

# The manager who gave back his fees



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The mutual fund industry is going to *hate* this.

Investors will be angry that they don't see more of it.

Unhappy at the returns he has generated for clients, money manager Francis Chou is refunding almost all the management fees collected by his Chou Europe fund since it opened for business in September, 2003.

"We have not made money since inception," explained Mr. Chou, a widely respected investing figure whose financial career began in an investment club he formed in 1981 with six Bell Canada co-workers. "I don't like negative numbers long term. Short term – one year, two years or three years, if you do badly that's fine. But long term, you want to make sure you're making money for your unitholders."

What a difference there is between Mr. Chou's tiny, eponymous fund company and his big-boy competition. He looks out for unitholders. They look out for shareholders.

Investors are lax about understanding the cost of owning mutual funds, which means they may not realize that the fees charged by funds don't typically vary with results they produce for investors. Among the 15 largest equity and balanced funds by assets, losses for the 12 months to Feb. 28 range from 16 to 38 per cent. Don't waste your time waiting for fee re-



Francis Chou, who is refunding almost all the management fees collected by his Chou Europe fund since it opened for business in 2003: 'It was the right thing to do.' JIM ROSS FOR THE GLOBE AND MAIL

## The Wisdom of Francis Chou

### THE MARKETS

"I think the economy may go south somewhat, but the stock market may not go along. The stock market tends to be a leading indicator by nine months to a year. So it could go up if the economy goes south."

### PICKING SECTORS

"All sectors are cheap. Right now, we're just trying to wade into some financials."

### FURTHER OPPORTUNITIES

"Everything is depressed, but corporate bonds are more mispriced than equities."

### HOW LONG A COMMITMENT INVESTORS SHOULD MAKE TO HIS FUNDS

"I would prefer 10 years."

bates from any of them.

Mr. Chou's company, **Chou Associates Management**, has five funds in its lineup and their losses in 2008 ranged from a better-than-average 17.6 per cent for Chou Asia to a lower-than-average 44 per cent for Chou Europe.

As of the end of February, Chou Europe had lost a compound average annual 6.2 per cent since inception. This is the result that prompted him to ask the Ontario Securities Commission for guidance on how to do what may never have been attempted before by a fund company: Rebate all fees taken in by a fund throughout its history.

"It was the right thing to do," Mr. Chou said from his office in the Toronto suburb of North York, which is way off Bay Street.

In fact, Mr. Chou has rebat-

ed fees on a limited basis several times in the past. Most recently, he decided to waive roughly 77 per cent of the management fees collected last year from Chou Bond, a fund that holds high-yield corporate bonds. In the mid-1990s, he waived 19 months' worth of fees taken in by Chou RRSP. In 1990, he waived fees for Chou RRSP and his flagship fund, Chou Associates.

These moves are costly, even for a small firm like Mr. Chou's. About \$700,000 extra will be available in Chou Bond so it can be invested for the benefit of unitholders, and a total of \$547,000 will be put back into Chou Europe.

It's not only unique for a fund company to give back fees it has collected, it's also difficult because of the need for regulatory, legal and ac-

counting advice. "When you go and give back money, you sometimes have to jump through hoops to get it done," Mr. Chou said.

What eased the way was an unusual clause in the prospectus for the Chou family of funds. It states that the matter of waiving management fees entirely or in part is reviewed annually at the discretion of the manager without notice to unitholders.

Management fees are what fund companies pay themselves from their mutual fund returns to cover the costs of running a fund. Some companies have fixed their management fees so they can't rise, others leave themselves the flexibility to charge more.

Mr. Chou's take: "I look at it more that you have to earn that fee rather than have it given to you. If I feel I earned it, I take it."

Here's something else Mr. Chou takes – responsibility for his investment returns, both good and bad. In 2008, the results were largely bad as a result of his value investing approach of seeking beaten-down stocks with the potential to rebound. In the financial crisis that blew up last year, these stocks have been pounded still lower.

In his annual report to clients, Mr. Chou wrote about how he was worried about irresponsible lending and the U.S. housing market, but did not foresee how severely the financial system would be hurt when the bubble burst.

"And so, based on the information we had in 2007, we purchased some stocks at prices that, in hindsight, were too high," Mr. Chou wrote. Go contrast that with the explanations you're going to be seeing from other fund companies as they explain the fiasco of 2008.