

July 27, 2022

Submitted via email

Alberta Securities Commission
Autorité des marchés financiers
British Columbia Securities Commission
Financial and Consumer Services Commission (New Brunswick)
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Nova Scotia Securities Commission
Superintendent of Securities, Nunavut
Ontario Securities Commission
Securities Commission of Newfoundland and Labrador
Registrar of Securities, Northwest Territories
Registrar of Securities, Yukon Territory
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island

Attention:

Me Philippe Lebel
Corporate Secretary and Executive Director, Legal Affairs
Autorité des marchés financiers
Place de la Cité, tour Cominar
2640, boulevard Laurier, bureau 400
Québec (Québec) G1V 5C1
Fax: 514-864-6381
consultation-en-cours@lautorite.qc.ca

The Secretary
Ontario Securities Commission
20 Queen Street West
22nd Floor, Box 55
Toronto, Ontario
M5H 3S8
comment@osc.gov.on.ca

Mr. Tony Toy, Policy Manager
Canadian Council of Insurance Regulators
National Regulatory Coordination Branch
25 Sheppard Avenue West, Suite 100
Toronto, Ontario
M2N 6S6
ccir-ccrra@fsrao.ca

Re: CSA and CCIR Request for Comment – Total Cost Disclosure Reporting Requirements

Dear Sirs and Mesdames:

The Investment Industry Association of Canada (the “IIAC”)¹ welcomes the opportunity to provide feedback on the CSA and CCIR Joint Notice and Request for Comment – Proposed 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* and Proposed CCIR *Individual Variable Insurance Contract Ongoing Disclosure Guidance Total Cost Reporting for Investment Funds and Segregated Funds* (together, the “Initial Proposals”).

The IIAC is the leading national association representing investment firms that provide products and services to Canadian retail and institutional investors. Our members manufacture and distribute a variety of securities such as mutual funds, exchange-traded funds, segregated fund contracts and other managed equity and fixed income funds, and provide a diverse array of portfolio management, advisory and non-advisory services.

The Initial Proposals require various components of the financial industry to develop coordinated solutions. Consequently, the IIAC has ensured our comments reflect a holistic response from the investment industry, and specifically represents the views of investment fund managers (“IFM”), investment dealers, and insurance intermediaries.

GENERAL COMMENTS

The IIAC and our members support the objective of improving investors’ understanding of their investments and, specifically, providing meaningful cost disclosure associated with investing. The Initial Proposals represent the CSA’s first written proposal for stakeholders to review and provide comments. The investment dealer community, which would be responsible for the majority of systems builds to produce the client disclosures, has not been previously consulted by the CSA on the potential impact to their clients and their operations².

We do not believe that the CSA’s policy objectives can be achieved through the Initial Proposals, and as currently conceived, they may result in significant harm to investors and the capital markets.

In order to develop appropriate total cost reporting requirements, the CSA should complete a comprehensive cost-benefit analysis that takes into consideration the financial costs to industry participants, which will ultimately be passed on to shareholders and investors and outlines the unintended consequences of proceeding with the Initial Proposals reflecting feedback from the comment process. The analysis should align with the joint IOSCO-OECD recommendation³ that

“...regulators gain a full understanding of the problem that consumers or investors face before designing a solution; taking the context of financial decision making into account; conducting small-scale pilot and field tests before implementing and scaling up initiatives; evaluating outcomes rigorously...”.

We believe obtaining this information prior to proceeding further is critical and therefore the IIAC would be pleased to lead the effort to collect industry costs that would be incurred to implement the Initial Proposals. We would also appreciate the opportunity to work with the CSA to capture investor feedback

¹ See www.iiac.ca for more information.

² The IIAC responded to the MFDA’s 2018 consultation but has not been consulted otherwise on the total cost reporting.

³ The Application of Behavioural Insights to Financial Literacy and Investor Education Programmes and Initiatives, IOSCO-OECD report, May 20, 2018

that is meaningful and includes the value of the additional disclosure information weighed against the financial costs they and/or shareholders would incur to have this information.

We also ask the CSA to publish its latest Behavioural Insights research that was used to inform the CSA's Initial Proposals. The CSA's Initial Proposals appear to contradict earlier public behavioural research on the value of certain additional financial information disclosure. Specifically, research⁴ conducted by the Ontario Securities Commission Investor Office which has clearly cited that, "...relying on extensive disclosure to achieve better consumer outcomes was a flawed approach." The research continues, stating that "even when traditional regulation successfully identified a problem...it frequently used ineffective measures (such as very detailed disclosure to correct market flaws) to address them."

Further, we believe the international experiences are instructive regarding the difficulties incurred by the financial industry to comply with third-party cost disclosure. In the U.S., the SEC considered adopting similar disclosure requirements, however, after consideration of the implementation challenges and financial costs for both industry and to investors, the SEC proceeded with an alternative approach to enhancing investment fund disclosure⁵. In the UK, firms were required under MIFID II to provide third-party costs and charges, however, during post-rule reviews, the Financial Conduct Authority ("FCA") noted firms were seeking to comply, but the required third-party data was not always available. The Australian Securities & Investment Commission ("ASIC") noted their legislative framework for fees and cost disclosure was designed to strike a balance between: (a) ensuring that consumers and market professionals have useful information; and (b) you [firms] being able to practically comply with the fees and costs disclosure requirements⁶.

KEY RECOMMENDATIONS

1. The CSA should conduct a robust cost-benefit analysis considering the costs to investors and industry participants and the unintended consequences of proceeding with the proposed disclosure reflecting feedback from the comment process.
2. Revise section 14.14¹ to remove the requirement to disclose the fund expense ratio on the Account Statements.
3. Dealers must be able to rely on information provided by the IFMs.
4. The CSA should develop a Total Cost Disclosure Stakeholder Committee to facilitate timely dialogue between the regulators, and stakeholders to support rule finalization.
5. The CSA should work with stakeholders to develop achievable implementation timelines to ensure clients are provided with accurate and meaningful information.

⁴ Behavioural Insights, Key Concepts, Applications and Regulatory Considerations, OSC Staff Notice 11-778, March 29, 2017

⁵ Shareholder Reports and Quarterly Portfolio Disclosure of Registered Management Investment Companies, Investment Company Act Release No. 26372 (Feb. 27, 2004).

⁶ ASIC RG97 <https://download.asic.gov.au/media/5801438/rg97-published-28-september-2020.pdf>

PROPOSED SECURITIES AMENDMENTS

The Initial Proposals for the securities sector (the “Proposed Securities Amendments”) would require new elements to be included in the Account Statement and Annual Report on Charges and Other Compensation (“Annual Cost Report”). We will be discussing these two deliverables separately, as we have specific comments related to each client disclosure document.

Unlike CRM2, which was a large-scale development requiring significant human and financial investment by dealers, the Proposed Securities Amendments require the dealer to provide data to their clients that they do not manage or control. This reality informs our comments.

The cost and effort required to implement the Proposed Securities Amendments will be far more complicated than it was for CRM2, given the obligation for dealers to obtain accurate data outside of their sphere of control.

ACCOUNT STATEMENTS

Recommendation: Remove the requirement in section 14.14 to disclose the fund expense ratio (“FER”), stated as a percentage, on the Account Statements.

We do not believe that the proposed new elements for Account Statements outlined in section 14.14 provide meaningful information to investors. The Account Statements are designed to provide clients with pertinent information about their trading activity during the month or quarter, as applicable. The CSA has not articulated the investor benefit of including the fund expense ratio, stated as a percentage, on the Account Statement, nor has the CSA balanced the potential benefits against the financial costs.

The FER is based on a yearly ratio and does not align with monthly or quarterly disclosure. As a result, we do not believe including the FER on Account Statements will increase client comprehension, and in fact risks creating further investor confusion. The proposed required information would not include critical context to the fees (i.e. is that percentage average?) and the client would not be able to determine if the FER provided value in relation to the fund’s performance.

Disclosure of ongoing cost information is most beneficial when an investor is making purchase decisions. Fund Facts provide detailed MER and TER data and are required to be provided to clients in advance of a purchase of an investment fund. For those clients with an advisor, section 14.2.1 *Pre-trade disclosure of charges*, requires the advisor to disclose to the investor if there are investment fund management expense fees or other ongoing fees that the client may incur. As well, ongoing costs are a factor the advisor must take into consideration when making a suitability determination under section 13.3.

It is not clear from the Initial Proposals if a cost-benefit analysis was completed that takes into consideration the various cost disclosure information currently contemplated by the Initial Proposals. With respect to the Account Statements, we do not believe there are sufficient benefits to justify the significant financial costs of implementation. The MFDA’s 2021 *Improving Fee Disclosures for Canadian Investors*⁷ research found that “adding a column with MER to account holdings tables does not have an

⁷ Click [here](#) for the MFDA’s June 2021 Research Report.

impact on core comprehension” and that overall, “our research suggests that including the MER in account statements *may have a small* positive impact on investor comprehension”.

We believe the inclusion of the FER, stated as a percentage, could have negative unintended consequences. The prominence of investment funds’ ongoing fees, when costs for other products are not included, and no performance information is included, could negatively influence investor behaviour. Clients may consider selling products that are providing meaningful returns and contribute to the client’s ability to achieve their financial objectives. A suitable portfolio could include a variety of products, such as passive ETFs, actively managed funds, individual securities etc., and associated costs for the products will necessarily be different. Without this context and performance data, the client may focus on cost, to the exclusion of other relevant factors when evaluating their portfolio, which will not lead to informed financial decisions.

In addition to the lack of clear investor benefit, the percentage will not necessarily be accurate at the individual client level. A series of funds does not have a uniform daily cost of ownership. The MER may be overstated as clients may qualify for a reduced MER based on householding, or a management fee rebate. Further, fee-based products would have a lower MER than what is disclosed as the fund’s overall MER. As well, since the MER and TER are annualized ratios, applying them daily will not necessarily be representative of how the fund is incurring expenses over time (e.g., trading expenses may be heavier in some months and lighter in others). The MER and TER are disclosed at least 60 days after the period end. The daily cost per unit would be based on these ratios and applied to units held by clients for a different period. Therefore, the calculated cost may not be a reasonable approximation of the actual cost incurred.

The proposed data elements may be operationally prohibitive for IFMs to provide to dealers within a time period required to produce monthly or quarterly statements. In many instances there may be thousands of data points individual IFMs have to transmit daily to dealers based on the number of funds and series they manufacture. We believe monthly or quarterly statements should be based solely on data elements that are within the control of the dealer.

Finally, the inclusion of the FER on the account statements is unnecessary, as the more precise dollar amount is proposed to be included in the Annual Cost Report, where there is performance context and comparison to other products’ expenses such that clients can more fairly determine value.

We recommend that the requirement in section 14.14 be revised to require the Account Statement include a notation, similar to the example in Annex G, footnote 1, referencing the indirect costs of investment fund ownership and directing investors to refer to Fund Facts, MRFPs and/or Financial Statements that are all publicly available for more information. This will serve as a fee reminder and the documents referenced will have explanations of the fees in plain language and can provide some historical performance information for context. Further, the ongoing fee reminder will not impact the dealer’s ability to provide accurate and timely Account Statements to their clients.

ANNUAL COST REPORT

The IIAC supports the principle of providing clients with additional investment fund expenses information on the Annual Cost Report. However, there are a number of issues that must be addressed in order for the IFMs and dealers to be able to provide streamlined, accurate information to clients.

1. Dealer Reliance on IFM Information

Recommendation: Dealers must be able to rely on information provided by registered IFMs. Proposed section 14.17.1 and the corresponding 31-103CP language should be removed.

It is the IFM who has direct access to accurate and complete data required to determine the fund expenses required in the Initial Proposals and it is the dealer who must provide that information on the Annual Cost Report. A core requirement in the Initial Proposals must be total dealer reliance on fund expense information provided by a registered IFM. The IIAC agrees with the language in the 31-103CP stating that “dealers are required to rely on information provided by registered investment fund managers pursuant to 14.1.1.” The IIAC strongly supports the inclusion of this requirement in section 14.1.1, *Duty to provide information*.

Despite the statements indicating that dealers can rely on information provided by IFMs, proposed section 14.17.1 (2) would reverse that onus. Dealers would have to assess all data provided from registered IFMs for completeness and reasonableness to ensure it is not misleading to a client.

Complying with 14.17.1(2) would be extremely onerous for dealers and require significant resources, as it would require a manual assessment of all information before it is inputted in the Annual Cost Report. For example, if dealers were required to compare a static percentage of the MER on a Fund Facts or ETF Facts where available, against the information provided by the IFM that may be in dollars and client specific.

The CSA must also consider this requirement against the number of products and thousands of accounts that dealers have, as well as the backdrop of reporting timelines to complete the Annual Cost Report.

If information is provided by a registered IFM, who has obligations under NI 31-103, and is regulated by the CSA, the dealer must be able to have confidence that it is the most accurate information and is compliant with the Initial Proposal.

If the required information is not provided by an IFM, there is no registered IFM, or the IFM is a non-Canadian investment fund, then a disclosure should be provided in the Annual Cost Report noting that no information is available, as the dealer cannot reasonably research its accuracy.

Further, the Initial Proposals should be revised to add a safe harbour for dealers relying on information provided by registered IFMs.

2. Prescribed Reporting Timelines

While we appreciate the intention of the flexibility in section 14.1.1. for IFMs with respect to the delivery of the required information provided in the Initial Proposals, it is not operationally feasible for IFMs and dealers to potentially have individually set dates to distribute information. We do recognize that there may be variation based on the product as to how the information is delivered to dealers (i.e. Fundserv, CDS, other vendors, etc.) but there must be a uniform standard of what information is required to be provided by the IFM to the dealer, and when that information must be delivered. The requirement for IFMs to provide accurate and timely data to dealers must take into consideration dealers’ current timelines for reporting to avoid disruption of the dealer’s current infrastructure, as dealer production of Annual Cost Reports is not segmented based on products held by customers. Any delay by IFMs to deliver

the complete and accurate information to meet production timeframes would impact delivery of all client reporting, including for those that did not invest in investment funds.

The IIAC would like to work with the CSA to develop a standardized timeframe for reporting prescribed information which reflects the recommended changes.

3. Standardized Data

We recommend the 31-103CP *Division 1 Investment Fund Manager* section be revised to remove reference to “An investment fund manager must work with the dealers and advisers who distribute fund products to determine what information they need from their investment fund manager in order to satisfy their client reporting obligations.”

The rules must set out the required data that IFMs need to provide dealers. There cannot be discrepancies between what information IFMs provide. While there may be a need for variation based on investment fund product type (i.e. conventional mutual funds, ETFs, prospectus-exempt funds, scholarship plans and labour-sponsored funds), there must be consistency for the same products. Further, the client will benefit from having standardized data elements.

The IIAC would like to work with the CSA and other stakeholders to standardize the form of data to be provided to dealers.

4. Fund Expense Ratio

Recommendation: We recommend that the MER alone be used to calculate the fund expenses for the purposes of the Annual Cost Report.

IIAC members understand the objective of the Initial Proposals is to provide enhanced cost disclosure to clients. In response to Annex A, Question 2, we believe in most instances, the MER is the most significant ongoing investment fund cost. We support the use of the MER.

The TER is typically a small portion of fund expenses and fluctuates periodically due to the fund’s trading activity. It is important to understand that the TER is not applicable to all investment funds, such as fixed income funds, as trading costs are captured in bond selling prices and are not charged separately as a commission. Thus, all bond fund TERs are reported as nil in Fund Facts reports, and the MER would equal the proposed FER. Further, some products are not valued daily – if there is no NAV calculated, the TER cannot be calculated. For ETFs, closing price is dictated by the secondary market. As a result, closing price could be at a discount from NAV or a premium of NAV.

In addition, the Initial Proposals would mandate that the FER calculation to be the same regardless of the type of investment fund product. However, the proposed required disclosure does not work for all products; for example, for foreign funds (i.e. Luxembourg funds that are distributed in Canada) costs are not comparable, due to fund currency and other considerations.

While we do appreciate the desire for consistent calculation methodologies, the Initial Proposals must be responsive to necessary variations by product type to ensure there is accurate, timely data.

With respect Annex A, Question 4, we support the use of NAV in the calculations. Further, we believe the NAV input, which is net of fees and expenses, is the fair and accurate representation of true cost.

5. New Investment Fund Products

The rules should not apply to new investment fund products until they have operated for 12-months and there is an established MER and TER. Since there would be no MER available, it would be extremely onerous to require the IFM to determine cost information prior to the 12-month period. New, innovative products should be encouraged. Costly administratively burdensome requirements for the IFM to determine the fund expense ratio, prior to an accurate MER, will lead to a reluctance to launch the products and limit innovation.

Further, under NI 81-106F1 *Contents of Annual and Interim Management Report of Fund Performance*, performance is not to be reported for funds less than 12 months' old and the data would be without this vital context.

6. ETFs (and closed-end funds)

The Initial Proposals should differentiate between conventional mutual funds and ETFs in terms of what information is required to be provided to the dealer.

ETF IFMs have stated they are only able to provide historical average MER and TER figures. However, there is no current infrastructure through which the ETF IFMs can provide even this limited data to the dealers. These products are traded on an exchange and information is not transferred between parties on Fundserv, which serves to transmit information for mutual fund transactions. ETF IFMs and dealers will need to coordinate to develop new infrastructure through a third-party vendor, not subject to regulatory oversight. This is a significant, costly undertaking that will need to be co-ordinated by potentially hundreds of individual parties (all dealers and ETF manufacturers). Once a vendor is selected, then the parties will be able to establish an accurate implementation timeline.

In addition, dealers would also have to build additional infrastructure to automate calculations to determine the personalized ongoing costs for the client and coordinate with their own vendors who produce the client reports. This is another significant build for dealers and their vendors. Dealers and vendors are unable to estimate the scope of the project as it is unknown how and in what format the information will be passed on by the ETF IFMs.

There is no clear precedent for the builds contemplated in this proposal to provide the required information for ETFs. Consequently, we strongly question the feasibility of the proposed implementation dates.

As discussed below, the IIAC would like to work with the CSA (through a Total Cost Disclosure Stakeholder Committee) to discuss realistic timelines.

7. Other products listed in Annex A Question 1 (excluding ETFs)

There are currently also unique challenges for IFMs and dealers to provide the required information for prospectus-exempt investment funds, scholarship plans, and labour-sponsored funds outlined in Annex A, Question 1.,

Prospectus-exempt investment funds: We believe prospectus-exempt investment funds should be excluded from the scope of the Initial Proposals. There is no requirement pursuant to NI 81-106 for prospectus-exempt mutual funds to calculate the MER. It would be burdensome to require these funds

to produce reporting that they have been specifically exempted from to produce MERs to comply with the proposed requirements. There is concern that additional administrative costs for these small funds would result in higher MERs. In addition, dealers would not currently have access to the required information and as noted in previously our response, are unable to determine IFM data points such as MER.

Scholarship plans, and labour-sponsored funds: Information for products such as scholarship plans, and labour-sponsored funds is generally not transmitted through Fundserv and dealers do not have current access to the data. We understand that members of Fundserv are considering adding these products to the Fundserv build, to facilitate information exchange between the IFMs and dealers for compliance with the Initial Proposals. If accurate information to dealers in a timely and accessible manner can be provided through Fundserv, then we support inclusion of these products.

However, as noted, there is no current infrastructure to support the transmission of data between the IFM and dealer and if these products are not included on Fundserv, the dealer will not have access to the required information. As noted above, the dealer must be able to rely on information provided by the IFM and it is not feasible for the dealer to conduct due diligence to gather data. If the IFM is unable to transmit the information, the dealer cannot be required to report on the products.

The reference to foreign investment funds is not clear. If the intent is to refer to IFMs that are not unregistered (i.e. that the CSA does not have jurisdiction to mandate compliance with NI 31-103), then we believe products distributed by those IFMs should be excluded. The dealer must have reliable, accurate data to include on client reports.

8. Non-individual Permitted Clients

The IIAC appreciates the continuation of the existing exemptions for non-individual permitted clients (i.e. institutional investors under IIROC rules). We believe that the exemptions in 14.14.1(6) and 14.17(5) should be expanded to include “overflow accounts” where a non-individual permitted client opens additional related accounts, however, these “overflow accounts” would not satisfy the financial threshold required.

In addition, we suggest that certain accounts be captured in the exemptions, including but not limited to:

- Health and welfare trusts (distinct entities under the *Income Tax Act (Canada)*);
- Unions and union-related benefit plans;
- Multi-employer benefit plans;
- Some foundations and registered charities;
- Some overflow pension accounts (associated with pension plans, but not pension plans themselves);
- Supplemental employee retirement plans;
- Disability plans;
- First Nations trust vehicles (i.e., for government monies); and
- Retirement Compensation Arrangements.

PROPOSED INSURANCE GUIDANCE

The IIAC agrees with the distinctions made between the Proposed Securities Amendments and Proposed Insurance Guidance with respect to the role of registrants/insurers. It is appropriate for the insurer to provide the reporting to the clients (policyholder) directly. As noted in Appendix K, the insurer already provides certain cost and performance information directly to the client (policyholder). While many IIAC dealers are considered insurance intermediaries, in numerous cases there is no intermediary equivalent that could provide the information to the client. To ensure consistency, it is preferable for the insurer to provide the information in all instances.

IIAC's insurance intermediaries believe this standardized disclosure will be beneficial for clients. We are encouraged by the commitment for insurance and securities registrants to implement in lockstep as many clients have both insurance and securities products in their portfolios.

We do not have comments on Annex B or the template reports, as the insurance intermediaries do not have the data or the requirement to produce the client reports.

TOTAL COST DISCLOSURE STAKEHOLDER COMMITTEE

Recommendation: Create a Total Cost Disclosure Stakeholder Committee to facilitate timely dialogue between the regulators, stakeholders and vendors to develop a final rule.

Given the significant operational challenges associated with the Initial Proposals, the number of different registrants impacted, and the infrastructure required to be developed, it is imperative to have an industry stakeholder committee that can engage in problem solving dialogue with the regulators. We believe this committee should be struck prior to rule finalization to discuss critical data elements and timelines. We also recommend including the Investment Funds branches of the AMF, BCSC, OSC and other provinces who are involved with fund and ETF disclosure. Once rules are finalized, discussions will need to continue as operational challenges arise during the build and development phase.

IMPLEMENTATION CONSIDERATIONS

Recommendation: The CSA should work with stakeholders to develop achievable timelines to ensure clients are provided with accurate, meaningful information.

While IFMs, dealers and vendors are currently examining what is required to implement the Initial Proposals, there are still various unknowns with respect to critical data elements and it is not possible to begin meaningful systems builds until rules are finalized. The costs associated with system changes are significant and it is not responsible to incur those costs until feasible, attainable requirements are determined.

Further, there are several complex initiatives that will impact the availability of human resources required for the related IT system builds. For example:

1. Shortening the settlement cycle to T+1
2. CDS Modernization Project (potentially impacting transmission of ETF data)
3. Fundserv Development Project

It is not only a matter of dealers, IFMs or vendors expending more capital to meet a deadline. Rather, there are a limited number of qualified experts to manage and run these projects.

Thank you for your consideration of the concerns raised in this response.

Sincerely,

Laura Paglia
President & CEO