

IFIC Submission on Total Cost Reporting

Member Webinar

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IFIC

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Background

- IFIC continues to support expanded cost reporting to investors
 - IFIC submission to the MFDA – July 20, 2018
 - IFIC submission to the OSC/AMF - Dec 20, 2021

Overview of Key Points

- IFIC recommends:
 - That the amendments do not include the changes to the quarterly client account statements
 - Extending the proposed transition period
 - That investment fund managers be permitted to provide dealers with cost information derived solely from their most recent disclosure documents
 - That dealers be permitted to rely solely on such information for providing enhanced cost disclosure

Regulatory/Industry Collaboration in Complex Rule Implementation

- **CSA/Industry Implementation Standing Committee**
 - Membership – CSA, Industry, Service Providers and External Experts
 - Mandate – Not to debate the policy objective, identify technology constraints, barriers, Propose realistic implementation timeline
- Implementation period would have the support of those responsible for implementing the solutions

Overview of Research

- PwC research is based on literature review, surveys and interviews with industry experts
- Concludes that the regulatory amendments proposed by the CSA will improve investors' awareness and understanding of fees
- No strong evidence that quarterly account statement fee reporting would provide additional benefit to investors beyond what they would receive with the annual report on charges and other compensation

Account Statements Requirements - Recommendations

- IFIC recommends that the proposed changes to Account Statements not be adopted
- Use CSA's access equals delivery model
- SEDAR+ can also be used

Account Statements Requirements - Analysis

- Inclusion of FER in Account Statements could be misleading, confusing and/or counter productive for investors
- FER data not specific to an investor's circumstances
- Mismatched data
 - performance indicators - book cost and market value - are in dollars
 - cost indicator – FER – is a percentage
 - performance indicator and cost indicator measurements do not align
 - time periods do not align

Account Statements Requirements - Analysis

- Data not properly contextualized without fund performance
- Investors cannot be expected to convert/determine annual percentage performance/cost relationship
- No full cost information in current Account Statements – FER alone can reflect only part of cost of investing (e.g. Series F)
- Investors well served by Annual Report on Charges and the Annual Investment Performance Report
 - does not serve investors' interests to provide less meaningful data, such as the FER, on a stand-alone basis

Account Statements Requirements - Analysis

- IFIC is concerned about the potential for negative investor outcomes
 - stand-alone FER cost information, presented without any context could:
 - cause investors to unduly focus on costs
 - narrow focus on cost – potential for inappropriate comparison of a fund, to other funds, and banking and other products
 - lead investors to make counter-productive decisions to exit certain fund holdings based solely on the FER information
 - potential negative consequences for investors' achieving long-term investment goals

Account Statements Requirements – Analysis

- Inconsistent with theme of regulatory burden reduction
 - disproportionate increase in costs and time for system enhancements given no clear, significant, and demonstrable benefits to investors
 - creates inconsistency between Account Statements (FER) and disclosure materials (no FER number)
 - reporting of FERs at a different reporting cycle than MER and TER disclosures in the MRFPs

Account Statements Requirements – Analysis

- Very robust disclosure regime already exists
 - point of sale – MER/TER information in Fund Facts and ETF Facts
 - after point of sale – MER/TER information in MRFPs
 - fund managers would be required to have these documents on their websites (if access = delivery is implemented)
- IFIC believes investors would prefer annual fee reporting, rather than quarterly

Account Statements Requirements - Research

- PwC concludes that there is no strong evidence that the proposal for quarterly disclosures would significantly benefit investors above and beyond what would be included in the Annual Report on Charges
- Research shows that when it comes to percentages, investors tend to neglect small amounts and misinterpret percentages when making decisions around fees and returns
- The PwC Report finds that presenting fee information on its own (without the context of value, or performance) can negatively impact investors and lead them to become overly focused on the costs, leading to loss aversion or fee aversion

Account Statements Requirements – Research cont.

- Research also suggests that investors prefer annual rather than quarterly fee reporting
- There is already a high level of products fee understanding
- According to PwC, While jurisdictions like the EU, the U.K. and Australia have comparable annual fee disclosure to regulatory proposals, there is no comparable jurisdiction that requires quarterly fee disclosures as contemplated by the CSA

Annual Report on Charges - Recommendations

- IFIC supports expanded cost disclosure in the Annual Report on Charges
- IFIC recommends that the FER be reported in dollars as a single number if the TER is included
- Delete the requirement for dealers to disclose individual, non-standard, descriptions of any assumptions or approximations used by fund managers

Annual Report on Charges - Analysis

Fund Managers' Duty to Provide Information, ss. 14.1.1(3) and (3)(b)

- Fund managers should only be required to use most recently filed data
- Should not require subjective determinations
- Consistent with regulatory burden reduction, would:
 - not require off-cycle data calculations
 - streamline data collection process (potentially new system requirements)
 - reduce litigation risk
 - make disclosure documents and client enhanced reporting more consistent
- Information gap exists for new funds

Annual Report on Charges - Analysis

Fund Managers' Duty to Provide Information - **Recommendations**

- IFIC has provided recommended drafting changes to amend ss. 14.1.1(3) and (3)(b) such that:
 - fund managers' obligation is an objective requirement (should not be dependent on fund managers' subjective determinations)
 - the information gap that exists for new funds is resolved

Annual Report on Charges - Analysis

Disclosure to Describe Approximations or Assumptions, ss. 14.17(1)(p) [report on charges and other compensation], ss. 14.14(5)(c.2) [account statements], and ss. 14.14.1(2)(c.2) [additional statements]

- Not reasonably possible for dealers to obtain all types of assumptions or approximations from fund managers
- If required, approach would need to be standardized through rules
- Would be incomprehensible and overwhelming to investors
- Investors would better understand a short, standardized explanatory note

Annual Report on Charges - Analysis

Disclosure to Describe Approximations or Assumptions, ss. 14.17(1)(p) [report on charges and other compensation] - **Recommendations**

- Remove obligation for dealers to disclose any assumptions or approximations used by fund managers to calculate FER
- Instead, permit dealers to use a generic *explain/disclaim* disclosure statement; suggested wording:

“This information uses data provided by the investment fund managers and is calculated using the investment funds’ most recently published information. It may not reflect the actual charges you have indirectly incurred but is a required calculation that is intended to be an approximation.”

- If proposed Account Statements proceed, use same wording

Annual Report on Charges - Research

- PwC finds that the regulatory requirements will improve investors' understanding of fees
- Currently, evidence shows that the majority of investors report receiving and reading annual fee and performance statements
- However, survey research finds that many investors mistakenly believe that current CRM2 statements show the total cost of investing, and most investors would prefer total cost reporting

Implementation Timeline Implications - Recommendations

- Transition period should be a minimum of one year more than is currently proposed
 - final amendments – in effect in September 2025 (vs 2024)
 - total implementation timeline about a minimum of 3.5 years (from final rule)
- Entails:
 - minimum 2.5 years - develop, test and implement systems required for fund managers and dealers (calculate, delivery, and store daily data)
 - one additional year thereafter - collection of data for a full year
- Investors receipt of first enhanced Annual Report on Charges – for reporting period ending December 31, 2026

Implementation Timeline Implications - Analysis

- Proposed transition period of 18 months is neither reasonable nor practical
- Prototype timeline delineated by Fundserv, and its members (i.e. mutual fund dealers and investment fund managers) - Appendix B in Submission
 - will take longer than CSA's proposed transition period
 - need final version of amendments before work can start
 - technology builds - require BRDs & budget approvals based on final rule

Implementation Timeline Implications - Analysis

- Material system enhancements must be carried out sequentially - by each of Fundserv, fund managers, dealers, and third-party service providers
- Fundserv has set timeframes to design, code, and publish system changes
- Based on Q2 2023 publication date of final amendments:
 - July 2024 – earliest for Fundserv to complete draft technical requirements (V35 BRD)
 - October 2024 - publish the final technical solution (V35 BRD)
 - November 2024 - dealers and fund managers start project planning/perform development/internal testing/ re-engineering, then industry testing via Fundserv
 - June 2025 - Fundserv production ready
 - by December 31, 2025 – Fundserv activates new enhancements
 - January 1, 2026 to December 31, 2026 – collection of one full year’s worth of data for each client

Implementation Timeline Implications - Analysis

- New data elements required - FER data does not exist
- Mutual fund managers have to program to calculate and transmit daily FER factors to dealers through Fundserv
- Dealers have to:
 - program to receive and store the new file from Fundserv, calculate at an investor account level the dollar cost of the FER, and aggregate amounts for each investment fund holding
 - redo existing Annual Report on Charges
- Requires significant system enhancements - time consuming, expensive, & significant operational risk

Implementation Timeline Implications - Analysis

- No infrastructure currently exists for required ETF data transmission, such as Fundserv
 - same uncertainty for other types of investments funds
- For dealers to commence builds, solutions needed first for all types of investment funds
- The move to T+1 proposed to be effective Labour Day weekend, September 2024 - presents added risk to successful implementation

Implementation Timeline Implications - Research

- PwC research confirms industry concerns with respect to timelines
- Based on PwC's experience and from interviews with stakeholders, it would not be possible to begin process and technological changes until regulations are finalized

Unreasonableness of Dealer Expectations - Recommendations

- Delete both ss. 14.17.1(2) and (3)
 - is overly and unnecessarily burdensome and places unreasonable liability on dealers
 - the information belongs to fund managers – dealers cannot be responsible for obtaining and assessing
- Revise ss. 14.17.1 (4) to include that if the registrant has not obtained the information from a registered investment fund manager within a reasonable period of time, the information must be excluded from the applicable calculations and reporting

Unreasonableness of Dealer Expectations - Analysis

- Dealers do not have the tools/information to assess whether information provided by fund managers is misleading
- Unclear, when not provided by the fund manager, whether dealers are expected to complete the calculations which the fund managers are expected to do using the formula in ss. 14.1.1(2)
- Fund managers' responsibility is diminished by this section
- Timeliness of information provided by fund managers impacts statement production
- Fund managers should be solely responsible for providing the FER related data required by dealers

CSA's Sample Prototype Annual Report on Charges

- IFIC supports not making it mandatory to use CSA's sample prototype
- Dealers should have flexibility on the presentation of this material
- IFIC's concerns with the CSA's prototype - could be misleading
 - two tables with cost totals - potential double counting (trailer commissions) and overstatement of total cost of investing (if two totals added together)
- IFIC's proposed alternative prototype Annual Report on Charges – Appendix C of Submission

QUESTIONS?