received an invoice from the third party, i.e. the custodian, and would be confused by receiving further disclosure on the same cost. In addition, it would be inappropriate to require the registrant to report on an operating charge that it neither levies nor bills for.

While we understand that the CSA's objective is to disclose all costs to the clients on one statement we believe such a need is undermined by the fact that the client may experience confusion resulting in inaccurate tax reporting as a result of this approach. Clients use their account statements to submit certain costs relating to the account in their tax filings. Clients may accidentally over-submit costs since such costs will be disclosed on the registrant's statement and on a separate statement provided by the actual service provider. It is for these reasons that we recommend that the CSA limit the disclosure of operating charges on the client statement to those charges that have been levied by the registrant whether or not charged out of the account.

With respect to this section, we would like confirmation in the Companion Policy that the breakdown of operating costs does not extend to registrants such as portfolio managers who charge one fee for all services rendered. Such registrants should be able to disclose the one fee without engaging in an artificial exercise of breaking down the fee.

Section 14.2(4.1)(c)

See comment on section 14.2(4.1)(b) above. We also recommend that this section be limited to transaction charges levied by the registrant. This is because transaction charges not levied by a registrant are levied by a related party or a third party and billed separately to the client so that the client is already obtaining full disclosure of costs relating to their account albeit not in one statement. We think the CSA's objective to provide complete cost disclosure in one account statement is undermined by the reality of resulting client confusion of potentially receiving cost reporting on one item twice.

Section 14.2(4.1)(e)

We query why the CSA feels the need to duplicate already existing disclosure requirements in NI 31-103 in this section. For example, this proposed section would capture the need to disclose referral fees paid to a registrant. The need to disclose referral fees is already mandated in NI 31-103. For other types of fees paid to a registrant, NI 31-103 already requires registrants to disclose the existence of such fees under the conflicts of interest sections in NI 31-103. As a result, we suggest that this section be deleted as it is duplicative of other existing NI 31-103 requirements. While the intent to provide clients with fulsome cost disclosure in one statement is noble, the CSA must weigh this benefit against the industry wide costs of meeting this proposed requirement (i.e.

duplicating work efforts, cost and operational inefficiencies) especially given the fact that clients are already receiving this cost disclosure albeit not in one statement.

Section 14.2(4.1)(f)

Please clarify how registered firms are expected to identify the securities that are subject to DSC on account statements. Is it sufficient if the names of securities include “DSC”?

Section 14.2(4.1)(g)

In the case of trailing commissions, current reporting from mutual fund companies is provided to firms on a representative code basis and not on a client or account basis. As a result, registrants do not have the means to determine what the trailing commissions earned on a client or account basis are. In order to comply with this proposed requirement, the CSA will need to mandate that fund companies provide reporting of trailing commissions on a client or account level as opposed to a representative code. This is a very ambitious and costly proposition one that we do not think is necessary in light of the existing regulatory framework of suitability and KYC assessments and the disclosure regime found in prospectus and fund facts. In addition, under NI 31-103 registrants would have to disclose the general existence of trailing commissions. As a compromise, we believe that it should be sufficient for registrants to disclose the existence of trailing commissions and to provide an approximate percentage of trailing commissions i.e. 0.5-1.5% (which is consistent across all mutual funds). In doing so, we believe that the CSA would strike a balance between transparency for investors and not unduly burdening registrants.

3.8 Account statements - section 14.14

Section 14.14 (5.1)

Certain securities are not priced on a monthly basis or there are subtleties related to the security which cannot accurately reflect the correct average or original cost. Where these securities are detected by the registered firm an option to suppress the value on the account statement must be included to not mislead the client in terms of gain/loss. For example, Corporate Actions where the FMV has not been disclosed before the account statement is generated, segregated funds, GIA's, LPU's etc.

Section 14.14(5.2)

The section should allow the use of blank or null values with disclosures on why the value was suppressed on the account statement where the registered firm has reason to believe the value to be incorrect on the transfer. If a market value is displayed, there is no incentive for the client to provide the correct original or average cost for the asset transferred and will also not provide the client with a clear understanding of how their asset is performing.

Please reference the comments in the introductory section of this letter suggesting that the CSA exempt institutional accounts from the provisions of these sections.

3.9 Performance reports - section 14.15

IIROC firm members service a wide array of client segments, each with different needs and expectations. The CSA proposal, however, mandates performance reporting for nearly all client accounts, regardless of whether or not clients want, need or are willing to pay for the information. The costs required for firms to implement the performance reporting proposals will be material. Ultimately, it is the firms' clients that bear these costs. For many clients, these additional costs will outweigh any of the perceived benefits from mandated performance reporting.

We note that various types of accounts are excluded from the requirement of receiving performance reports. In particular, subsection (5) excludes permitted clients, of whom institutional accounts are a subset, if a waiver is obtained. To expand upon the comments made in the introduction above, the value of performance reporting to institutional accounts is negligible and unnecessary. These types of accounts are sophisticated, usually provide their own investment strategy and would likely have their own mechanisms for tracking performance. The cost/benefit of providing this information to institutional accounts is not warranted. Obtaining waivers would be a time-consuming and non-productive exercise. We strongly urge harmonizing the exclusion for permitted clients under NI 31-103 and the exclusion for institutional clients in the IIROC Proposed Rules.

Self-managed (direct investing) accounts should also be excluded. The type of clients who operate a self-managed account are often more sophisticated and knowledgeable and do not always hold all of their investable assets in their self-managed account which renders performance irrelevant. As well, the services they receive are generally restricted in nature, priced competitively by individual requirements or offered as value added service. Providing a service of performance reporting at a significant cost to the firm would be inconsistent with this type of basic account.

It is also suggested that this requirement can be fulfilled, in the case of managed accounts, by reporting on a quarterly basis, as that is currently the practice for many dealers, rather than requiring a report every 12 months.

For these reasons performance reporting may make servicing some accounts uneconomical. Firms will have to be more critical with respect to the types and sizes of accounts they continue to administer, possibly raising the minimum investable assets limits for clients. A possible unintended consequence of the performance reporting requirement, therefore, is that fewer individuals may continue to have access to the guidance of a full-service advisor at an IIROC regulated firm. To address this concern, the IIAC strongly recommends that a minimum portfolio size threshold be established for which performance reporting would not be mandated by the CSA. The threshold recommended is \$100,000 and we would recommend that this be valued annually and reporting be provided in the following calendar year.

Lastly, we seek confirmation that the requirements only apply to clients who reside in Canada.

Performance Reports – delivery to clients

The Working Group suggests that section 14.15 (1) be clarified to indicate that delivery of the report can be made in electronic form, unless specifically requested in hard copy by the client. Many clients now already receive their account statements, as well as other financial information, in electronic form and would not be inconvenienced by this form of delivery. This would reduce the cost of compliance by the amount that would have been incurred to send this information to all retail clients. The same rationale would apply to the other information which is required to be sent to the client under section 14.2 (4.1).

3.10 Content of Performance Reports - section 14.16(1)

Section 14.16(1)(f)

Subsection (f) refers to performance reporting “net of fees”. The Proposed Rules has primarily discussed “charges” to the account, rather than fees, which is not a defined term. It is suggested that there be consistency and clarity of language. Another approach would be to specify that this reference to fees is to investment management fees only.

We also suggest that you consider that a firm may present this calculation using either net or gross of fees, provided that full disclosure is made to the client. It should be noted that the CFA Institute Global Investment Performance Standards advocates presenting this calculation gross of fees, but allows either. For greater clarity, the Companion Policy could note the acceptability of globally generally accepted performance calculation methodologies inclusive of Internal Rate of Return, Modified Dietz and Dietz methods, all of which are widely used by IIROC members and the investment community.

With reference to section 14.16(3), we suggest that the CSA allow some flexibility for firms to report over regular periods to the client and not mandate specific time periods for disclosure as this could be very onerous on firms and more importantly may not meet client’s specific needs.

3.11 Implementation Periods and Costs

The IIAC believes that the implementation and ongoing costs associated with cost disclosure and performance reporting will be significant across the industry. It does not appear that either the CSA or IIROC fully appreciate the extent of the expenditures that will be required. Longer and harmonized transition periods should be adopted as they will help contain the cost of implementation. It is suggested that the requirements be effective at least 3 years after implementation date.

Firms have many competing priorities that need to be addressed and generally priorities are set at a minimum 12 months in advance. Firms require sufficient time to ensure that the performance information they will be providing to clients is accurate and free from errors. The process of ensuring that the quality of the information supplied is meaningful will be a huge undertaking. Many firms currently provide performance reporting to only a small segment of their clients and the work involved in expanding this to all clients will be extensive. As such, to produce this information for all accounts, with data that the

Member Firms are comfortable delivering to clients, will take at minimum 24 to 36 months to fully organize the information, adjust systems and refine processes.

The IIAC Working Group suggests that the CSA consider the use of a phase in system for implementation of the performance reporting requirements. This could allow firms to test systems and ensure that rules can be met or that firms are on their way to meeting the requirements. Milestones could be set to ensure that firms are progressing in meeting a 3 year deadline which would provide the CSA with comfort that firms were working towards implementing the requirements. The IIAC would be pleased to work with its firms in organizing such a phase in system.

There appears to be lack of consistency in the implementation provisions. In Appendix A of the amending instrument, Item 18 provides that section 14 is to be implemented 10 years after the implementation date. In Appendix B, the coming into force schedule referred to in Appendix A indicates a number of different transition periods after implementation date for different provisions of section 14; for example, original cost information and performance reporting is stated to be effective 2 years after implementation date. Subsection 14.15 (1) provides that performance reporting must be delivered to the client every 12 months, which effectively means that the first report could be 3 years after implementation date. In addition, the schedule provides that 3, 5, and 10 year performance reporting is to be done 3, 5, and 10 years after implementation date. Effectively, this means that the provisions regarding performance reporting (and effectively cost disclosure) would cover periods beginning with the implementation date, not 2 years thereafter. The IIAC does not believe that the CSA intended that these performance period prescriptions refer to a time period prior to implementation date plus 2 years. We suggest that the drafting be addressed to resolve these issues. The CSA likely intended that these provisions only apply on a prospective basis and it is suggested that this be stated directly.

It should be noted that section 11.6 of NI 31-103 has a record retention requirement of 7 years. This is inconsistent with a 10 year reporting requirement, as obviously records will have to be kept longer than 7 years.

Subsection 14.15 (1) allows flexibility as to when firms will deliver the first performance report, up to 12 months past implementation date. This will mean that clients who have accounts at different firms will receive reports covering different time frames. Although the IIAC is not suggesting that all firms be held to the same reporting periods, or even a calendar year period¹ it might be beneficial to prescribe that the reporting periods conclude at a calendar quarter, which would allow for some consistency and convenience for clients. In addition, some provision should be made which would allow firms to change the period of reporting. For example, a firm may start with a time period other than year end, but wish to move to a calendar year reporting period in the future.

¹ While conceding that a report ending at December 31 is useful, this would impose a considerable burden upon firms who have numerous other year end obligations, in addition to being just prior to the RRSP selling season.

3.12 Sample Account Performance Report - Appendix D

While we appreciate that this is just a sample form, we suggest a number of changes. As an initial comment, this report is organized by account, rather than by client. There should be the opportunity to provide reporting on an aggregate basis for the client. This would alleviate some of the issues discussed above relating to charges in one account but applicable to another account for the same client. We suggest that there be separate line entries for dividends and interest so that these can be cross-referenced to tax reporting the client receives. Under rates of return, the phrase “fees” is used. This should be made consistent with the Rule which refers to “charges”.

3.13 Content of Relationship Disclosure Information – CP section 14.2

The introduction to this part requires that “registered individuals spend sufficient time with clients as part of an in-person or telephone meeting to adequately explain the written documents that are delivered under subsection 14.4(2)”. While registered individuals already discuss some of the aspects of this required written disclosure with their clients, to mandate verbal disclosure in addition to the written disclosure seems excessive. As stated above under part 3.4, this creates a requirement that is difficult to audit appropriately. Surely the written document provides the necessary disclosure as is the case in other areas of securities law such as prospectus delivery, leverage disclosure, derivatives risk disclosure, etc. We would respectfully suggest that current requirements with respect to know-your-client and suitability obligations, and the proposed written disclosure documents are satisfactory.

Part 4 - Conclusion

In closing, the IIAC and our members support the principles behind the proposed cost disclosure and performance reporting rules; however, we believe that there can be improvements and clarifications in the rules, including allowance for the time and expense involved in implementing them.

The IIAC has a serious concern regarding the lack of harmonization in the rules and also in the proposed implementation periods, in similar proposals put forth by the CSA, IIROC and the MFDA. The CSA should exempt SRO members from the Proposed Rules as the SROs are best situated to regulate their own members. In the case of IIROC, Proposed Rules in the area of cost disclosure and performance reporting have been proposed and await CSA consultation.

Rules with a common regulatory focus need to be harmonized as much as possible and to the extent it makes sense to achieve efficiencies and reduce compliance costs. Regulators should focus their efforts on achieving these harmonized standards as it is not apparent why different standards and different implementation periods are imposed on different registrants.

The IIAC would be happy to work with the CSA to improve the proposed cost disclosure and performance reporting rules to ensure an appropriate model is developed which will enhance the experience investors have when working with our member firms.

Yours sincerely,

A handwritten signature in black ink, appearing to read "J. Mann". The signature is written in a cursive style with a long, sweeping underline.