Ian C.W. Russell FCSI
President & Chief Executive Officer

May 30, 2013

Mr. William S. Rice
Chair and Chief Executive Officer
Alberta Securities Commission

Ms. Brenda Leong
Chair and Chief Executive Officer
British Columbia Securities Commission

Mr. Don Murray
Chair
Manitoba Securities Commission

Mr. David G. Barry
Chair and Chief Executive Officer
New Brunswick Securities Commission

Mr. Douglas J. Connolly
Superintendent of Securities
Service Newfoundland and Labrador

Ms. Sarah P. Bradley
Chair
Nova Scotia Securities Commission

Mr. Gary MacDougall
Superintendent of Securities
Government of Northwest Territories

Mr. Louis Arki
Superintendent of Securities
Government of Nunavut

Honourable Howard I. Wetston
Chair
Ontario Securities Commission

Ms. Katharine Tummon
Superintendent of Securities
Consumer, Corporate and Insurance Services
Office of the Attorney General

Mr. Mario Albert
President and Chief Executive Officer
Autorité des marchés financiers

Mr. Dave Wild
Chair
Financial and Consumer Affairs Authority

Mr. Fred Pretorius
Superintendent of Securities
Yukon

Dear Sirs and Madams:

Re: Request to Permit Time-Weighted Performance Reporting under National Instrument 31-103

As you know, the Investment Industry Association of Canada has expressed support publicly for the principles and many requirements of the Client Relationship Model (CRM). This has now been released in final form as the Canadian Securities Administrators (CSA) *Notice of Amendments to National Instrument 31-103 Registration Requirements, Exemptions and Ongoing Registrant Obligations and to Companion Policy 31-103CP Registration Requirements, Exemptions and Ongoing Registrant Obligations (Cost Disclosure, Performance Reporting and Client Statements)* [the Reporting Rule]. We are grateful that the CSA phased in the effective dates for implementing different parts of the Reporting Rule in view of the extensive technology, policy and procedural changes, as well as the staff training and client communication, that are required for CRM compliance.

With respect to the performance reporting component, we agree with the CSA that providing a rate of return to clients is beneficial; however, our members remain concerned that mandating use of only one among two credible return calculation standards – a money-weighted rate of return (MWRR) – will disadvantage investors. We have argued consistently that member firms should have the option of applying either the MWRR or time-weighted rate of return (TWRR) methodology and we sought to meet with Staff this past March to discuss our reasons further. The majority of clients of member firms offering portfolio performance reporting provide the rate of return using the TWRR method. Therefore, while we know the Reporting Rule is final, we are taking the unusual step of requesting that the CSA amend the Reporting Rule now to give member firms the option to select **either** the MWRR **or** the TWRR methodology to measure portfolio performance, for the reasons detailed below. Our comments are provided not from the perspective of

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the position of our member firms, whose views were conveyed to Staff in previous submissions, but rather on the basis of independent, investor-focused public sources, including CSA-commissioned performance-reporting research by The Brondesbury Group (2010) and Allen Research Corporation (2011).

Rationale for Flexibility of TWRR or MWRR Reporting

As the CSA have noted, the objective of the Reporting Rule is to provide clients with information regarding the performance of their accounts. The challenge to providing meaningful reporting is that there are several factors – or inputs – involved in this determination: some market-related, some driven by the advisor (e.g., assistance with investment selection, tax-efficient strategies[1]) and some by the client (e.g., when and how much is contributed or withdrawn). The investment literature is clear that no single performance calculation methodology – MWRR or TWRR – is the best way of measuring rate of return in all circumstances.

The CSA-commissioned research lists two key findings, one a preference common to all investors and another particular to investors with greater holdings.

1. **All investors:** CSA research shows that *all* investors, regardless of portfolio size, assess the performance of their portfolio based on the amount of money in dollars that they have gained or lost.[2] For this reason, advisors talk to their clients about the dollar value of assets each client might need and the contributions he or she should aim to make, for example, to maintain his or her desired lifestyle in retirement. Advisors, as well, will provide a target or assumed market rate of return (note that this rate of return would be TWRR-based). In the case of retail investors who best understand amounts gained or lost expressed in dollars, CSA research confirms that a rate of return percentage is relevant, but suggests that, rather than using technical terms with clients, it could "… be easier to explain the main difference between time-weighted and dollar-weighted rates of return and state which method is used."[3] Indeed, the Reporting Rule expresses the regulators' expectation that advisors will discuss with clients the impact on returns of the timing of when they contribute and withdraw from their portfolio, implying that using a TWRR approach can be made understandable. And TWRR is currently used, and will continue to be used, by mutual, exchange-traded and index-linked funds, as well as by benchmarks.

2. **Investors with greater assets:** The same CSA research notes that among those with greater amounts of money invested, there is a small preference for using a benchmark, which the report authors suggest means that more sophisticated investors are more capable of using more complex methods for assessing returns. More sophisticated and perhaps financially literate clients can understand the effect of large, unevenly-timed deposits and withdrawals on their personal rate of return and typically would find the TWRR methodology preferable to the extent that a TWRR:
   - Allows comparisons with other advisors/asset managers;
   - Simplifies contrasts with returns on alternative investments in and outside Canada;
   - Permits appropriate comparisons to well-known benchmarks such as the S&P and FTSE; and
   - Is calculated using clear criteria – the Global Investment Performance Standards (GIPS) – which are championed by the CFA Institute and whose benefits are 'consistent and comparable performance measurements built on ethical principles so that clients can be sure that the historical performance they receive is both complete and fairly presented.'

Over time, it is not evident that there will be a major difference between the results of either method used uniformly. Material on the Investor Education Fund 'Get Smarter about Money' website articulates the benefits of regular, even payments through good times and bad[4] and we believe that this approach, if followed, would reduce differences between TWRRs and MWRRs.

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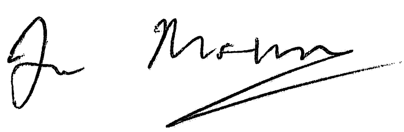
What is certain, however, is that the dollar value change in the worth of the investor's holdings, which CSA research has shown to be most important to investors of whatever knowledge and holdings' size, will be identical. More importantly, some investors accustomed to TWRR reporting will not understand why their returns have changed at a point in time, possibly dramatically, by the mandated move to MWRR percentages. This would be further complicated, where an MWRR is provided for the return on the account, because TWRRs will apply to individual account investments. Even if there is time to prepare clients used to TWRR for the change to MWRR, many may be concerned by the loss of an unbroken history of their investment returns. We believe that the possibilities of both client confusion and heightened concern are at odds with the CSA's tagline, which includes "maintaining confidence in the markets".

While the Reporting Rule allows a registrant *also* to include TWRR percentages, we understand that the option to provide both is unlikely to be adopted by registrants and would be contrary to one of the CSA's purposes, that is, avoiding duplication of work. This is not only due to the cost of maintaining two separate performance tracking systems, but also because, from a client's perspective, it would add to the number of percentages on account statements, possibly confusing rather than providing clarity for the investor.

As mentioned, we understand that the Reporting Rule is now final, however, we believe improvements can be made that will allow it to better achieve its intended objective of providing meaningful information to clients on the performance of their investments. We therefore would like to arrange for a number of senior executives of our member firms to meet with you in the near future to discuss providing registrants with the option of using either a money- or time-weighted rate of return, before firms invest in rate-of-return information systems they think may not be appropriate for their clients.

Yours sincerely,



[1] Finance Canada estimates an after-tax yield improvement of about 1.5% on assets held in registered form as compared to when the same assets are held in non-registered form (Department of Finance Canada, *Statistics on RPP/RRSP Participation and Savings*, March 31, 2010, footnote 23).

[2] Report*: Performance Reporting and Cost Disclosure Prepared for Canadian Securities Administrators*, Dr. Edwin L. Weinstein, The Brondesbury Group, September 17, 2010.

[3] Report: *Canadian Securities Administrators Performance Report Testing*, Allen Research Corporation, February, 2011.

[4] For information on pre-authorized debits and dollar-cost averaging, refer: http://www.getsmarteraboutmoney.ca/en/managing-your-money/planning/investing-basics/Pages/when-is-it-a-good-idea-to-set-up-a-pad.aspx; note that under the MWRR method, investors may think they will be rewarded for making larger investments during periods of greater price increases, however, this may emphasize efforts to time the market when an important lesson of investing is how risky trying to time the markets can be ("Timing is everything but you can't time the market", Jonathan Satovksy, *Forbes*, June 18, 2012).

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