

## **Notice relating to the findings of a review of the consistency of information presented in investment fund offering and continuous disclosure documents**

### **Context**

As part of its investment fund oversight program, the Autorité des marchés financiers (the “Authority” or “We”) reviewed information presented in investment fund offering and continuous disclosure documents for consistency (the “Review”).

Under section 13 of the Securities Act, CQLR, c. V-1.1, the prospectus must provide full, true and plain disclosure of all material facts relating to the securities issued or proposed to be distributed. Information consistency is key to providing clear and unambiguous disclosure to investors.

By means of this notice, the Authority wishes to share the principal findings from the review and to communicate the areas for improvement it identified.

### **Objectives and scope**

In this review, the Authority analyzed the information presented under various items of the offering and continuous disclosure documents of a sampling of mutual funds (the “Mutual Funds”) for consistency. The selected Mutual Funds are managed by various investment fund managers headquartered in Québec (the “IFMs”) and invest in a range of asset classes.

We accordingly compared the information disclosed in the prospectuses, the fund facts documents (the “Fund Facts”), the management reports of fund performance (the “MRFP”), and the financial statements of the Mutual Funds.

We assessed the consistency of the information presented by the Mutual Funds under the following elements:

- Fund name
  - Type of fund
  - Investment objective
  - Investment strategies
  - Risks of investing in the fund
  - Assets effectively held in the portfolio
  - Reference index
  - Who should invest in the fund

### **Summary of findings**

Observations were communicated to certain IFMs when, in the Authority’s opinion, a disclosure deficiency could have an impact on an investor’s investment decision or when a violation of the current regulations was found. Discussions were then held with those IFMs so that they could state their positions.

The principal findings of this review are:

- All the Mutual Funds invested their assets in accordance with their investment strategies
- 21% of the Mutual Funds presented discrepancies between certain disclosed elements
- 29% of the Mutual Funds provided long, complex or imprecise investment strategies descriptions
- 21% of the Mutual Funds presented issues related to the determination of an appropriate reference index
- 14% of the Mutual Funds presented charts that differed between the MRFP and the Fund Facts.

## **Principal findings and areas for improvement**

### **I. Discrepancies between certain disclosed elements**

While the information included in the offering and continuous disclosure documents of the Mutual Funds was generally consistent, we noted certain discrepancies in the information presented—in the fund name, type of fund, investment objectives and investment strategies, for example. The main discrepancies relate to the geographic regions and level of market capitalization of the securities a Mutual Fund may invest in. In the case of one Mutual Fund, for example, the investment type and objectives presented investments in North American securities, whereas the name and the item “Who should invest in the fund?” presented investments in Canadian securities only, which seems to be a discrepancy between these different sections.

Moreover, certain characteristics of the Mutual Funds that were presented in their names or investment objectives were not described in detail in their investment strategies. We wish to reiterate the requirement to describe under the simplified prospectus sub-heading “Investment strategies” “the process by which the mutual fund’s portfolio adviser selects securities for the fund’s portfolio, including any investment approach, philosophy, practices or techniques used by the portfolio adviser or any particular style of portfolio management that the portfolio adviser intends to use.”<sup>1</sup>

#### *Areas for improvement*

- Investment fund managers should ensure that information is consistent between all the items in the various offering and continuous disclosure documents, particularly with respect to the geographical diversification and market capitalisation of the securities the mutual fund may invest in.
- Considering that the elements presented in the name and investment objectives of a mutual fund are fundamental with respect to the nature of the mutual fund, it would be appropriate to provide information thereon in the investment strategies, as mentioned previously.

### **II. Long, complex and imprecise investment strategies descriptions**

We also noted that the descriptions of some of the investment strategies analyzed were long and/or used technical financial language. When investment strategies descriptions are long and the information presented is highly complex, it may interfere with an investor’s comprehension of the strategies. In this respect, the Authority wishes to reiterate the requirement set out in subsection 1 of section 4.1 of Regulation 81-101 respecting Mutual Fund Prospectus Disclosure, CQLR, c. V-1.1, r. 38: “A simplified prospectus, annual information form and fund facts document must be prepared using plain language and be in a format that assists in readability and comprehension.”

Moreover, some Mutual Funds, mainly of the “balanced” type, had investment strategies that presented little information on the target allocation of assets, thereby allowing them to invest in a broad range of assets, both in terms of types of assets and in terms of geographical regions. Subsection(4) of Item 7 of Part B of Form 81-101F1 Contents of Simplified Prospectus stipulates that the Item “Investment strategies” of the simplified prospectus must “[s]tate whether any, and if so what proportion, of the assets of the mutual fund may or will be invested in foreign securities.” We also wish to emphasize that we consider a clear description of the types of assets a mutual fund may invest in as assisting in investors’ comprehension.

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<sup>1</sup> Paragraph (b), subsection (1), Item 7, Part B of Form 81-101F1 Content of Simplified Prospectus.

#### *Areas for improvement*

- Issuers should pay particular attention to the length and level of complexity of the descriptions of their investment strategies and should use clear language to assist in readability and comprehension.
- Specifying the investment ranges with a target weight by type of asset and by geographic region may constitute relevant information to be included in the investment strategies.

### **III. Determination of an appropriate reference index**

We noted that for the purposes of fund performance comparisons in the MRFP, most of the Mutual Funds used an index, or a combination of indexes, corresponding to their investment strategies and covering assets classes in proportions similar to those of their portfolios. Meanwhile, other Mutual Funds presented general indexes that did not cover all the assets held in the portfolio. Although there are a number of ways to compare a fund's performance and the performance of one or more reference indexes, we wish to reiterate the requirement to present a comparative analysis presenting all the facts relevant to investor comprehension and that "explains clearly any factors necessary to make the comparison fair and not misleading[...]"<sup>2</sup>

We also noted that the reference index used to establish the level of risk of certain Mutual Funds, as indicated in their prospectus, sometimes differed from the reference index used in the "Annual compound returns" section of the most recent MRFP. In light of their distinct purposes, the regulations offer the possibility, when warranted, of disclosing a reference index in the MRFP that is different from the one used to determine the risk level of the mutual fund. In such a case, the investment fund manager should be able to explain his or her decision using a financial analysis demonstrating that different reference indexes are used in the investors' interest to facilitate their comprehension.

#### *Areas for improvement*

- Where more than one index is used on an aggregated basis to compare a fund's returns in the MRFP, it is suggested that their weightings be reviewed periodically to ensure that they are similar to the allocation of the assets in the portfolio.
- Where the reference index presented does not cover all the assets in the portfolio, it is suggested that the difference between the reference index and the investment strategies be indicated and that adequate explanations be provided regarding the relevance of the chosen reference index.
- Where the same reference index is not used in the prospectus and the MRFP, investment fund managers should provide adequate explanations regarding their decision to present different reference indexes.

### **IV. Charts presented in the MRFP and the Fund Facts that do not agree**

Some Mutual Funds displayed charts in the MRFP that presented a different breakdown of their investments than the one presented in the charts included in their Fund Facts. In accordance with Instruction 11 under Item 3 of Form 81-101F3 Contents of Fund Facts, the charts presented in these two offering and continuous disclosure documents must be the same.

#### *Areas for improvement*

- Investment fund managers must ensure that the charts presented in the MRFP and the Fund Facts are the same.

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<sup>2</sup> Paragraph (c), subsection 1, section 15.3 of Regulation 81-102 respecting Investment Funds, CQLR, c. V-1.1, r.39.

## **Conclusion**

As a result of these findings, we asked certain Mutual Funds to make immediate or prospective changes to their prospectuses and Funds Facts.

The Authority expects the findings and areas for improvement in this notice to be used in presenting the information required by current legislation and regulations. Investors will then have consistent and clear information enabling them to make better-informed investment decisions.

As part of its investment fund oversight program, the Authority will continue to closely monitor how the issues identified during this review evolve.

## **Additional information**

Please refer your questions to:

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