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Mr. Christopher Jepson
Senior Legal Counsel, Compliance & Registrant Regulation, Ontario Securities Commission
Chair, Total Cost Reporting Securities Sector Working Group
20 Queen St. W., 22nd Floor
Toronto, ON M5H 3S8

Dear Mr. Jepson:

RE: Total Cost Reporting Joint Project – Consultation on Preliminary Options

The Investment Funds Institute of Canada (**IFIC**) appreciates the opportunity to provide feedback on the preliminary options being considered by the Joint Committee to expand upon cost reporting to investors.

IFIC is the voice of Canada's investment funds industry. IFIC brings together 150 organizations, including fund managers, distributors and industry service organizations to foster a strong, stable investment sector where investors can realize their financial goals. IFIC works collaboratively with industry representatives, regulators, governments and investor advocates to help cultivate a system that is fair, secure and efficient for all stakeholders.

Before responding directly to the options that have been raised in Appendix A, we would like to provide some overarching comments on the consultation.

Evidence-Based Solutions

IFIC members support enhanced fee transparency. However, before determining its policy direction, we encourage the Joint Committee to clearly articulate what the intended objectives are.

Our members agree that, as this initiative moves forward, it will be important to consider behavioral insights and other available research to help determine what cost information is important to investors. Therefore, we recommend that any proposal be thoroughly tested with investors before implementation to ensure the proposed direction is useful and comprehensible. In 2019, IFIC conducted some limited research with BEworks on expanded cost disclosure. Although this research is not publicly available, we would be pleased to walk you through the research and its findings. An interesting and relevant finding is that while basic boosts (such as simplified wording and chunking of information) improved investors' higher-order comprehension of statements, expanded cost disclosure lowered confidence in understanding

Practical Implications

While IFIC members fully support expanding cost reporting to investors, it is important to understand that providing new data elements will have a significant impact on many industry participants. As such, it is critical that industry stakeholders continue to work together to come to the best possible solution for investors.

In reviewing our feedback to the options provided, it is important to keep in mind that any option that requires data that is not currently part of an existing data file will require material system enhancements across various stakeholders.

Practical implications when adding a new data element to facilitate expanded cost disclosure include:

Fundserv

- Fundserv will need to add new data fields to be able to exchange information between fund companies, dealers and service providers.
- Fundserv enhancements are finalized in January and released in June each year. For example, to add any new data fields into the June 2022 release, final requirements would need to be in place by January 2022.
- These timelines are dependent on the complexity of the rule and its associated requirements.

Fund Companies

- The complexity of the Fund Manager changes required will depend on the nature of the requirements under the rules. For example, to provide basic fund MER data similar to the disclosure contained in the Fund Facts will require a process to populate the data in back office systems and transmit it to Fundserv.
- Following the initial change to data files, a process will be required to maintain or update the data as needed.

Dealers

- Dealer systems will need to be updated to be able to accept, retain, use and periodically update the new data elements.
- Changes will be required to the data file that contains the inventory of securities available on the dealer's platform with the associated security details (**security master**).
- Changes will be required to the dealer's statement files.

Print Vendors and Other Service Providers

- Print vendors will need to update their systems to be able to accept and use the new data files.
- Changes will be required to the statement layout and design.
- Other service providers may need to adapt functionality to accept new data points and provide calculation services, as deemed necessary.

Since some of these changes will need to be done sequentially, it will be particularly important that the implementation period provides sufficient time to build and test the enhanced functionality.

Cost and Complexity

You will note in the responses provided, there are three broad classifications for the proposed options:

LOW

Simple disclosure elements will have a low level of cost and complexity.

HIGH

Although a flag or a single new data element may seem to be simple, because the information to support that element is not readily available in existing data files, the cost and complexity will be high.

VERY HIGH

Options that contemplate one or more new data elements and new calculations will be very high in cost and complexity.

As complexity increases, there will be a commensurate increase in the time necessary to implement the change(s).

While CRM2 challenged the industry to use and report on data that was generally available, expanding cost disclosure to include calculations or estimates asks the industry to source and use data that is not currently contained in the data files exchanged between stakeholders. As such, the cost, time and effort to implement this type of solution may approach or exceed that of CRM2.

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We would be pleased to provide further information or answer any questions you may have. Please feel free to contact me by email at kvickers@ific.ca or by phone 416-309-2324. Thank you once again for seeking our input. We appreciate this opportunity and stand ready to assist with this initiative.

Yours sincerely,

THE INVESTMENT FUNDS INSTITUTE OF CANADA

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Appendix A

1. **Account statements**

   a. **A <u>simple reminder in plain language</u> if a client may incur "investment fund management expense fees or other ongoing fees" in connection with a security (borrowing from s.14.2.1(d) for consistency in drafting). There would be "flag" on each security with an embedded fee, but the text need only be set out in one place.**

   This option references "an investment fund management expense fee or other ongoing fee" as well as an "embedded fee". For clarity, we would recommend using "investment fund management expense or other ongoing fee" consistently.

   To provide feedback on this option, we have separated the option into two components, the disclosure and the flag.

   As noted above, simple disclosures can be added to a statement relatively quickly and inexpensively, provided the statement layout has the available space to add the disclosure. The cost and complexity to add a simple disclosure would be LOW.

   In regards to the flag, it appears that this option intends to take a similar approach to NI 31-103 s. 14.14.5(g), which identifies securities that might be subject to a deferred sales charge if they are sold. This was generally satisfied by including "DSC" in the naming convention of the fund along with a disclosure. This requirement did not require a material change because most security masters already used this naming convention to identify DSC mutual funds.

   Adding a flag to each security if a client may incur an investment fund management fee or other ongoing fee is not a simple task. Such a flag would require data that is not currently included on a firm's security master, nor is it contained in the Fundserv data files. As such this is not data that can be communicated between stakeholders in today's environment. Additionally, dealer systems are not currently configured to accept, store and use the data. The cost and complexity for a flag would be HIGH.

   Lastly, we would encourage the Joint Committee to consider a flexible approach to applying a flag. For example, a business model could provide access to a broad spectrum of investment funds, only some of which have investment management expense fees or other ongoing fees. This may necessitate that a flag be applied to individual securities. Alternatively, under a different business model, a firm or account type might only permit access to investment funds with investment management expense fees or other ongoing fees, in which case the described disclosure could be provided at the account level.

   b. **The same as (a), but with <u>prescribed text designed to ensure clarity</u>. The text might be something along the lines of *"You pay ongoing fees to the manager of the fund for so long as you have this investment in your account. You do not pay these fees directly; they are deducted from the fund. These fees were already deducted from the fund before its market value was calculated. These fees are the principal way the fund's manager covers its costs and makes an operating profit."* It may also be useful to include reference to the availability of information in each funds' current offering document (prospectus/fund facts) and where it can be found online.**

   While suggested text would be helpful, IFIC members would prefer the option of using the suggested language or something "substantially similar". This approach is consistent with NI 31-103 s. 14.17 (e) and (h). The cost and complexity would be the same as option 1a.

   We are not confident that that the sentence "These fees are the principal way the fund's manager covers its costs and makes and operating profit" is necessary or helpful to the investor. It would be prudent to determine if the expanded language improves investor confidence and comprehension through testing.

   c. **The same as (b) with the addition once per year, in the statement sent closest in time to the annual compensation and performance reports, of expanded reporting consisting of the <u>fees per fund expressed as a percentage and the</u> <u>approximate dollar amount deducted</u> in respect of the client's holding in the fund (e.g., the "flag" beside the security would say**

something like "… *ongoing management fees of 2.2% are deducted from the fund. During the reporting period this was equivalent to approximately $x for your investment*").

This option requires data elements that are not currently contained in data files as well as a complex calculation. As noted above, this would require substantial system enhancements across multiple stakeholders. As a result, the cost and complexity for this option would be VERY HIGH.

Requiring a flag for each security held at the end of the period that includes the management expense ratio (**MER**) and an estimate of dollars paid poses several challenges:

- A reasonable estimate of the amount of management fees deducted from the fund during the reporting period would require the calculation of an approximate daily cost to the client of each holding. This approach is outlined in the IFIC response to the MFDA Discussion Paper on Expanded Cost Reporting.
- Calculations based on the MER include the trailing commission paid to the dealer. As a result, the commission paid to the dealer may be double counted since it would be reported to the client twice – once in the report on charges and other compensation to the dealer and a second time through the estimate of the amount of management fees. This issue is also discussed in the IFIC response to the MFDA Discussion Paper on Expanded Cost Reporting.
- Investors might well also want or need a narrative that explains the calculation.
- If you consider this approach in the context of an account with multiple holdings, the result may be confusing to investors. As an example, if there are 10 mutual fund holdings in an account, the result would be 10 flags and 10 associated disclosures to cross reference.
- This option does not contemplate if there are funds held during the period that are not held at the end of the period.

Lastly, we would question if this information should be included on the account statement given there is a separate report that details changes and other compensation to the dealer. This approach should be tested to ensure investor comprehension and confidence is not diminished by having cost information in two separate reports.

2. **Report on charges and other compensation**

   a. **A simple reminder in plain language using prescribed text designed to ensure clarity. The text might be something along the lines of *"You pay ongoing fees to the manager of certain funds for so long as you have them as investments in your account. You do not pay these fees directly; they are deducted from the funds. These fees were already deducted from the funds before their market value was calculated for purposes of your investment performance report. These fees are the principal way the funds' managers cover their costs and make an operating profit. For information about specific funds, see [your account statements and] the relevant fund facts documents available on each fund's issuer's website."***

   A simple reminder in plain language can be included cost effectively, in a reasonably short amount of time. The cost and complexity would be LOW.

   As discussed in 1b above, firms should have the ability to use the suggested language or something substantially similar. We would again question the value of the sentence "These fees are the principal way the funds' managers cover their costs and make an operating profit".

   b. **The same as (a) with the addition of aggregate fees expressed as a percentage. Challenges identified with this option include the following:**

   - **would have to be expressed as either a range or an average if this report is to remain at the whole account level,**
   - **would create the potential for client confusion,**
   - **would need to be sure that most investors would find the additional information to be useful.**

The cost and complexity of this option is VERY HIGH and may meet or exceed the costs associated with implementing CRM2. The addition of aggregate fees expressed as a percentage requires new data elements and calculations.

We agree with the challenges that you have identified and would again refer you to the IFIC response to the MFDA Discussion Paper on Expanded Cost Reporting .

c. **The same as (a) or (b), with the addition of the (approximate) aggregate dollar amount deducted in respect of funds in the client's account (e.g., "*During the year covered by this report, ongoing management fees of approximately $x were deducted from funds in your account*"). This would be consistent with the basis for the current information in the report: account-level, dollar amounts. For that reason, it might be more meaningful than the percentage-based information discussed in (b). It will be a challenge to avoid causing some clients to think that they pay these fees directly, perhaps on an after-valuation basis.**

The costs and practical implications for this option would be the same as those outlined in 2b.

3. **Investment performance report**

a. **No change as this document is meant to provide investment performance information only at the account level and it would therefore be the wrong place to address costs embedded in certain products. It may be confusing to clients if information about embedded fees was included there.**

We agree that cost information should not be included in the investment performance report.

b. **Include the following additional information for the change in market value to reflect the impact of charges and ongoing embedded fees at the account level:**

Opening market value
Deposits
Withdrawals
Change in the market value of your account:
- **Increase\Loss in value (plus embedded fees)**
- **Ongoing embedded investment fees (i.e., as a separate line item)**
- **Charges you paid directly to us**
- **Net change in the market value of your account**
Closing market value

While this option is more in line with the feedback that IFIC provided on the MFDA Consultation on Expanded Cost Reporting, the IFIC response did not contemplate intermingling cost information with investment performance.

As you have noted in option 3a, including cost information on the investment performance report may be confusing to investors. We agree that the investment performance report may be the wrong place to address investment fund management expenses or other ongoing fees.

If this option continues to be considered, the cost and complexity to implement would be VERY HIGH and may meet or exceed the costs associated with implementing CRM2.

c. **Same as (b) broken down by security position**.

Generally, the response to this option is the same as 3b above. There are however some additional comments that we would like to offer.

As you have noted above, the investment performance report is a document that provides account level investment performance. This option considers adding cost information by security position which does not align with the intent of the investment performance report.

For accounts that hold multiple security positions, and potentially a variety of security types, we would question if investors want this amount of detail or if it would negatively impact investor comprehension and confidence. This approach has the potential to include a great deal of information and research has proven that more data does not always lead to greater investor confidence or comprehension.

To align the information at the security level with the investment performance at the account level, this amount of detail may need to be reported for all holdings held during the period, not just the holdings at the end of the period. Reporting this information for just the holdings at the end of the period may impact investors' ability to connect the performance of the account to the information on the report.

Similarly, given the investment performance report details account performance over various periods (1,3,5, and 10 years and since inception), firms may be required to provide security level detail on all holdings since the inception of the account. This doesn't seem to be the right result for investors.

4. New stand-alone report

We do not currently anticipate proposing a new stand-alone report to address embedded fees. We are concerned that a new stand-alone report might be disregarded by many investors and confusing to others. It might also create a perception of undue focus on products with embedded fees.

We agree that a new stand-alone report may not be the most appropriate solution for investors.