



JOANNE DE LAURENTIIS

President and CEO *Présidente et chef de la direction*

jdelaurentiis@ific.ca 416 309 2300

June 3, 2013

Delivered By Email: rday@osc.gov.on.ca

Mr. Robert Day
Senior Specialist, Business Planning and
Performance reporting
Ontario Securities Commission
20 Queen Street West, Suite 1900
Box 55
Toronto, ON M5H 3S8

Dear Mr. Day:

RE: Ontario Securities Commission Notice 11-768 – 2013-2014 Statement of Priorities

We are writing to provide comments on behalf of the Members of The Investment Funds Institute of Canada (“IFIC” or “we”) with respect to the draft of the OSC’s Statement of Priorities (“the Statement”) for the financial year ending March 31, 2014.

General Commentary:

As the Statement notes, mutual funds make up the largest single share of investable assets for the typical Canadian household at approximately 28 percent of the total. As such, the Canadian mutual funds industry is an important contributor to the wealth-creation of Canadians. We appreciate that one of the contributors to the growth of the fund industry is a sound regulatory framework and support the OSC’s continued focus on delivering strong investor protection.

Recognizing the industry’s importance, our Members expect to be well-regulated, but they also expect that regulation to be balanced - both on a cost/benefit basis and as compared to comparable products, whether they are banking, insurance or securities products.

We provide comments below on several of the Commission’s priorities for the coming year

Priority 2 – Adviser Responsibilities to Investors

The Statement observes that *“issuers, product manufacturers and intermediaries must meet high standards of conduct and disclosure in order to earn the trust and confidence of investors.”* We concur. Investor trust and confidence are foundational to our industry’s success.

The topic of advisor responsibilities to investors is front-of-mind for investors, industry participants and regulators alike. We note that the OSC recognizes the complexity and far-reaching implications of statutorily changing the nature of the investor-advisor relationship. (*“This is a complex issue that requires careful consideration [...]”*). We reiterate one of the key comments set forth in our response to CSA Consultation Paper 33-403, *The Standard of*

Conduct for Advisors and Dealers: Exploring the Appropriateness of Introducing a Statutory Best Interest Duty When Advice is Provided to Retail Clients, i.e. that the securities industry in Canada currently is in the process of implementing changes that will significantly enhance a regulatory regime that already features strong investor protections. It would be prudent to permit recent rule changes, particularly those simplifying and enhancing point of sale and performance and cost disclosure, to be fully implemented and evaluated before imposing an additional framework upon the advisor-investor relationship.

Priority 3 – Disclosure to Investors

We support the OSC's efforts to ensure that investors receive key information about financial products. IFIC's Members support the general principle of delivering simplified and enhanced disclosure to investors. Studies confirm investors' preference for short and simple point-of-sale disclosure documents and it is hoped the use of Fund Facts in place of the prospectus will better inform investors about their mutual fund choices. We look forward to a continuing dialogue regarding the next stage of Fund Facts; in particular to demonstrating that the increasingly widespread availability and use of the Fund Facts renders unnecessary, a rigid rule requiring delivery in advance of a purchase.

We commend the OSC for identifying the increasing interchangeability of financial products, and recognizing the commensurate challenges faced by investors trying to distinguish among them in order to assess product suitability. Investors need to be able to compare different products.

Investor protection should be extended to investors in all investment products. While the OSC regulates only securities we continue to encourage you to collaborate with your CSA and Joint Forum colleagues to create a broadly comparable set of disclosure and other investor protection rules to give investors a consistent experience across all of the products they own.

Priority 4 – Mutual Fund Fees

As we noted in our response to CSA Discussion Paper 81-407, *Mutual Fund Fees* ("Discussion Paper"), it is disappointing to see a narrow focus placed on mutual fund fees. The other jurisdictions which have addressed the question of embedded distribution fees have not taken a narrow focus but, instead, have included insurance and some banking products in their rule coverage, thereby avoiding regulatory arbitrage.. Mutual funds are among the most transparent financial products available to retail investors in Canada. The full cost of ownership is explicitly included in the multiple disclosure documents required of each fund. While embedded fees are used by many retail financial products, of which mutual funds are but one, only mutual funds are already required to fully publish their costs.

We recommend that the new disclosure rules under CRM2 be allowed to be implemented and assessed before any more changes are introduced. It is informative to note that the jurisdictions that are "prohibiting" embedded distribution fees did not have in place the level of detailed disclosure that CRM2 will bring to investors, and that they implemented their solutions to address market circumstances unique to their jurisdictions and that do not exist in Canada. The new CRM2 disclosures with which Canada is proceeding will increase transparency and help to alleviate concerns as to potential conflicts of interest as expressed by the OSC in the Discussion Paper.

It is troubling to see the OSC's inclusion of the following statement: "A number of comparative studies on fund fees indicate that Canadian mutual funds fees are among the highest in the world". While there have been two studies – one by a group of academics and a second by Morningstar U.S., the data used in both used has all come from the same source of incomplete data which does not, particularly in the case of the U.S. data, take into account the added costs investors pay directly to their advisors – this has the effect of underreporting the fund fees in other jurisdictions when compared to Canada.

Several months ago, OSC staff was provided with detailed third-party research conducted in 2012 by Investor Economics and Strategic Insight¹ showing definitively that the cost of owning mutual funds in Canada and the U.S., purchased through advisors, is virtually the same. Both reports were included in IFIC's response to the Discussion Paper. We were, therefore, surprised to see this outdated view of Canadian fund fees restated in the draft Statement and request that it be removed from the final document.

Priority 7 – Regulation of Fixed Income Securities

Regarding the regulation of fixed income securities, we remind the OSC that Canadian mutual funds are major participants on both the buy- and sell-side of this important market area. This deep experience gives Canadian mutual funds an unparalleled understanding of the risks and opportunities within the fixed income marketplace. As the OSC reviews its oversight of these securities, we would urge the OSC to consider the mutual funds industry a key stakeholder that can offer valuable investor feedback on any issues and proposed regulatory changes concerning fixed income securities. Many of our recommendations regarding comparability of regulation of interchangeable products may also be relevant here as fixed income products comprise a significant share of the financial wealth of Canadian households.

Priority 11 – Reliance on Data and Analysis

We commend the OSC for its renewed commitment to increasing its reliance on data and analysis in undertaking its work. Fact-based rulemaking is critical for Ontario's capital markets and securities regulations to remain world-class. Particularly as it considers what actions to take, if any, respecting *best interest standards*, or *fund fees*, we encourage thorough market impact research of similar actions in other jurisdictions, including whether the investor is better served under the new regimes.

We also acknowledge the OSC for its intention to be efficient, effective and accountable in delivering its mandate, and particularly support its goal of improving "*regulatory capacity through the development of people and expertise (e.g., training, secondments)*". We believe that this expertise can be developed through regular and meaningful dialogue with market participants. Additionally, we suggest exploring the use of two-way secondments, such that OSC staff gain a hands-on understanding of the challenges and opportunities within the investment funds industry, while market participants would gain valuable expertise and insight into the fast-moving regulatory arena.

We also strongly support the OSC's intention to improve its cost-benefit analysis capability. Commission representatives have confirmed the OSC's lack of capacity in this area in meetings and in public forums, such as the 2012 OSC Dialogue. Evidence-based cost analysis must be factored into the assessment of any proposed regulatory initiative and we encourage the OSC to provide information on the concrete steps that will be taken in this regard.

As we have noted in previous submissions, the OSC is required by Section 2.1 of the Securities Act to have regard to fundamental principles in pursuing its objectives under the act. Principle 6 states "*business and regulatory costs and other restrictions on the business and investment activities of market participants should be proportionate to the significance of the regulatory objectives sought to be realized.*" Historically, in accordance with section 143.2(2) of the Act, the OSC has included, in every notice of a rule, a brief discussion of alternatives, if any, to the proposed rule that were considered and the reasons for not proposing the adoption of alternatives considered, as well as a description of the anticipated costs and benefits of the

¹ Investor Economics and Strategic Insight, *Monitoring Trends in Mutual Fund Cost of Ownership and Expense Ratios, A Canada-U.S. Perspective*, November 2012, which is a comparative analysis of the following individual studies: Investor Economics, *Mutual Fund MERs and Cost to Customer in Canada: Measurement, Trends and Changing Perspectives*, September 2012 and Strategic Insight, *A Perspective on the Evolution in Structure, Investor Demand, Distribution, Pricing and Shareholders' Total Costs in the U.S. Mutual Fund Industry*, November 2012.

proposed rule. However we believe that to meet the standard of Principle 6, it is imperative that the notices also provide thorough, detailed research and analysis or calculations to support the conclusion to proceed with the rule as proposed.

* * * * *

We thank you in advance for considering our comments on the 2013-2014 Statement of Priorities. Please do not hesitate to contact me directly, or contact Ralf Hensel, General Counsel, Corporate Secretary and Director of Policy (Fund Manager Issues) by email at rhensel@ific.ca or by phone at 416-309-2314 if you have any questions or would like to discuss our comments in more depth.

Yours sincerely,

THE INVESTMENT FUNDS INSTITUTE OF CANADA



Joanne De Laurentiis
President and CEO

c.c. Rhonda Goldberg, Director, Investment Funds Branch