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Submitted via Email: **kwoodard@mfda.ca**

Ken Woodard
Director, Membership Services & Communications
Mutual Fund Dealers Association of Canada
Toronto, ON M5H 3T9

Dear Mr. Woodard:

Re: MFDA Bulletin #0748-P: Discussion Paper on Expanding Cost Reporting

The Investment Industry Association of Canada[1] (the "IIAC" or "we") appreciates the opportunity to provide comments to the Mutual Fund Dealers Association of Canada (the "MFDA") with respect to the Discussion Paper on Expanding Cost Reporting (the "Paper"). The proposals in the Paper have impacts beyond MFDA constituents and it is important to consider the challenges from all registrants' perspectives.

The introduction of the Client Relationship Model Phase 2 ("CRM2") reporting requirements was a significant undertaking and represented an important step forward in providing clients with transparency around their cost and performance information. The IIAC and its members have been very supportive of CRM2 and believe that the increased transparency will strengthen the client-advisor relationship. We appreciate the Paper's objectives of providing clients with additional product cost information, however, there are a number of implementation barriers that must be considered. Foremost, Investment Industry Regulatory Organization of Canada ("IIROC") Dealer Members do not currently have access to elements of the investment fund cost information and would not be able to comply with the Paper's requirements unless other industry participants are mandated to provide that information and significant structural changes are made to enable Dealer Members to provide that information on client reports.

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[1] The IIAC is the national association representing the investment industry's position on securities regulation, public policy and industry issues on behalf of our 120 IIROC-regulated investment dealer members in the Canadian securities industry. These dealer firms are the key intermediaries in the Canadian capital markets, accounting for the vast majority of financial advisory services, securities trading and underwriting in the public and private markets for government and corporations. For more information visit, **http://www.iiac.ca**

Our response focuses on the IIROC Dealer Member perspective.

Expanding Cost Reporting

1. *Should regulators consider expanding cost reporting for investment funds?*

   IIAC Members would support the expansion of CRM2 Reports if it provided clients with more fulsome and meaningful disclosure that can be presented in a manner that facilitates clients' comprehension of their investment, related costs and performance. In order to determine how to proceed, we encourage the Regulators[2] to conduct client research to determine if the CRM2 Reports should be substantially modified from their original purpose of displaying the Dealer/Advisor Compensation and Fees, and Performance. Similar to FAIR Canada's position, we believe that client engagement in this process is critical to ensuring that proposed changes are based on providing clients with meaningful data that they value and that the information is presented in a manner that is easy for clients to understand[3]. We also agree with FAIR Canada that the "consideration of expanded cost disclosure is in its formative stages as regulators need to reflect on the policy goals of expanding cost disclosure, the optimal means of achieving these goals and consider factors such as what the impacts will be of the Canadian Securities Administrators' (the "CSA") Reforms to Enhance the Client-Registrant Relationships as well as the CSA's Mutual Fund Fee Reforms"[4].

   Further, we believe a cost-benefit analysis is warranted. The CSA is currently undertaking a comprehensive study on the impact of CRM2 and the Point of Sale amendments to National Instrument 81-101 *Mutual Fund Prospectus Disclosure* requirements. Many Dealer Members have individually spent over $10 million dollars implementing CRM2 and with only two years' worth of CRM2 Reports provided to clients, its effectiveness and impact on clients has not yet been established. It is imperative that research be conducted on the costs, as well as the material benefits to clients, of each aspect of the proposed regulations before Regulators impose additional requirements or modifications to CRM2 that would result in the need for:

   - new infrastructure to exchange information between registrants;
   - internal system builds;
   - vendor builds to modify CRM2 Reports;
   - advisor training;
   - policy updates; and
   - client education.

   Further, the CSA must lead any initiative that expands cost reporting for the securities industry. IIAC Dealer Members do not have many of the key data elements outlined in the Paper. Our members

[2] The term Regulators refers to the CSA, IIROC and MFDA working together
[3] See FAIR Canada's submission: https://faircanada.ca/submissions/mfda-discussion-paper-on-expanding-cost-reporting/
[4] See above FAIR Canada submission.

would not be able to comply with the Paper unless certain registrants were mandated to provide those data elements.

From an implementation perspective, the rules would need to be harmonized across registrant categories. CRM2 provided valuable lessons with respect to the difficulties firms experienced when the Regulators finalized rules at different times and where it was not clear how exemptions and other nuances between rules would be interpreted. We strongly encourage the CSA, the MFDA and IIROC to coordinate not only the content of the regulations, but the timing of implementation. This would also be most beneficial to clients to ensure that the reporting and their experience across registrant categories is consistent.

2. *Should regulators consider expanding cost reporting for other investment products?*

The IIAC supports a level-playing field and if the proposals outlined in the Paper goes forward, we support the inclusion of other similar products. In addition, if the Regulators are considering any other changes to CRM2, we strongly encourage those recommendations to be included in the next phase of the consultation process to enable one implementation for all CRM2 related changes. The CRM2 reports cannot be modified on an ongoing basis. IIAC Members are concerned that existing CRM2 reports could be impacted by proposed rules to different aspects of the CRM2 Reports from various Regulators. In 2016, the CSA proposed “technical” amendments to NI 31-103 and its companion policy. The IIAC viewed those proposed changes as substantial changes to data elements and provided comments. The CSA has not responded regarding the status of that proposal. CRM2 was extremely challenging for firms to implement due to the numerous required systems changes and firms’ reliance on third-party vendors.

Continuous changes to the CRM2 reports could diminish their value to clients. It could be very confusing for clients if they try to compare their annual reports. The IIAC again stresses the need for a coordinated effort among the Regulators.

Costs Considered

3. *Do you agree that the costs considered in this Discussion Paper should be disclosed to clients?*

IIAC Members agree with the fees outlined in the Paper. With respect to calculation methodology for the management expense ratio (“MER”), we support IFIC’s recommendation to use the last posted MER (on the Fund Facts) x average daily account balance to give the cost per day, and the sums would then be added up over the year. Most mutual funds have a December 31 year-end and if there was a requirement to adjust the MER to determine the exact amount paid by each client, it is likely to delay CRM2 reporting. There should also be a consistent calculation methodology for exchange-traded funds (“ETFs”).

As we will discuss in our responses to Question 7 and 8, the Fund Manufacturers (both mutual fund and ETF) must be mandated to provide certain data elements to the Dealers.

4. *Are there any other costs that should be reported to clients?*

   We believe the costs outlined in the Paper capture the material costs associated with investment funds. We support the MFDA's decision not to include the total expense ratio ("TER") as we believe the inclusion of the TER would provide a level of detail that would be unhelpful and confusing to investors.

Cost Reporting

5. *What are your views on the reporting examples provided in this Discussion Paper?*

   Figure 1 - Account Statement

   The Paper contemplates expanding the Account Statement Disclosure to include the MER percentage for each investment fund held by the client. While we appreciate that the ability of an investor to easily compare MERs could be helpful, the MER percentage displayed would be historical in nature and may not be an accurate reflection of the personal MER percentage that the client is paying. Many fund companies rebate or reduce management fees for particular funds and/or certain investors, primarily based upon the size of investment in the fund but also based upon the expected level of account activity and/or the investor's total investments with the fund company. Those rebates or discounts are applied annually by the Fund Manufacturer. In addition, the MER may not be accurate for clients in fee based accounts where the MER may be adjusted to remove the trailer portion, in addition to other potential rebates. The Dealer Member may not have the information needed to provide personal MER percentages. We question the value that may be provided to the client if the information cannot be personalized. It is a significant undertaking to make those changes to the Account Statement. Further, for IIROC Dealers, investment funds may only represent a portion of a client's portfolio and providing additional details for only a subsection of products may lead to client confusion.

   Figure 2 – Investment Fund Report

   We agree with the MFDA that a separate Investment Fund only report would be difficult to implement and incorporate into existing account reporting. Further, we question the value that clients would receive in having to review another report that focuses on complex and confusing fund level details rather than their personal cost or performance information.

   Figure 3 – Cost and Compensation Report

   If the Regulators impose the expanded cost disclosure requirements on the Dealer Members rather than Investment Fund Manufacturers, then we agree that any proposed new cost information should be incorporated into the current CRM2 Cost and Compensation Reports. However, we found this example to be confusing in how the investment fund cost information was presented and we are also concerned that clients would similarly struggle to understand the new information. How the information is presented is critical to its value for clients. The level of detail in the example may overwhelm clients and serve as a barrier to them reading and understanding any of the information.

We are concerned that it could actually make this reporting less helpful to clients than current reporting, despite the laudable objective.

The Figure 3 Sample Report includes dealer compensation in the two different sections and the fees are not clearly identified as duplicative. The IIAC is concerned that clients will overestimate their costs when certain costs are listed in multiple sections. It was also not clear that the trailing commission was included in the MER amount because the terms in the footnote differed from the terms used in the Compensation Report section. When there are numerous securities aggregated in those two sections, it could be very difficult to track what amounts are repeated.

Additionally, in the context of IIROC Dealers with a broader range of products that goes beyond investment funds, some of the line items included in the Sample Report may not be applicable.

We strongly believe the CRM2 Reports should stay principle-based (as allowed under the current CRM2 model) with mandated data elements. The CRM2 reports need to have the flexibility to recognize various business models and account types require the information to be presented in different formats.

As previously discussed, we strongly recommend that the Regulators conduct client research to determine how the information should be best presented to clients in order to facilitate understanding. The Paper would represent a fundamental shift in what information is provided.

Figure 4 – Proprietary Only

We do not have any comments on Figure 4 as it was not applicable to our members. However, we appreciate that the MFDA recognizes that different business models may necessitate flexibility in how cost reporting information is presented.

6. *Are there better ways to report the costs of investing to clients?*

Yes, we believe that the cost information can be provided in a more understandable, client friendly manner. Unfortunately, IIAC Members have not had sufficient time to provide specific feedback on how any proposed changes should be reported. Further, as repeatedly emphasized, consultation with clients is required to develop impactful and understandable Cost and Compensation Reports.

The IIAC would like to again stress the need for flexibility in how the information is presented, similar to current CRM2 reporting.

7. *What challenges or issues do you foresee in obtaining and reporting expanded cost information to clients?*

8. *Are there different challenges or issues to expanding cost reporting for investment dealers or other securities registrants?*

   There are unique challenges for the various securities registrants that must be considered. We are responding to Questions 7 and 8 together from the IIROC Dealer Member perspective.

   One challenge for Dealer Members is in obtaining the required data. Dealer Members do not currently have access to important data elements outlined in the Paper, specifically related to the MER. Regulators must mandate Fund Manufacturers (both mutual fund, and ETF) to provide required data elements in the same manner that trailing commission information was mandated to be provided for CRM2. For example, Dealers need data elements such as the net asset value per unit ("NAVPU") from ETF manufacturers in order to do required calculations. In addition, it is crucial that the Regulators mandate a standard cost calculation methodology and reporting format as to how that information is provided to the Dealer Member, as some IIROC dealers sell thousands of different investment funds from over 100 different fund manufacturers.

   With respect to mutual funds, even once the data is mandated to be provided to Dealer Members, there would still need to be infrastructure built (likely through FundSERV) to exchange the data between the Fund Manufacturer and Dealer Member. It would be a new build. Dealer Members must then have in place systems to verify the accuracy of the data, store the data and determine how to aggregate and incorporate the data into the CRM2 Reports. This is a complex implementation involving different registrants, vendors and service providers.

   In addition to these extensive operational challenges, Dealer Members need to provide education and training to advisors on the new data elements, develop new client materials, and update policies and procedures.

   The Paper includes expanding cost information reporting to include ETFs. There are a number of unique challenges for disclosing ETF cost information. It is the Dealer Member who is the trading agent and there is no industry infrastructure like FundSERV to host data exchange. There would need to be infrastructure built to exchange data elements that Dealer Members need to do their calculations, such as the NAVPU. Since there is currently no equivalent to FundSERV for the exchange of that information and it is not clear how this information would be exchanged at this time. Dealer Members would also have to develop their own systems to then determine the MER calculations. This is another significant build. Then, as with mutual fund disclosure, the Dealer Member would need to determine how and where to store the data, and determine how to aggregate and incorporate the data into the CRM2 Reports.

   If other products or changes are proposed, there could be additional challenges that are unknown at this time.

Implementation

9. *Based on the cost reporting approaches detailed in the Discussion Paper, what would be a realistic timeframe for implementing expanded cost reports to clients?*

   It is difficult to provide a realistic timeframe for implementation without a clear understanding of what data elements will be mandated and what other products or changes to CRM2 may be required.

   It is essential that the introduction of new requirements be contemporaneous in terms of implementation. It is not feasible for firms to add cost information for certain products in a staggered manner.

   Assuming only the changes in the Paper are finalized, then the expanded cost reporting would require a minimum three-year implementation time-frame from the release of the final rules by the appropriate regulator. It will take approximately two years to complete the necessary systems builds and testing (outlined in Appendix A), after which the industry will need an additional year for data collection to be able to provide the information on the CRM2 Reports.

   In addition, we ask the Regulators to consider the implementation timing of this Paper in light of other initiatives such as the CSA's proposed Client Focused Reforms amending National Instrument 31-103 and Companion Policy 31-103CP.

We greatly appreciate the ongoing work and dialogue with the financial industry on considerations for expanding cost disclosure. If you have any questions with respect to the foregoing, we kindly ask that you contact the undersigned at **awalrath@iiac.ca** or 416-687-5472. Thank you.

Yours sincerely,

"Adrian Walrath"

Assistant Director

Appendix A – Implementation Builds required for Dealer Members

As noted in our response, the minimum time-frame for the various builds described below is two-years.

* The development process cannot begin until there are finalized rules from the CSA and SRO's with specific data elements mandated to be provided by the Mutual Fund and ETF Manufacturers.

* The suggested timelines are based only on the proposed expanded cost disclosure in the Discussion Paper and the timelines are subject to change if the data elements differ or if additional products or changes are made to the CRM2 Reports.

Mutual Fund Infrastructure and System Builds – High-Level Overview:

Mutual Fund Manufacturer Build

- Mutual Fund Manufactures do not currently have account level data for certain required data elements. This build will depend on what data elements are mandated. We defer to Mutual Fund Manufacturers to assess the timeline required.

Central Information Repository and Exchange Build

- As previously noted, Dealer Members do not currently possess certain data elements required to complete necessary calculations for the proposed expanded cost disclosure.
- It is expected that FundSERV will facilitate the exchange of information between the Mutual Fund Manufacturers and Dealer Members. It will be a net new build for FundSERV. FundSERV operates on a June – June full year cycle for the consideration, development and release of new FundSERV protocols.

Dealer Member Data Storage and Calculation Build

- Dealer Members must be able to verify the data from the Mutual Fund Manufacturer, store the data and integrate the data in order to utilize it to complete necessary calculations for the CRM2 Reports.
- Dealer Members will likely have different external vendors and those builds in terms of timing could vary.
- Dealer Members may also have internal system builds to manage the data from the external vendors to produce their CRM2 Reports. Dealer Members may use different vendors for the calculations than the for producing the actual reports.
- Introducing Brokers may need to rely on their Carrying Broker for certain aspects of the build.

Dealer Member CRM2 Report Builds

- The Paper is proposing significant changes to both the Account Statements and Cost and Compensation Report.
- Dealer Members need to work with their external vendors to determine what options are available in terms of how to include all required information in a comprehensible and meaningful way on the CRM2 Reports. There are restrictions as to how many characters are able to fit in certain items on the CRM2 Reports and there may need to be a rebuilding of the report frameworks to accommodate the new information.
- Similar to CRM2, Dealer Members need a data gathering period of one-year.
- Dealer Members and their vendors need sufficient time to conduct testing of the new data and the accuracy of the calculations.
- Introducing Brokers may need to rely on their Carrying Broker for certain aspects of the builds but may also need to complete internal builds to customize the CRM2 Reports. This relationship and division of responsibility can further complicate estimating timelines.

ETF Infrastructure and System Builds – High-Level Overview:

ETF Fund Manufacturer Build

- This build will depend on what data elements are mandated. We defer to ETF Fund Manufacturers to assess the timeline required.

Central Information Repository and Exchange Build

- There is no central information repository similar to FundSERV currently for ETFs. It is not clear how the information will be exchanged between ETF Fund Manufacturers and Dealer Members. Regulators and industry need to have discussions to determine if exchanges, third-party vendors or FundSERV could develop the infrastructure capabilities needed.
- There is no timeline suggestion for this step as it is very unclear how this process will be managed.

Dealer Member Data Storage and Calculation Build

- Dealer Members must be able to verify the data from the ETF Fund Manufacturers, store the data and integrate the data in order to utilize it to complete necessary calculations for the CRM2 Reports. Dealer Members, as the trading agent for ETFs will have to manage more data elements for the calculations.
- Dealer Members will likely have different external vendors and those builds in terms of timing could vary.
- Dealer Members may also have internal system builds to manage the data from the external vendors to produce their CRM2 Reports. Dealer Members may use different vendors for the calculations than the for producing the actual reports.

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