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May 26, 2014

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Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
Financial and Consumer Services Commission (New Brunswick)
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island
Nova Scotia Securities Commission
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RE: PROPOSED AMENDMENTS TO NATIONAL INSTRUMENT 81-101 MUTUAL FUND PROSPECTUS DISCLOSURE AND COMPANION POLICY 81-101CP (2ND PUBLICATION)

Dear Sirs/Mesdames,

We are writing in response to the Canadian Securities Administrators' (CSA's) *Request for Comment on Proposed Amendments to National Instrument 81-101 Mutual Fund Prospectus Disclosure* (the Proposed Amendments) as published on March 26, 2014. The Proposed Amendments are to the existing mutual fund disclosure rules and seek to implement new requirements regarding the pre-sale delivery of the Fund Facts document. This iteration of the development of Fund Facts represents the third stage of the CSA's point of sale disclosure project for mutual funds. In specific, the CSA's proposal would require a Fund Facts document to be delivered to investors *before* the advisor receives instructions from the client to execute the transaction to purchase a mutual fund. This general delivery requirement would be subject to very limited exceptions.

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EXECUTIVE SUMMARY

As a general matter, Advocis supports delivery to the consumer of the Fund Facts document to the retail investor prior to his undertaking the decision to purchase mutual funds and communicating the same to his advisor.

We consider the mode and timing of the delivery of the Fund Facts document, and the advisor and dealer obligations attendant thereto, to be essential to the point of sale disclosure project. To ensure the best possible disclosure system for mutual funds and their investors, as well as the elimination of unnecessary costs and duplication of disclosure and effort, we suggest a number of changes to the Proposed Amendments, summarized here and explained in greater detail below.

Advocis recognizes the need to strike a balance between the promotion of consumer protection and the maintenance of consumer choice. That's why we believe that retail investors who do not wish to receive Fund Facts – either on a pre-sale basis or altogether – should be given the ability to opt out of its delivery. However, in the interests of consumer protection, we also believe that the typical "passive" investor in pre-authorized purchase plans and in company-sponsored group RSPs invested in mutual funds should receive the Fund Facts annually *and* when it is amended, unless they expressly opt-out of such delivery. At a minimum, sophisticated investors, such as persons who would qualify as accredited investors for the purposes of prospectus exemptions, should be exempt from mandated pre-sale delivery.

Regulatory Arbitrage

We continue to believe that subjecting mutual funds to enhanced and now pre-trade point of sale disclosure requirements places them at a competitive disadvantage in relation to other financial products. While we recognize the difficulty in identifying widely-used retail investment products which are comparable to mutual funds, and the jurisdictional impossibility of the CSA regulating segregated funds, we do believe that similar fund products should be subjected to the same burden of regulation as that placed on mutual funds.

Delivery Issues

In brief, while Advocis generally supports the notion of Fund Facts and its pre-sale delivery where appropriate (we would offer an exemption for a low-risk investment such as certain money market funds), the submission takes issue with the CSA's blanket proposition that calls for pre-sale delivery of Fund Facts for all mutual funds, regardless of whatever delivery arrangement the advisor and client want to make. An alternative delivery regime which would accomplish the same ends as the Proposed Amendments while preserving consumer choice would have pre-sale delivery as the default position and annually permit consumers to opt out of delivery, should that be their preference.

In specific, we urge the CSA to reconsider its rejection of the concept that access to Fund Facts equals delivery of Fund Facts. Prohibiting this form of electronic delivery in today's increasingly "wired" society strike us as a retrograde policy: in 2012, 83% of Canadian households had web access at home.[1] Indeed, in the interests of reducing time and therefore client expense, the advisor should be expressly permitted to orally and/or electronically direct the client via a specific hyperlink to a web site where he or she can find the relevant Fund Facts. It should be recalled that the CSA's original intention with the Fund Facts enterprise was to be compliant with the International Organization of Securities Commissions' *Principles on Point of Sale Disclosure – Final Report*. Principle Two of the IOSCO report clearly permits delivery of pre-sale disclosure in an embedded link: it states that "Key information should be delivered, *or made available*, for free, to an investor before the point of sale" (emphasis added). Given that since 2011 Fund Facts has been available on the web, the submission opposes this regressive approach.

[1] Statistics Canada, "Canadian Internet Use Survey, 2012." November 26, 2013. Accessible at http://www.statcan.gc.ca/daily-quotidien/131126/dq131126d-eng.htm.

Cost-Benefit Issues
Point of sale disclosure requirements should not be imposed without the benefit of consumer testing and assessment. Such data-gathering and analysis is essential to determining the likely effectiveness of Proposed Amendments. Regardless of the final point of sale regime that is adopted for Fund Facts, it will not have the intended outcome if retail investors fail to read and understand the information provided. Accordingly, the CSA should defer the introduction of Fund Facts' pre-sale delivery requirement and focus more on working with stakeholders to better familiarize retail investors with Funds Facts and how they can benefit from it – and how the Fund Facts document can be improved.

Compliance
Requiring pre-sale delivery of the Fund Facts document to retail investors – and without a waiver for those clients who do not wish to receive it – places significant administrative pressure on the advisor-client relationship. As well, the conditions which must be fulfilled to make use of the "not reasonably practical" exemption from the pre-sale delivery requirement are so onerous as to make what in almost all cases will be critical mutual fund purchases (by definition, these trades will be both investor-initiated and of the "time-is-of-the-moment" variety) more time-intense and cumbersome for both the advisor and the client. It must be considered by the regulator that all of this will transpire on a daily basis in an area of financial advising which is already severely burdened by myriad administrative and compliance requirements.

With the obligation for pre-sale delivery of Fund Facts becoming the responsibility of financial advisors, it is to be hoped that the CSA will heed advisors' industry experience both in delivering disclosure documents to retail investors and in explaining investment concepts to them. Advocis members know that sufficient time is needed for fund manufacturers, dealers and advisors to develop a workable framework to ensure the effective working of the entire Fund Facts regime, including pre-sale requirements. Our members also know that the costs of compliance all too often weigh much heavier on small and independent firms. The realization of a compliance outcome which is beneficial to the consumer but which does not privilege firms with "deep pockets" over those who will struggle to fulfill pre-sale rules is surely the CSA's goal.

Transition Period
When the CSA indicates the possibility of implementing mandatory pre-sale Fund Facts delivery in a compressed three-month period, we must conclude that the CSA is overly optimistic on the administrative, practical and technical issues and costs associated with preparing the funds industry for pre-sale delivery. Unduly accelerating the process with scant regard for those who must implement it is a disservice to investors and the capital markets at large.

Instead, Advocis believes that the best interests of Canada's retail investors and capital markets will be better met by focusing on successfully implementing Phase Two of the Client Relationship Model (CRM-2) and on further refinement of the Fund Facts document. Once outstanding concerns – including questions regarding risk methodology – are settled, then and only then should the CSA begin the process of mandating pre-sale delivery. We believe that the least intrusive way to implement pre-delivery of Fund Facts is to give the industry sufficient time for personnel training and compliance testing. Indeed, we take issue with the notion of rushing into mandating the pre-sale delivery of Fund Facts within the next six to nine months (as the CSA seems to be considering), in light of the ongoing, complicated and resource-intense roll-out of CRM-2. Ideally, we would suggest that the CSA consider the effective date for pre-sale delivery of Fund Facts to be scheduled somewhere in the period of May to July, 2016, so that it may be harmonized with the final scheduled set of CRM-2 changes coming in 2016. Failing that, coordinating pre-sale delivery with the changes in CRM-2 which take effect in July 2015 would be advisable.

Part One of the submission raises and responds to several general concerns with the proposed pre-sale delivery of Fund Facts, and Part Two tracks the CSA's question-and-answer format as set out in its *Request for Comment*.

PART ONE: GENERAL COMMENTS AND CRITICISM

A. Advocis: Who we are

Advocis is the largest and oldest professional membership association of financial advisors and planners in Canada. Through its predecessor associations, Advocis proudly continues over a century of uninterrupted history serving Canadian financial advisors and their clients. Our 11,000 members, organized in 40 chapters across the country, are licensed to sell life and health insurance, mutual funds and other securities, and are primarily owners and operators of their own small businesses who create thousands of jobs across Canada. Advocis members provide comprehensive financial planning and investment advice, retirement and estate planning, risk management, employee benefit plans, disability coverage, and long-term care and critical illness insurance to millions of Canadian households and businesses.

As a voluntary organization, Advocis is committed to professionalism among financial advisors. Advocis members adhere to our published *Code of Professional Conduct*, uphold standards of best practice, participate in ongoing continuing education programs, maintain professional liability insurance, and put their clients' interests first. Across Canada, our members spend countless hours working one-on-one with individual Canadians on financial matters. Advocis advisors are committed to educating clients about financial issues that are directly relevant to them, their families and their future. Our following comments on the CSA's proposal reflect the priorities of Advocis' members and their clients.

B. Overview of the Proposed Amendments to Fund Facts

It will be recalled that the first Fund Facts proposal was published for comment by the CSA in 2009. This most recent proposal is part of the third and presumed final stage of the implementation of the CSA's point of sale disclosure regime for mutual funds. The point of sale enterprise – with the Fund Facts sheet as its centrepiece – seeks to provide retail investors with key, timely and accurate information, written in plain-language, when or before they make an investment. The CSA has indicated its plans to expand the concept of Fund-Facts-style short-form disclosure to other investment funds, including exchange-traded funds, as another part of Stage Three's implementation.

Currently, advisors are required to deliver the simplified prospectus for a mutual fund to investors within two days of a trade. Amendments to provincial securities legislation and National Instrument 81-101 will mandate that dealers deliver the applicable Fund Facts instead of the simplified prospectus. No changes to the actual delivery requirements have been made at this stage, nor have

the withdrawal and rescission rights been amended, other than to require and acknowledge that the applicable Fund Facts document is to be delivered in place of the simplified prospectus. This requirement will come into force for any trades on or after June 13, 2014.

The Proposed Amendments at issue here will require delivery of Fund Facts to investors on a pre-trade basis – that is, before the purchase order is submitted. Under the proposed pre-sale regime there will be only two exceptions to pre-delivery: (1) pre-authorized purchase plans (similar to the current simplified prospectus delivery exemption now in place), and (2) purchases where the investor expresses a desire to complete the purchase immediately or by a specified time, and it is "not reasonably practicable" for the dealer to complete pre-sale delivery of the Fund Facts within the investor's time frame. In this case delivery will instead be made within two days post-trade and the dealer must provide extensive verbal disclosure *prior* to the trade.

Significantly, all other existing pre-delivery exceptions are removed, including on purchases of money market funds. However, there is no requirement to redeliver the Fund Facts if the investor previously received the current Fund Facts.

Finally, in terms of transition, a careful reading of the CSA's *Request for Comment* indicate that the CSA may believe that both firms and external service providers have by now created or can create in short order the compliance and delivery systems needed to implement pre-sale delivery of the Fund Facts document. As well, certain statements suggest a possible twelve-month transition period, perhaps to commence early in 2015.

C. General contextual criticism of the Proposed Amendments to Fund Facts

1. <u>Rights of rescission and withdrawal</u>

The CSA states in the *Request for Comment* that it is "not proposing any changes to existing investor rights under securities legislation."[2] This means that the investor's right of withdrawal of purchase within two business days after receiving the Fund Facts remains unchanged, which leads to the paradox of improving consumer disclosure to a minimum baseline across all CSA member jurisdictions while maintaining the *status quo* of uneven levels of consumer protection. As the CSA describes it: "Consistent with securities legislation today, depending on the timing of delivery of the Fund Facts and the timing of the trade, the investor *may or may not have the right of withdrawal of purchase*" (emphasis added)[3]. In addition, the *Request for Comment* states that "In some jurisdictions, investors also currently have a right of rescission with delivery of the trade

[2] Canadian Securities Administrators, *Notice and Request for Com*ment – *Implementation of Stage 3 of Point of Sale Disclosure for Mutual Funds – Point of Sale Delivery of Fund Facts – Proposed Amendments to NI 81-101 Mutual Fund Prospectus Disclosure and Companion Policy 81-101CP*. In 37 *Ontario Securities Commission Bulletin* 3105 (March 27, 2014), p. 3108.
[3] *Ibid*., p. 3108.

confirmation for the purchase of mutual fund securities. This right also remains unchanged under the Proposed Amendments."[4] Given that that Fund Facts project seeks to achieves a uniform model of consumer disclosure and protection across Canada, Advocis would prefer to see a standardized right of rescission across Canada, so that certain investors are not privileged simply on the basis of the province or territory in which they reside.

Accordingly, Advocis believes that it to be in the best interests of Canadians that the CSA bring uniformity to mutual fund investors' rights of rescission and withdrawal. Various industry stakeholders have for over a decade articulately and forcefully emphasized the pressing need for harmonization of these rights and for clarification of how they are to be interpreted and applied.

In addition, Advocis notes that the Proposed Amendments may be problematic in regard to withdrawal rights: currently, the mutual fund investor's withdrawal rights are legally tied to his or her receipt of the "prospectus" and, by extension, of the Fund Facts document. The Proposed Amendments provide for the investor's right of withdrawal of purchase of the fund within two business days after receiving the Fund Facts. So, depending on the timing of delivery of the Fund Facts and the timing of the trade, the investor may or may not have the right of withdrawal of purchase. This potential and presumably unintended outcome means that the withdrawal rights could be rendered non-existent if the Fund Facts is provided to the investors at least two days *before* mutual fund purchase and one is not sent with the trade confirmation. We would therefore suggest that the CSA redraft the summary of investor rights contained in the Fund Facts template to eliminate this possibility.

2. <u>Mutual funds, IVICs, and the incentives for regulatory arbitrage</u>

Unfortunately, the CSA has still not addressed the long-standing problem of subjecting mutual funds – which with over a trillion dollars of assets under management remain Canadians' most popular investment – to more stringent regulation than that applied to similar investment vehicles. To Advocis, it is not clear why the CSA now wants to introduce the additional step of pre-sale delivery of the Fund Facts document before the investor may make an initial investment in a mutual fund: the disclosure regime for mutual funds now so far exceeds those of other investment products that the problem of regulatory arbitrage is very real.

It should be recalled that the point of sale project is a continuation of the shared vision of securities and insurance regulators to provide investors with more meaningful and effective prospectus disclosure for mutual funds and segregated funds (individual variable insurance contracts or IVICs), as described in *Framework 81-406 Point of Sale Disclosure for Mutual Funds and Segregated Funds*, which was published by the Joint Forum of Financial Market Regulators on October 24, 2008. On January 1, 2011, new disclosure requirements took effect for segregated funds. These requirements

[4] *Ibid*., p. 3108.

were approved by Canadian insurance regulators in 2009 and were meant to be a way to implement the principles set out by the Joint Forum of Financial Market Regulators to harmonize the short-form disclosure practices for mutual funds and segregated funds.

In brief, the purchaser of the IVIC must receive an Information Folder which contains a "Key Facts" or Fund Facts document that briefly describes the key features of the IVIC. The client can choose how he or she receives the Information Folder and Fund Facts documents – physically (in person, mail or facsimile) or electronically (via e-mail or viewed online). There is no requirement for pre-sale delivery of the IVIC's Key Facts/Fund Facts document. The result? It is possible that the Proposed Amendments, which require pre-sale delivery of Fund Facts for mutual funds in nearly all sales situations, could lead to a product or regulatory arbitrage which would favour the insurance sector.

In short, regulatory arbitrage is a real and ongoing with Fund Facts and imposing pre-sale delivery requirements only on mutual funds will certainly exacerbate the problem *vis-à-vis* segregated funds. The impact of such arbitrage will only expand as insurance companies continue their foray into wealth management. Even a small re-allocation of investment assets to alternative product choices as a result of the different requirements of the IVICs sales process should be cause for regulatory concern. If IVICs do not have the same pre-sale delivery requirements as mutual funds, then the Canadian retail investor is exposed to the problem of less-than-professional dual-licenced advisors diverting clients from mutual funds to more costly IVICs.

As well, advisors who are not members of a professional or membership association (such as one which requires adherence to an ethical code of conduct and the fulfillment of ongoing continuing education requirements) might be subject, however unconsciously, to a bias towards dealing with more lightly regulated IVICs over mutual funds. Such a bias can creep in unawares and need not be made explicit to have an effect: a client may sense an unconscious preference in the advisor due to an IVIC's reduced compliance obligations and general legal liability as against mutual funds and accordingly select the IVIC product he or she thinks their advisor secretly prefers, regardless of the advisor's formal recommendation.

We would therefore encourage the CSA to hold off on requiring pre-sale delivery of Fund Facts, in whatever final form it takes, until it has: (1) made efforts with the Joint Forum of Financial Market Regulators and the Canadian Life and Health Insurance Association to harmonize the Fund Facts pre-sale delivery requirements with those governing segregated funds, and (2) widened the scope of its point of sale disclosure project to include the mandatory delivery of summary disclosure documents for other investment funds, including exchange-traded funds and closed-end funds. Such delivery would preferably be on a pre-sale basis, and should at minimum be within two days of a trade. Imposing pre-sale delivery on other types of investment fund products would at least prevent Canadians' most popular investment from being further used as a "test subject" for regulatory

experimentation. The creation of a level playing field on which all fund products must play by the same disclosure rules would both extend the benefits of this form of disclosure to more products and enhance investor protection while simultaneously removing the ongoing competitive disadvantage the current Fund Facts regime has placed on mutual funds, and which the Proposed Amendments will only exacerbate. Whenever possible, investor protection should not play out on an un-level playing field.

3. Refining the Fund Facts document and its interaction with the Customer Relationship Model

With the CSA continuing to work on the complex issue of a simplified, industry-accepted mutual fund risk classification methodology, it seems that the Fund Facts document may still be a long way from reaching its final content and template requirements. Moreover, the CRA still has to revisit the status of long-standing documents such as the annual information form and the simplified prospectus to bring them into line with the latest amendments to Fund Facts and, more generally, with the overall trend toward enhanced disclosure and delivery. Further, we would prefer the CSA to offer some forward-looking guidance on how it plans to coordinate – and expects impact stakeholders to coordinate – the Proposed Amendments at issue here with (1) the ongoing changes to the Fund Facts format and required content and (2) the changes to the CRM-2's cost and performance disclosure obligations, which are scheduled to take full effect by July 15, 2016.

PART TWO: RESPONSES TO THE CSA'S SPECIFIC QUESTIONS

For your ease of reference and review, the *Request for Comment*'s question-and-answer format is reproduced below. Advocis has inserted its comments and concerns in the appropriate locations.

A. Exceptions from Pre-Sale Delivery of the Fund Facts

1. While the Proposed Amendments generally require pre-sale delivery of the Fund Facts, they also set out specific circumstances that would permit post-sale delivery. a) Do you agree that we should allow post-sale delivery of the Fund Facts in certain limited circumstances?

Yes.

Introductory comments

As a general proposition, Advocis agrees with the CSA that the most recent Fund Facts for the applicable series of the mutual fund to be purchased be made available to the client *before* the advisor can accept the trade for processing. We also agree that delivery should not be required if the client has already received the most recently filed Fund Facts. However, as will be argued below,

the category of circumstances in which the Fund Facts document may be delivered *post-sale* should be expanded.

Advocis members already anticipate the pre-sale delivery requirement to lead to new levels of client frustration. Advocis is unique among advisory associations for its size and diversity of membership and long history; Advocis members are among those persons best aware of the impact on the average retail investor of the pre-sale delivery requirement. They are also professionals committed to putting into practice the ethical belief that retail investors should know what they are buying *before* the transaction occurs. But the delays in executing and processing trades certain to result from the Proposed Amendments will become very expensive for both clients and advisors.

The pre-sale delivery requirement, with its accompanying guidance that delivery must give the client reasonable time to review the Fund Facts, will prove problematic for rural and older clients. For many of these clients it will not be reasonable or feasible for them to discuss with their advisor their personal situation, decide what mutual fund investments may be most suitable, and then receive and review the relevant Fund Facts documents, unless if the meeting is in the advisor's office or client's home. The Proposed Amendments will mean that in instances where previously one face-to-face meeting was sufficient, now two client-advisor meetings must be held – with one being simply for delivery of the Fund Facts. For the bulk of these cases, it strikes us that the costs to both parties of the second meeting must surely outweigh the benefits.

Complicating the matter is any *de facto* or *de jure* requirement that the client must confirm receipt of the Fund Facts document *before* processing of the trade: many clients will not be able to immediately confirm receipt of electronic documents, thereby leaving their advisors at risk of delaying transactions that would otherwise be executed. The practicality of expecting anxious clients and busy advisors to accomplish all of this in a compressed period of time must subjected to vigorous scrutiny by the industry, especially when it is brought to mind that many advisors will be facing these time pressures *every* day, throughout the day.

What is meant by delivery?

We have concerns about what is meant by "delivery." In general, the CSA does not propose to mandate how the document is to be delivered or sent, stating that any conceivable method of actual delivery or electronic sending will be acceptable – that is, by mail, courier, email, fax or in-person delivery. At minimum, we believe that an advisor should be able to fulfill delivery obligations by emailing the client a direct link to the specific Fund Facts document's web location. However, the CSA is dismissive of any notion that "access to equals delivery of" the Fund Facts document. This position is perplexing, given: (1) the current ease of access to *all* Fund Facts on the web, and (2) the fact that the pre-trade emails which will be necessitated by CRM-2 are the obvious vehicles through which advisor and client can most efficiently satisfy the Fund Facts delivery requirement.

It should be pointed out that the CSA's original intention with the Fund Facts enterprise was to bring Canada into compliance with the International Organization of Securities Commissions' *Principles on Point of Sale Disclosure – Final Report*. Principle 2 of the IOSCO Report states that "Key information *should be delivered, or made available*, for free, to an investor before the point of sale, so that the investor has the opportunity to consider the information and make an informed decision about whether to invest" (emphasis added).[5] And IOSCO Principle 3 requires that "Key information *should be delivered or made available* in a manner that is appropriate for the target investor" (emphasis added).[6] Clearly, from IOSCO's perspective, making a summary disclosure document such as Fund Facts available to the client in the form of an embedded link or uniform resource locator placed in an email's body of text will be – if acceptable to the client – perfectly satisfactory.

It is unfortunate that the proposed disclosure regime does not recognize the realities of Canada's largely wired and technically literate society. We urge the CSA to amend its conception of delivery to expressly include electronic delivery as a pdf attachment to an e-mail, or as direct hyperlink to the relevant Fund Facts web page. Accordingly, Advocis recommends that for any finalized requirement of a pre-sale delivery*, Companion Policy 81-101CP* state explicitly that the delivery requirement may be satisfied by:

1. physical delivery: in person, or by mail or courier or facsimile; or
2. electronic delivery: by e-mail with an attached file version of the particular Fund Facts, or an email or other form of electronic transmission with a hyperlink to or url for the particular Fund Facts.

This is essentially the same wording as is used by the Canadian Life and Health Insurance Association's Fact Sheet for the delivery of segregated funds.[7] Advocis believes it is in the best interests of the Canadian retail investor to bring National Instrument 81-101 into congruence with the CLHIA's position governing the pre-sale delivery of summary disclosure documents for segregated funds.

Multiple pre-sale deliveries

The Proposed Amendments raise another delivery-related concern. The proposed restrictions on binding Fund Facts with other Fund Facts for the purposes of delivery. We believe the CSA should reconsider this proposed guidance. Among other things, it will prevent the advisor from mailing to the client, in advance of a meeting, a sheaf of Fund Facts for client-suitable mutual funds. Such a

[5] International Organization of Securities Commissions, *Principles on Point of Sale Disclosure – Final Report*, February 2011, pp. 28, 29. Accessible at http://www.iosco.org/library/pubdocs/pdf/IOSCOPD343.pdf.
[6] *Ibid.*
[7] See Canadian Life and Health Insurance Association*, Implementation of New Requirements for Segregated Funds* (October 2010). Accessible at http://www.clhia.ca/domino/html/clhia/CLHIA_LP4W_LND_Webstation.nsf/resources/Financial+Advisors/$file/Advisor_fact_sheet.pdf.

prohibition is not in the best interests of the client, it is not conducive to efficient and timely asset allocation, and it certainly runs counter to the goal of consumer empowerment which underwrites the entire Fund Facts regime. The bundling restriction inhibits the advisor from quickly gathering and delivering to the client a suitable set of Fund Facts for review and prevents the client from examining *en masse* various suitable alternative investments at his or her convenience; it will therefore extend – at the client's expense – the time needed by the advisor to make suitable recommendations and, in the end, gather finalized instructions from the client.

However, permitting bundled delivery of Fund Facts will enable the client to review the material at his or her discretion and, after the next in-person meeting or telephone conversation with the advisor, make a more informed investment decision and issue instructions to the advisor, who in turn can immediately proceed to the trade's execution.

With regard to the use of multiple Fund Facts documents, it is interesting to note that the *CSA Point of Sale Disclosure Project: Fund Facts Document Testing* report stated that many retail investors felt that "having Fund Facts would make the decision easier for them and the job easier for their advisers"[8]; but in terms of maximizing the utility for the investor offered by Fund Facts, participants were explicit on the benefits of being able to consider multiple Fund Facts with regard to a single fund purchase

> The adviser should recommend 3 or 4 funds and give me [Fund Facts for them]. I'd go home and discuss it with my wife. Then I'd like to go back and discuss it with him [FA], circle different points. Then I'd go home again, check with my wife and decide[9]…
>
> More knowledgeable investors want to look at more than one mutual fund using Fund Facts, their adviser's comments and their own research on the internet, in newspapers and Morningstar. Fund Facts would be very valuable for considering multiple mutual funds, because using the clear structure of the document they could easily compare the different funds section by section.[10]

Advocis believes it is clearly in the best interests of Canadian retail investors that the CSA remove the bundling restriction on Fund Facts delivery.

The timing of the pre-sale delivery

Another puzzling aspect of the Proposed Amendments concerns the timing of the pre-sale delivery. There is guidance in the proposed *Companion Policy* that investors must be given a "reasonable

[8] Canadian Securities Administrators, *CSA Point of Sale Disclosure Project: Fund Facts Document Testing* (prepared by Allen Research Corporation), September 2012, p. 57. Accessible at www.osc.gov.on.ca/documents/en/InvestmentFunds/pos_ www.osc.gov.on.ca/documents/en/InvestmentFunds/pos_201209_fund-facts-doc-testing.pdf.
[9] *Ibid*., p. 56.
[10] *Ibid*., p. 57.

opportunity" to consider the information in the Fund Facts before proceeding with the purchase, and that it "should not be delivered or sent so far in advance of the purchase of a security of a mutual fund that the delivery cannot be said to have any connection with the purchaser's instruction to purchase the mutual fund."[11] The CSA seems to envision the advisor either speculating on the mental state of the client, or seeking formal determination of whether or not the Fund Facts motivated the client to buy the mutual fund. Perhaps the CSA expects the advisor to explicitly ask if the Fund Facts is "connected" with the client's "instruction to purchase the mutual fund."[12]

Interestingly, in the *CSA Point of Sale Disclosure Project: Fund Facts Document Testing* report, the authors note (in Section 7, entitled *The Ideal Process*), that "Many retail investors wanted to receive Fund Facts 1 to 3 weeks in advance of meeting with their adviser. They would then make notes on it and prepare questions for their meeting."[13] It would thus seem difficult for an advisor to comply with the proposed changes to National Instrument 81-101 and its *Companion Policy* while simultaneously maximizing the utility for the client of the Fund Facts document: while an advisor is told that Fund Facts should not be delivered or sent so far in advance of the mutual fund purchase that its delivery cannot be said to be connected to the purchase – in itself an odd and vague test – the evidence available clearly states that receipt of the Fund Facts weeks in advance is "wanted" by "many retail investors."[14] Again, one may wonder if to CSA- compliant, if the advisor should or is expected to query the client regarding the connection, if any, of the time of the Fund Facts' delivery with his final investment decision?

In addition, it is unclear if the standard of "before" may mean a period of time as brief as several minutes prior to the advisor receiving and implementing the client's instruction to purchase the mutual fund. Certainly there are clients who are sophisticated enough to evaluate a Fund Facts sheet and arrive at an informed decision in a span as brief as several minutes. The guidance in the proposed *Companion Policy* – that the CSA expects investors will be given a "reasonable opportunity" to consider the information in the Fund Facts before proceeding with the purchase – would be clearer if it indicated that the test depends on the capacities and capabilities of the individual client, or on those of a hypothetical "reasonable client." A client experienced with equity funds but not, for example, with balanced funds, will need varying amounts of time depending on the investment. Determining this may be a difficult proposition for the advisor – and indeed could become a source of friction between the client and advisor. The "bright line" standard offered by the requirement for delivery within two days of the trade at least offers both parties a higher degree of certainty.

[11] Canadian Securities Administrators, *Notice and Request for Comment – Implementation of Stage 3 of Point of Sale Disclosure for Mutual Funds, op. cit*., p 3148.
[12] *Ibid*.
[13] Canadian Securities Administrators*, CSA Point of Sale Disclosure Project: Fund Facts Document Testing*, *op. cit*., p. 56.
[14] International Organization of Securities Commissions, *op. cit*., p. 28.

Documenting the client's receipt of Fund Facts, pre- or post-sale delivery

Next, we note the issue of proof of the client's receipt of the Fund Facts document. The Proposed Amendments to National Instrument 81-101 and its *Companion Policy* are silent on whether the advisor or dealer is *explicitly* obligated to get proof of receipt *before* executing the trade. The Proposed Amendments to the National Instrument simply provide that:

> **3.2.1.1 Delivery of Fund Facts Document**
> (1) Before a dealer accepts an instruction for the purchase of a security of a mutual fund, the dealer must deliver or send to the purchaser the most recently filed fund facts document for the applicable class or series of securities of the mutual fund.[15]

It should be noted that the CSA does not currently require evidence of prospectus delivery to clients from advisors; it may be the case that the Investment Industry Regulatory Organization of Canada (IIROC) and the Mutual Fund Dealers Association of Canada (MFDA) would prefer that this situation also apply to Fund Facts delivery. One suspects that without clear direction from the CSA, the default position will be a requirement of proof of client pre-sale receipt of Fund Facts.

In terms of the exemption permitting post-sale delivery of Fund Facts when "delivery is not reasonable practical," the *Companion Policy* states that *proof in writing* from the purchaser of receipt of the Fund Facts is not required, but that *evidence of delivery* of the Fund Facts document and receipt of purchaser consents to post-sale Fund Facts delivery *is* required. This is unfortunately somewhat vague; the CSA states that it expects advisors and dealers to continue to rely on their current policies and processes in this regard. From the *Companion Policy*:

> **7.3. Post-Sale Delivery of the Fund Facts Document**
> (5) In accordance with existing practices, dealers must establish internal policies and procedures to ensure delivery of the fund facts document occurs in accordance with section 3.2.1.1. *Dealers must maintain evidence of delivery of the fund facts document, as well as receipt of purchaser consents to receive delivery of the fund facts document after entering into the purchase of a security of a mutual fund.* Dealers must also maintain adequate records to evidence that satisfactory disclosure about the fund facts document has been provided to purchasers in compliance with subsection 3.2.1.1(3). Such records should also indicate why delivery of the fund facts document was impracticable in the circumstances. The Canadian securities regulatory authorities expect that dealers will follow their current practices to maintain evidence of required disclosures to sufficiently document delivery of the fund facts document.

[15] Canadian Securities Administrators, *Notice and Request for Comment – Implementation of Stage 3 of Point of Sale Disclosure for Mutual Funds, op. cit*., p 3149.

> (6) The Regulation does not specify a particular manner of evidencing a purchaser's consent to allow delivery of the fund facts document after entering into the purchase of a security of a mutual fund. *In particular, the Regulation does not require dealers to obtain written consent from clients. The Canadian securities regulatory authorities expect that dealers will follow their current policies and procedures for tracking and monitoring client instructions and authorizations* (emphases added).[16]

Pragmatically, once the CSA states that the standards which the advisor and dealer have to meet in the exempted cases of post-sale delivery are the requirements set out in section 7.3 (2), what choice will the advisor and dealer have but to assume out of an abundance of caution that evidence of delivery should be generated, documented and retained in their records in *all* cases? Since the CSA has explicitly stated in the *Request for Comment* that "availability does not equal delivery", Advocis members have reported that many dealers have understandably concluded that electronic delivery of a link to the Fund Facts will not be CSA-recognized proof of client receipt and so they have assumed the necessity of creating an entire recordkeeping regime dedicated to proving Fund Facts delivery. Once again, this sort of compliance-to-prove-compliance drives up costs across all industry players – yet does nothing to enhance disclosure to and protection of Canada's retail investors.

Finally, proposed section 3.2.1 (2) states a dealer is "not required to deliver or send the fund facts document if the purchaser has previously received the most recently filed fund facts document" for the mutual fund at issue." [17] It would be helpful to know if the advisor or dealer is supposed to verify this receipt if the client reports that he received the most recent Fund Facts from a third party, such as another advisor, and whether the client simply downloading the most recent Fund Facts from the web on his own initiative will qualify as receipt for the purposes of this section. Again, the problem is two-fold: (1) it is unclear how far the advisor is expected to go to document receipt by the client of the most recent Fund Facts: for example, is a client statement over the telephone that "another advisor sent it to me sufficient"?; and (2) the resulting strain on the advisor-client relationship if the advisor is expected to "second guess" or otherwise act doubtful of the client's statement regarding receipt: for example, is the advisor expected to delay the fund purchase by insisting the client must first have demonstrated receipt from a party other than the advisor, failing which the client must wait until he receive the Fund Facts document from the advisor?

Shifting the burden of recording proof of receipt: Daily recordkeeping versus intervention-focused regulation

From a fairness standpoint, it would be more justifiable to have all advisors and dealers exempted from requiring proof of pre-sale delivery, *until* the regulator determines that pre-sale delivery is not

[16] *Ibid*., p. 3149.
[17] *Ibid*., p. 3145.

being properly executed by an advisor or dealer. At that point, the laborious and costly requirement of documenting proof could be applied to the miscreant as a disciplinary measure – one with a distinctly laudable consumer protection justification. Certainly, the vast majority of compliant advisors would not have to bear unnecessary compliance costs.

However, regardless of the contents of the Proposed changes National Instrument 81-101 and its *Companion Policy*, in its *Request for Comment* the CSA *does* envision the advisor or dealer having to document the client's receipt of the Fund Facts document. The *Request for Comment* states that:

> We recognize dealers will express concerns regarding compliance with the proposed requirements to utilize the exception to pre-sale delivery. *As noted in the Companion Policy, dealers will be required to maintain adequate records relating to fund facts delivery generally, whether pre-sale or post-sale*… we expect that dealers will be able to follow their current practices of maintaining evidence of required disclosures to document delivery of the fund facts document (emphases added).[18]

In particular, are there circumstances where post-sale delivery of the Fund Facts should be permitted but are not captured in the Proposed Amendments?

Yes.

Advocis is concerned how the Proposed Amendments represent a retreat from the exemptions set out in the original 2009 Fund Facts proposal. The CSA now proposes that the pre-sale delivery requirements will apply to *all* purchase orders for *all* types of mutual funds. This includes both initial and subsequent purchases of units in the same mutual fund – unless the client received the most recent Fund Facts on a previous purchase. In contrast to this over-inclusive regime, which the CSA justifies as an industry-friendly cost-savings simplification of the 2009 proposals, Advocis believes that the current reality that all Fund Facts documents are posted on publicly accessible web sites should be sufficient justification to enable clients to waive pre-sale delivery of Fund Facts.

Exemptions from the requirement of pre-sale delivery of Fund Facts

The most obvious circumstances where post-sale delivery of the Fund Facts should be allowed would fall under the following proposed permissions:

[18] Canadian Securities Administrators, *Notice and Request for Comment – Implementation of Stage 3 of Point of Sale Disclosure for Mutual Funds, op. cit.,* p. 3141. This is Annex C of the Proposed Amendments, and is entitled, "Summary of Public Comments on Proposed Delivery Framework Implementation of Point of Sale (POS) Disclosure For Mutual Funds (June 19, 2009). It contains a summary of the comments on the 2009 Proposal and the CSA's current position on those comments with regard to pre-sale delivery of Fund Facts.

1. **A general right to waive delivery when the client expresses his preference to not receive summary disclosure:** Advocis believes that all investors be permitted to waive pre-sale delivery of the Fund Facts document, and, if they wish, its delivery post-sale as well. While the default position of the CSA should be that investors should receive the Fund Facts annually for any mutual fund in which they hold units, the consumer should be empowered with the ability to annually opt out of receiving Fund Facts. Many investors are quite capable of visiting and downloading a fund company's web site the funds they hold. Fund Facts have been widely available on the web since 2011. Advisors should be permitted to ask their clients for annual instructions or standing instructions in manner analogous to the continuous disclosure process set out in National Instrument 81-106 - *Investment Fund Continuous Disclosure*.

   The basis for the right to opt out of Fund Facts delivery should in the form of the investor's express declaration that he or she wishes to do so. It could be a clause in the account agreement and subject to mandatory annual renewal in writing. Another form of a possible general exemption could be based on the client signing an acknowledgement document upon the purchase of a mutual fund that he or she has already assumed the onus of securing a copy of the Fund Facts for the mutual fund at issue, and will bear the responsibility for securing the most recent copy for the mutual fund's Fund Facts prior to any new trade instructions for that fund being conveyed to the advisor or broker.

   There is in fact evidence to support the creation of a general waiver of pre-sale delivery of Fund Facts. The *CSA Point of Sale Disclosure Project: Fund Facts Document Testing* study found that eight per cent of the participants reported wanting Fund Facts only *after* the purchase (among younger investors, this figure almost doubles: "Interestingly among the youngest group some 15% want to take home after purchase with 48 hours to decide whether to cancel or not."[19] As well, seven per cent of participants stated that "they would not want Fund Facts at all." [20] In other words, fully fifteen per cent of those tested expressed as an *initial* reaction that they would not want receipt of Fund Facts on a pre-sale basis, if at all.

2. **When delivery is not practical due to time constraints**: Advocis agrees with the proposed exemption from pre-sale delivery in cases where the client indicates a desire to complete the purchase of a recommended fund immediately or by a specified time, and it is impossible for the advisor to complete physical or electronic pre-sale delivery of Fund Facts. However, as we argue in response to CSA question (b), below, the requirement that the advisor "verbally disclose" specific salient features of the recommended fund is excessive. Essentially, the advisor is in a position where to fulfill the client's wishes he does not have the time to go the fund company's web site, download a copy of the fund's Fund Facts, and email it to the client – yet he is

[19] Canadian Securities Administrators*, CSA Point of Sale Disclosure Project: Fund Facts Document Testing*, *op. cit*., p. 94.
[20] *Ibid*.

expected by the terms of the exemption to produce a copy of it for himself and then review the key text of it in an in-person or telephone conversation with the client *before* executing the trade. In cases where "time is of the essence," this requirement is clearly absurd. Instead, we would submit that the exemption require that the advisor document the request, and delivery the Fund Facts document as soon after the purchase as possible, and definitely within two days of the purchase.

3. **An exemption for more experienced/sophisticated investors**: In the absence of a general right to waive delivery of Fund Facts (or at least its pre-sale delivery), Advocis would support the CSA in developing an exemption which distinguishes between typical retail investors and sophisticated individuals. Individual Canadian investors vary greatly in their level of understanding of investments, markets, and risk; some will have a high degree of sophistication, experience, knowledge and capability, and others will possess much lower degrees of acumen. Investors of a similar capacity of sophistication should be afforded a similar, appropriate *de minimus* levels of protection – as well as freedom from unnecessary regulatory constraints. Such investors should be able to transact immediately without expecting pre-delivery of Fund Facts.

   In fact, an nuanced exemption from delivery of the Fund Facts, or at the least from pre-sale delivery, on the basis of accredited investment acumen of an investor is a more conceptually sound basis for differentiation than some of the proposed exemptions set out the CSA's 2009 *Request for Commen*t. It is far better to draw a distinction between retail clients on the grounds of previous investing experience and acumen, than to simply place the same regulatory burden on all of them. Arguably, investors who meet the criteria of the exempt market category of accredited investor should be able to waive delivery of the Fund Facts, given that they typically have a higher level of investment acumen or access to sophisticated financial advice.

4. **An exemption for money market funds when their NAVPS does not fluctuate in value:** Money market funds are lower risk and are generally used by investors to "park" money in a way which maintains liquidity on a short-term basis. When the value of a money market fund's net average value per share or NAVPS does not fluctuate, that fund represents such a stable investment that the delivery of Fund Facts prior to purchase should not be required. Accordingly, an advisor should not have to provide the client with a Fund Facts for this subgroup of money market funds unless the client explicitly requests one pre-sale; the Fund Facts would then be sent with the trade confirmation. However, money market funds which can realize capital gains or losses should be treated like all other mutual funds for summary disclosure purposes.

b) When pre-sale delivery is impracticable, one of the conditions for post-sale delivery of the Fund Facts is that the dealer provides verbal disclosure to the purchaser of certain elements contained in the Fund Facts. Please comment on whether the proposed disclosure elements are appropriate.

While Advocis wholly agrees with the general spirit of this exemption to permit trades to be executed without advance delivery of Fund Facts, we have serious concerns about the number of conditions attached to it. The dealer must consider that it is not "reasonably practicable" to deliver the Fund Facts to the client before the specified time of the trade and the advisor must provide extensive and quite specific verbal disclosure to the client.

Required verbal disclosure

The Proposed Amendments will require the advisor or dealer to provide "verbal disclosure" of all of the following sections of the Fund Facts document:

1. "What does the fund invest in?" (Item 3 of Part I): a description of the fundamental features of the mutual fund, and what it primarily invests in;
2. "How risky is it?" (Item 4 of Part I): the investment risk level of the mutual fund;
3. "Who is this fund for?" (Item 7 of Part I): a brief statement of the suitability of the mutual fund for particular investors;
4. "How much does it cost?" (Item I of Part II): an overview of any costs associated with buying, selling, and owning a security of the mutual fund ; and
5. "What if I change my mind?" (Item 2 of Part II): a summary of any applicable withdrawal rights or rescission rights to which the purchaser is entitled.[21]

In other words, the advisor will be required to essentially read aloud the bulk of the text of the Fund Facts document, prior to purchasing the fund for the client. In instances where "time is of the essence," mandating this "verbal disclosure" for all investors who seek to obtain the exemption from pre-sale-delivery is self-defeating. The time commitment needed to obtain the exemption could very well run longer than the investment window. Moreover, in the case of client-initiated trades, especially by seasoned investors, this mandatory verbal disclosure will amount to an annoyance and delay *at best* – and one for which fee-only advisors will have to charge the client. This outcome strikes us as patently excessive.

The procedural requirements required by the exemption

As noted, if the client indicates that the purchase must be completed immediately or by a time specified by the client, then the advisor or dealer must comply with an elaborate process. The CSA in its *Companion Policy* provides that the request must be client-initiated. As we understand it, this means that:

1. the client must want to purchase the mutual fund immediately or within a specified time frame and communicate this explicitly to the advisor;

[21] Canadian Securities Administrators, *Notice and Request for Comment – Implementation of Stage 3 of Point of Sale Disclosure for Mutual Funds, op. cit.,* pp. 3145-6.

2. the client must then be informed by the advisor that presale delivery of Fund Facts is not reasonably practicable (note that this standard of impracticality is presumably to be defined, applied and assessed solely by the advisor);
3. the client must expressly state that he or she still wishes to go ahead with the trade;
4. the client must have the exemption and its conditions explained to him by the advisor, including the copious verbal disclosure set out in the Proposed Amendments;
5. the client must consent to the post-trade timing of the Fund Facts' delivery;
6. the client must indicate that he or she wishes the trade to be processed immediately or at a specific time; moreover, the client's instructions to proceed and consent to this delivery timing will only apply to the specific transaction, so no standing instructions will be allowed; and
7. the client must receive the Fund Facts within two days after the trade.

Consequences for the advisor-client relationship

In terms of the client-advisor relationship, the exemption is simply too stringent. It places the onus on the advisor to: (1) assess the "not reasonably practicable" standard of pre-sale delivery and to explain this standard to the client; (2) explain that the exemption is limited in applicability to the specific transaction at hand; and (3) explain the outright prohibition against standing instructions to execute mutual fund purchases under this exemption. Indeed, Advocis members already foresee that many clients will want to issue to their advisor standing instructions to proceed with trades in advance of Fund Facts delivery; it will be difficult, to say the least, for advisors to explain to clients that this is not permitted.

Additional compliance consequences for the advisor

In terms of advisor compliance pressures, the advisor will have to determine the specifics of his or her recordkeeping obligations and auditing requirements to satisfy the rules. It should be noted that the CSA states that "Such records should also indicate why delivery of the fund facts document was impracticable in the circumstances." (Presumably "impracticable" means the same as "not reasonably practicable").

This guidance means that the entire set of circumstances supporting the advisor's judgment call to rely on the exemption, which by definition must made in "the heat of the moment," will have to be committed to paper almost immediately afterwards, and in a way which will withstand third-party scrutiny months later.

In addition, the CSA does not specify what evidence is sufficient to document the client's consent to allow delivery of Fund Facts document post-sale, except to state that the advisors are "not required to obtain written consent from clients" and that they are expected to "follow their current policies

and procedures for tracking and monitoring client instructions and authorizations."[22] In other words, the onus rests solely on the advisor to document a decision initiated by the client.

How useful is the exemption as currently drafted?

It is difficult to imagine an advisor wanting to take on the obligations entailed by this exemption, especially if the "not reasonably practicable" standard is to be interpreted by the lights of what a hypothetical advisor, and not as what is "reasonable practicable" in that particular advisor's *own* practice at the *time* of the purchase discussion. A further complication is to the "reasonable practicality" standard comes to the fore when we consider the client's own unique and personal standards: depending on the client's goals and savings strategy and situation, an advisor may feel it is in the best interest of the client that the trade be executed under this exemption, even if he or she suspects that the reasons for relying on the exemption may be judged as too subjective by a regulator "looking over his shoulder" after the fact.

Presumably the staff of the Mutual Funds Dealers Association of Canada and the Investment Industry Regulatory Organization of Canada will arrive at guidelines; the risk is that the guidelines will be drafted too restrictively and the exemption is all but lost. This seems a real possibility. Indeed, the CSA in the proposed *Companion Policy* states that "regulatory authorities may examine practices or arrangements that raise the suspicion of being structured to permit dealers to do indirectly what they cannot do directly and that are inconsistent with the overall intent of providing key information to investors at a time that is most relevant to their purchase decision."[23]

In the light of all this, one wonders how useful this exemption from pre-delivery will be, since the CSA explains in its proposed *Companion Policy* that they "expect that post-sale delivery of the fund facts document will be the exception rather than the norm."[24]

If not, what additional disclosure should be included?

There should be no additional disclosure included.

Alternatively, are there any disclosure elements that should be excluded?

Advocis strongly supports permitting delivery of the Fund Facts document with the confirmation of trade documentation in cases where the investor expressly communicates that he or she wishes the purchase to be completed immediately.

We would suggest the following changes to the pre-sale verbal disclosure requirement:

[22] Canadian Securities Administrators, *Notice and Request for Comment – Implementation of Stage 3 of Point of Sale Disclosure for Mutual Funds,* p. 3149.
[23] *Ibid*.
[24] *Ibid*.

1. The requirement for pre-sale verbal disclosure should be made optional and deliverable only at the client's express request.

In the alternative, we would suggest the CSA consider the following options as amendments to the pre-sale verbal disclosure requirement:

2. A category of knowledgeable and experienced investor should be created. Members of this class would have the ability to exempt themselves from the pre-sale disclosure requirement, if they so desire, including those individuals who would qualify as an accredited investor for exempt market products.

3. A signed consent form which creates a standing instruction from the client to purchase a mutual fund, without pre-sale delivery of the Fund Facts, should be allowed under the Proposed Amendments.

In each of these cases, the advisor should be required take reasonable steps to communicate verbally to the client that he or she will receive the Fund Facts document with the trade confirmation, at which time he or she should review it, and that as a purchaser they possess the right to rescind the purchase within two days following the receipt of the Fund Facts document.

c) In the case of pre-authorized purchase plans, a Fund Facts would only be required to be sent or delivered to a participant in connection with the first purchase provided that certain notice requirements are met. Please comment on whether the Fund Facts should also be sent or delivered to a participant if the Fund Facts is subsequently amended and/or every year upon renewal of the Fund Facts.

The CSA's exception for pre-authorized purchase plans as drafted holds that the requirement for pre-sale delivery will not apply to subsequent purchases of a mutual fund, *if* the dealer provides initial and subsequent annual notices to the investor with information on how to access and request the Fund Facts for the fund, and has a statement that the purchaser will not have a right for withdrawal of the purchase (the purchaser of a pre-authorized plan will continue to have a right of action for rescission or for damages if there is a misrepresentation in the prospectus of the mutual fund, including any documents incorporated by reference into the prospectus, such as the Fund Facts).

Advocis is in agreement with the portion of the Proposed Amendments which hold that mutual fund purchases by a participant in a pre-authorized purchase plan will not require delivery of the Fund Facts, provided the purchase is not the first purchase under the plan and certain notice

requirements are met. We assume that this amendment is effective only until the renewal of the Fund Facts document.

We further support the requirements that the participant must receive information about how to access the fund facts document electronically, that he or she may terminate the plan at any time, and while there is no right of withdrawal for subsequent purchases under the plan, he or she will continue to have a right of action for damages or for rescission if there is a misrepresentation in the Fund Facts document, as well as in the prospectus, the annual information form, and so on.

But with regard to the main thrust of the Proposed Amendments governing pre-authorized purchase plans – which provide that a participant would not receive a Fund Facts document after the date of the notice, unless he or she specifically requests it – we would argue the reverse: namely, that investors participating in pre-authorized purchase plans, who are typically less engaged in routine and ongoing monitoring of their accounts, *should* have the Fund Facts delivered to them *whenever* the Fund Facts is amended. Changes in risk classification are of real significance to plan participants approaching retirement. The largely passive nature of these investors, and the largely impersonal, advice-free and automated process of pre-authorized purchases, also makes us support annual Fund Facts delivery to participants upon renewal of the Fund Facts. However, participants should be given the option to opt out of delivery of the Fund Facts if they so desire. We would also specify that providing electronic access to the Fund Facts document, such as a link to a pdf, should constitute effective delivery.

In addition, group registered savings plan accounts held in mutual funds should warrant the same treatment as pre-authorized purchase plans. Participants in company-sponsored group registered savings plans are in a similar position, since in most plans the employer sends the participant's monthly contribution directly to the fund company, and the fund company buys more of the same funds monthly. The initial purchase disclosure and further production upon amendment of the Fund Facts only makes sense in terms of protecting this subgroup of investors.

If so, what parameters should be put in place for such delivery? For example, should it be delivered in advance of the next purchase that is scheduled to take place after the Fund Facts has been amended or renewed?

Advocis would suggest that the dealer should have the choice of delivering Fund Facts to the participant for either (1) the first trade after the Proposed Amendments to National Instrument 81-101 have taken effect, or (2) in advance of the next purchase scheduled to take place after the Fund Facts is amended or renewed. This will alert the individual to the existence of Fund Facts, not just for his or pre-authorized purchase plan, but as an informational tool available for *all* mutual funds, thereby furthering the goals of consumer education and protection.

Or would post-sale delivery be more appropriate?

Given that there is no right of withdrawal for subsequent purchases under the pre-authorized purchase plan, post-sale delivery to this largely passive and less sophisticated audience seems inappropriate.

B. Compliance

2. The CSA expect that dealers will follow current practices to maintain evidence sufficient to demonstrate effective delivery of the Fund Facts. Are there any aspects to the requirements in the Proposed Amendments that require further guidance or clarification?

Yes.

If so, please identify the areas where additional guidance would be useful.

Advocis believes the following three areas are deserving of additional guidance:

1. methods of delivery of the Fund Facts document: please see our position set out above in "A. Exceptions from Pre-Sale Delivery of the Fund Facts";
2. the mutual fund risk methodology of the Fund Facts document: please see our position as set out in our submission of March 12, 2014 to the CSA on CSA Notice 81-324 and Request for Comment *Proposed CSA Mutual Fund Risk Classification Methodology for Use in Fund Facts*[25]; and
3. general withdrawal and rescission rights: please see our position set out in Part One, above.

C. Anticipated Costs and Benefits of Pre-Sale Delivery of the Fund Facts

3. We seek feedback on whether you agree or disagree with our perspective on the benefits and costs of implementing pre-sale delivery of the Fund Facts. Specifically, do you agree with our view that the costs will be incremental in nature and/or one-time cost?

No. The costs will be continuous and ongoing – and if history is any guide then the Fund Facts document itself will very likely be subjected to future amendments in terms of required content within one to two years from when the proposals first take effect. Depending on the business logic of a registrant's delivery system, adjusting the system to implement and record pre-sale delivery will

[25] Available online at http://www.advocis.ca/regulatory-affairs/RA-submissions/2014/Advocis-Response-CSA-Notice-81-324.pdf.

result in a not inconsiderable effort every time a new fund or new client is added to their back-office systems.

Consider the scope of the Fund Facts enterprise, which will entail copious compliance and production systems preparation and updating by the mutual fund companies; printing by advisors for clients, and hard and soft copy deliveries by advisors to clients; new documentation and recordkeeping obligations for dealers and advisors; preparing for and executing dealer audits, and numerous dealer-related compliance functions: this amounts to a very expensive process change, and every subsequent change to Fund Facts will have ripple effects on administrative, compliance and distribution systems.

Two observations immediately suggest themselves: first, that this is a transfer of the cost of printing and distributing disclosure documents from the mutual fund companies to the distribution arm of the industry. Second, all of this disclosure is being driven forward without assurances that retail investors will realize costs savings; i.e., do consumer groups or regulators anticipate or expect that any portion of a fund's management expense ratio will be reduced for retail investors? This is a valid concern, as operational savings from the cessation of prospectus distribution to investors may lead to the realization of material profits for fund company shareholders – while the distribution network of dealers and advisors pay for the bulk of the costs associated with the new Fund Facts regime.

We have already seen the establishment of a sub-industry of web sites which offer advisors access to libraries of Fund Facts forms, with delivery to clients, documentation of client receipt and other recordkeeping and fulfillment services also offered. Access for basic Fund Facts support starts at the $300.00 per year price point and rises rapidly thereafter. Across the advisory industry, then, advisors and dealers will soon be paying a significant amount of money for Fund Facts access and support, and much of it borne by independents and small firms.

We request specific data from the mutual fund industry and service providers on any anticipated costs.

While we have no specific data to share with the CSA, we believe we can offer some insight into what types of data may be of use. We believe that a cost/benefit analysis is essential for creating a fair and effective point of sale disclosure framework. Two concerns regarding fairness are critical here: (1) minimizing the impact of the regulatory action on those actors least able to bear it, such as small and independent firms and advisors, and (2) ensuring the policy framework adopted works to reduce those costs which will ultimately be borne by the consumer or retail investor. In terms of effectiveness, we would suggest that a trial program be conducted among a representative sample of dealers and advisors to gather data and see if the costs associated with pre-sale delivery of the Fund Facts can be justified in terms of its utility for retail investors.

Advocis Submission, National Instrument 81-101 - Pre-Sale Delivery of Fund FactsEvaluating costs/benefits to the mutual funds industry

A fair number of independent mutual fund companies in Canada are dependent on third party distributors, who rarely deal with clients face-to-face and often rely on telephone conversations or other impersonal means of communication. A pre-sale delivery requirement for Fund Facts will affect these companies in a disproportionate manner. Conversely, the pre-sale requirement will no doubt be less onerous for bank-owned distributors, who enjoy the ability to meet with clients at a local branch, thereby more readily facilitating personal pre-sale delivery of Fund Facts.

Also problematic is the impact on an advisor's product shelf. Presale delivery will make it more difficult for smaller and independent advisors and dealers to distribute a wide selection of mutual funds. To ensure effective delivery of the Fund Facts document and to maintain the ability to complete transactions on a timely basis, the advisor may be forced to narrow his or her "product shelf." A reduction in product choice, by disadvantaging smaller dealers, their advisors and their clients (particularly rural ones), could over time affect the level of competitiveness of the mutual funds industry.

Prior to implementation of pre-sale delivery, we would like to see the CSA provide some macro-level analysis of the impact to the various industry actors, including smaller firms, independents, and bank-owned distributors.

Evaluating the costs to individual actors

It is important to note that the costs of implementing the point of sale delivery requirements are in addition to those involved with implementing the various CRM-2 requirements. It is clear that there are substantive costs in retooling existing document production and delivery and compliance systems. As for the alternative option, the costs of contracting with a service provider to handle Fund Facts production, delivery and compliance tasks are no less formidable, especially for smaller firms which cannot realize the economic benefits of scalability.

The cost burden of the Proposed Amendments could be immediately reduced by: (1) giving retail investors the option to elect to opt of receiving delivery of Fund Facts altogether, and (2) by specifying that for retail investors who wish to receive Fund Facts electronically, an email containing a link to a downloadable and printable version of the Fund Facts document will satisfy delivery requirements.

The *general* costs associated with implementing the Fund Facts point of sale framework largely break down into (1) the document production and administration costs of drafting, printing, updating, filing, and administering the Fund Facts document; and (2) the delivery costs of delivering hard copies, or emailing electronic links or attached soft copies.

As against this general framework, the *specific* costs of implementing the *pre-sale delivery* of Fund Facts will generally fall into four categories: (1) the administrative and production/delivery costs associated with having to send the Fund Facts document separately, instead of combining it with the trade confirmation; (2) the operational costs associated with creating and running a process to ensure for *timely* pre-trade delivery of Fund Facts; (3) the costs of sufficiently documenting client receipt of the Fund Facts; and (4) the opportunity costs which arise from certain fact patterns – such as in the case when pre-sale delivery is impractical and the advisor has to read the bulk of the Fund Facts text to the client over the telephone.

Indeed, developing the business logic to ensure *accurate and timely pre-trade* delivery of Fund Facts, especially in "hard copy" printed format, will prove challenging and time-intensive for those persons responsible for designing and managing back office compliance protocols. Of particular concern is the ability of smaller firms to bear the costs of Fund Facts delivery. While larger operations can develop their own scalable compliance systems, or rely on external suppliers, many dealers and their advisors will not be able to develop or purchase a fully automated platform that can deliver Fund Facts electronically or by print and mail, depending on the investor's preference, plus provide documentation of the client's receipt of Fund Facts – and do so in a timely pre-trade manner. Many registrants will have to rely on a largely manual and time-intense implementation and recording of pre-sale delivery.

Evaluating the benefits

The pre-sale delivery of the Fund Facts document in electronic form is an appropriate complement to the ongoing roll-out of CRM-2 – *unless* the client formally and expressly wishes to opt out of receipt of Fund Facts. Customers should be able to manage their advisory "relationship" to stop receipt of information which they do not want or need. Otherwise, the words "Customer" and "Relationship" in the acronym CRM risk becoming terms of irony.

On the whole, however, pre-sale delivery, where possible and where desired by the client, is of a piece with the CRM's pre-sale disclosure of fees, account fees and charges, trade confirmations, enhanced client statement disclosure requirements and the detailed annual performance statement. In short, pre-sale delivery will continue the CSA's move toward transparency, improved investor protection and enhanced levels of financial literacy.

Pre-sale delivery of Fund Facts, subject to the qualifications we have outlined above, has the potential to benefit many stakeholders. Advisors can use the Fund Facts document as a tool to deliver informed advice (and document its delivery), and retail investors should as a result make better choices in regard to individual fund recommendations and the "fit" of each fund with their overall portfolio and savings strategy. Arguably fund companies themselves will be able to learn more about the needs of Canada's capital markets as asset allocation by retail investors becomes more informed by the use of the Fund Facts document.

In terms of enhancing advisor professionalism, pre-sale delivery of Fund Facts is consistent with requirements on securities registrants to deal fairly, honestly and in good faith with clients, and for this reason the prompt development of summary disclosure documents for other investment products, such as exchange-traded funds, is desirable.

Finally, we would urge the CSA to begin conducting trial research once the Proposed Amendments are finalized and before they take effect to determine if the use of Fund Facts in general may be linked to a reduction in investor complaints and to increases in investor satisfaction and financial literacy. More particularly, we would like to see data on the percentages of consumers who actually rely on Fund Facts in making investment decisions and, in specific, if how many investors report benefitting from pre-sale delivery, in what manner and to what extent.

D. Transition Period

4. We seek feedback from the mutual fund industry and service providers on the appropriate transition period for full implementation of the Proposed Amendments.

General feedback on implementing Fund Facts

The implementation of Fund Facts and of CRM-2 must be seen as an ongoing consultative process of graduated implementation. Their mutual goals should be the facilitation of concise, straightforward communication to investors, including summary disclosure documents, when the investor wants them. Enhanced disclosure to mutual fund investors should and must be part of a larger disclosure effort for other retail investment products.

That said, exposing Canadians to the frustrations and risks which inevitably come with unnecessarily accelerated implementation schedules is problematic; to do so when the complex demands of CRM-2 are reaching their peak – externally in the form of client education and internally in the form of adjusting and perfecting in-house administrative and compliance systems – is imprudent. This conclusion is all the more inescapable once it is recalled that any given Fund Facts document is now readily obtainable from the relevant fund company's web site by anyone with Internet access.

However, the CSA has released the Proposed Amendments with an uncharacteristically tight 60-comment period and appended to the *Request for Comment* the descriptor "second publication," even though the current proposal represents more or less an entirely new delivery regime. The CSA also refers in its *Request for Comment* to a possible one-year transition period, as well as a potential three-month transition period. From this one may conclude (perhaps wrongly) that the CSA is seeking to make pre-sale delivery effective on a dramatically aggressive timeline – perhaps as early as the first half of 2015.

Advocis believes that the best interests Canada's retail investors and capital markets will be better met by having stakeholders focus on the successful implementation of CRM-2 and on the finalization of further refinements to the Fund Facts document. Once outstanding concerns – including questions regarding risk methodology – are settled, then and only then should the CSA should begin the process of mandating Fund Facts' pre-sale delivery.

While the CSA asserts that implementation of the Proposed Amendments will be a process "incremental in nature," many advisors will not agree. The fact is that stakeholders have been intensely committed to implementing CRM-2: for advisors, explaining CRM-2 in conjunction with Fund Facts and its latest revisions is a time-consuming and ongoing exercise; adding pre-sale delivery to the mix at this stage is simply at odds with the goal of bringing clear, concise disclosure to investors.

Proposed "go-live" dates for Fund Facts pre-sale delivery

We would propose that the pre-sale delivery requirements, in whatever final form they take, not take effect until mid-2016. *At minimum* we would wish to see a twelve-month transition period before amendments to National Instrument 81-101 take effect. This should be a sufficient period of time to let dealers and advisors train their staff and make necessary preparations. Rather than trying to mandate a go-live date for presale-delivery in the next three to six months, Advocis believes that co-ordinating Fund Facts' delivery requirements with those obligations of CRM-2 which take effect in July 2015 or July 2106 is a more appropriate plan of action. The constant evolution and roll-out of CSA reforms is taxing enough on industry actors; rushing into pre-sale delivery with such minimal notice will prove counter-productive to the project's goals. But harmonizing pre-sale delivery with the final scheduled set of CRM-2 changes coming in 2016 would give the industry a final date for a host of production and disclosure requirements; working toward a "final unified date" would make it logistically easier for industry stakeholders to ensure all compliance, delivery and administrative systems are properly functional. Failing the adoption of a July 2016 date, coordinating pre-sale delivery with the changes in CRM-2 which take effect in July 2015 would be advisable. We would urge the CSA to continue to comply with the concept of a properly timed, multi-stage implementation of the point of sale framework, as set out in CSA Staff Notice 81-319 *Status Report on the Implementation of Point of Sale Disclosure for Mutual Funds*, published on June 18, 2010.

Need for regulatory co-ordination

Time must also be set aside for regulators to meet and act as an ensemble group to ensure harmonious implementation of even seemingly disparate regulatory projects. Electronic communications involving mutual fund purchases may at some point intersect with the Government of Canada's anti-spam legislation and its governance of commercial electronic messages or the legislation and guidelines enforced by the Financial Transactions and Reports Analysis Centre of Canada on anti-money laundering and anti-terrorist financing. Every new regulatory action in the

securities field now runs the risk of interesting with other current and proposed obligations created by non-securities regulators.

Specific transition concerns on implementing Fund Facts

Specific transition concerns arising from mandatory pre-sale delivery include:

1. **Training**—Advisors and their support staff will need to be trained on how to access a Fund Facts document, and make client-specific arrangements for the preferred mode of delivering the Fund Facts to each client. Advisors themselves will need to be trained on how to explain the Fund Facts document to clients, including risk methodology – and also be able to do so verbally (e.g., orally over the telephone) in the event of an urgent buy request from the client in which pre-delivery of the Fund Facts sheet is not possible. The compliance officer will have to be consulted and the firm's code of conduct duly amended.

   Implementation of pre-sale delivery will therefore require the development of training sessions and quite likely the drafting and distribution of conversation scripts. Regardless, each advisor will have to determine how to explain to clients and prospects numerous complexities, such as the new Fund Facts' risk methodology and how the Fund Facts requirements interact with Phase 2 of the Customer Relationship Model. Included in this process will be the thorny problem of explaining to long-time, sophisticated clients that their trade cannot be processed until the client has received the Fund Facts document and the advisor has proof of the same.

2. **Testing**—In terms of how to best implement the new pre-sale requirements — and in a manner that is both cost-competitive and in the best interests of the client — the development of a compliance system which tracks client contact points and records delivery fulfillment will be of paramount importance. Designing and implementing (or leasing/purchasing) such a compliance system will be particularly onerous on smaller firms. Firms will need to time to test and refine their own compliance policies and systems. Larger firms will want to conduct system testing by executing batches of pre-trade deliveries of Fund Facts well in advance of the official effective date and also review their effectiveness in documenting clients' receipt of pre-trade delivery of Fund Facts sheets.

   With a pre-sale delivery obligation becoming the responsibility of financial advisors, it is to be hoped that their industry experience with document delivery and acumen in explaining concepts to retail investors will be fully considered by the CSA; Advocis believes that a minimum sufficient time of 12 months is needed for fund manufacturers, dealers and advisors to develop a workable framework to ensure the effective working of the entire Fund Facts regime, including pre-sale requirements. The realization of a compliance outcome which is beneficial to the consumer but which does not privilege firms with "deep

pockets" over those who will struggle to fulfill pre-sale rules is surely a paramount goal for CSA. Rushing the process with scant regard for those who must implement it is a disservice to investors and the capital markets at large.

3. **Client management**—For their part, advisors will need to determine with each client how he or she wants to receive the Fund Facts document. Some will want paper copies of the individual fund's Fund Facts sent to them by regular post; others will want a pdf version emailed to them; still others will wish to receive Fund Facts by facsimile transmission. Advisors will also need to explain to each client that they will have to receive a Fund Facts document *before* investing. For older Canadians relying on letter mail, this situation may prove frustrating. Advisors will further need to explain the exceptions to the requirement for pre-sale delivery of Fund Facts, and the need for the advisor to document the client's proof of receipt. Some clients will want to meet in-person with their advisor to review the Fund Facts document and the rules surrounding its delivery. No doubt clients who prefer not to invest in web access and a colour printer will be heavily dependent on in-person delivery from their advisor.

   We believe that the least intrusive way to do implement pre-delivery of Fund Facts is to give the industry at least twelve months for training and testing, and to give clients the ability to opt out of its pre-sale delivery. Moreover, a twelve-month window means that the issue of pre-sale delivery and the exceptions thereto can be examined in the client's annual review, and not in a specially scheduled, one-off meeting.

For example, assuming that publication of final rules takes place in early 2015, please comment on the feasibility of implementing the Proposed Amendments within 3 months of publication.

For the reasons adduced above, we believe that the implementation of the Proposed Amendments within three months of their publication is, at minimum, highly impractical and quite likely simply not feasible at all.

Would a longer transition period of 6 months or 1 year be more appropriate? If so, why?

As noted above, a transition period of at least two years would be more appropriate. This is due in part to the reasons outlined immediately above — the need for the advisor to explain to the client pre-sale delivery regime. To look beyond the ken of the financial advisor for a moment: the desirability of a longer transition period from the point of view of other stakeholders, including clients, becomes readily apparent when one considers the tremendous changes currently at work in the regulatory milieu of the retail investment world.

As well, consumers are being flooded with information about point of sale issues, and have been for some time. For example, the new pre-trade disclosure requirements under CRM-2 become take effect on July 15, 2014. Diverting the client's attention from complex and substantive issues such as the mutual fund risk classification methodology contained in Fund Facts and the new cost disclosure requirements and other aspects of CRM-2 to the more prosaic aspects of the method and timing of Fund Facts' pre-sale delivery, and its exceptions, will only further complicate advisor-client meetings.

Every new amendment must be explained to the client, often in a one-on-one meeting; thus, even explaining the new point of sale delivery requirements will be a significant time commitment for both the client and the advisor. We would submit that the CSA commit to a uniform launch date for pre-sale delivery, possibly by combining the pre-sale delivery requirements of Fund Facts with those of the in-progress summary disclosure document for exchange-traded funds. Such a coordinated release would fit well with IOSCO's Point of Sale Principle 4, which calls for "Disclosure of key information… in plain language and in a simple, accessible and comparable format to *facilitate a meaningful comparison of information disclosed for competing CIS* [Collective Investment Scheme] *products*" (emphasis added).[26]

Meanwhile, it should be recalled that Fund Facts is readily available to many investors already:

1. since May 13, 2014, investors may be informed by their advisors that all mutual funds must now have their Fund Facts in the new form available on their web sites and filed on SEDAR; and
2. beginning on June 13, 2014, dealers are required to deliver to investors the Fund Facts for the applicable series invested in for all mutual funds trades.

In responding please comment on the impact these different transition periods might have in terms of cost, systems implications, and potential changes to current sales practices.

The more time advisors and dealers have to implement, test, refine and perfect their compliance systems and to train themselves and their staff on the delivery requirements, exceptions to delivery, acceptable proof of receipt, and the revised contents of the most recently amended Fund Facts template, then the more effective the Fund Facts regime will be as both an engine of consumer education and protection and a mechanism to assist in more informed allocation of capital. With CRM-2 now underway, implementing the revised pre-sale requirements before the third quarter of 2015 will prove too confusing to the Canadian consumer and too problematic for administrative and back-office staff on the industry side.

[26] International Organization of Securities Commissions, *op. cit*., p. 29.

5. We are currently contemplating a single switch-over date for implementing pre-sale delivery of the Fund Facts. From a business planning and business cycle perspective, are there specific months or specific periods of the year that should be avoided in terms of selecting a specific switch-over date?

The calendar year-end and the period known in the industry as "RRSP season" should be avoided in terms of selecting a specific switch-over date. Ideally, we would suggest that the CSA consider the effective date for pre-sale delivery of Fund Facts to be scheduled somewhere in the period of May to July, 2016, so that it may be harmonized with the final scheduled set of CRM-2 changes coming in 2016. Failing that, coordinating pre-sale delivery with the changes in CRM-2 which take effect in July 2015 would be advisable.

Please explain.

Both RRSP season and the calendar year-end are notoriously busy periods for the advisory industry and represent difficult times to contact clients in order to meet and explain detailed requirements such as the Proposed Amendments to point of sale delivery. We would ask the CSA to schedule the effective date for pre-sale delivery of Fund Facts during one of the industry's slower-volume periods, so that advisors and clients alike can more easily devote the time required to become accustomed with the process.

CONCLUSIONS AND LOOKING AHEAD

Transparency in the capital markets helps those markets run efficiently and with integrity. Achieving such transparency in the form of disclosure of information to investors is deservedly a high priority goal of Canada's securities regulators. Enhancing point of sale disclosure so retail investors may consider when or before they invest key information about mutual funds, closed-end funds, exchange-traded funds, and so on, is a critical step towards this goal. The absence of accurate, understandable and meaningful disclosure prior to the financial crisis at the end of the last decade helps demonstrate the utility of the CSA's project. It is because Fund Facts and CRM-2 are so critical that we believe they should be rolled out in a way that fosters renewed investor trust in the producers of retail investor products, the intermediaries that distribute them, and the regulators who create and enforce the rules which govern them. A key part of investor trust is the sense that the financial system is not and does not have to be so tightly regulated that the average retail investor lacks even the small ability to ask their advisor or dealer to not send them a Fund Facts document.

Subject to the qualifications outlined about, Advocis supports the CSA's efforts to help Canadian retail investors become more informed before purchasing units in a mutual fund. We would be pleased to offer further comment or assistance on this matter at any time in the future. To discuss

any of the issues that we have raised, please contact the undersigned, or email Ed Skwarek at eskwarek@advocis.ca.

Sincerely,

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