



July 27, 2022

VIA EMAIL

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Dear Sirs/Mesdames:

RE: Request for Comment – Total Cost Reporting for Exchange Traded Funds

The Canadian ETF Association (**CETFA**) welcomes the opportunity to provide feedback on the Request for Comment regarding proposed amendments to National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* and Companion Policy 31-103CP *Registration Requirements, Exemptions and Ongoing Registrant Obligations* (the **Proposed Securities Amendments**) concerning proposed enhanced cost disclosure reporting requirements for investment funds published by the Canadian Securities Administrators (**CSA**) on April 28, 2022, specifically as they relate to exchange-traded funds (**ETFs**).

CETFA is the only ETF association in Canada and represents members comprising 95% of the ETF assets under management in Canada. The mandate of CETFA is to support the growth, sustainability and integrity of Canada's ETF industry on behalf of our members, who are typically ETF managers. Based in Toronto, Canada, CETFA is the only ETF association in Canada, and the first of its kind in the world.

We would like to address the topics outlined below.

- 1. It is not sufficient to report the management expense ratio (MER) alone; the trading expense ratio (TER) should also be reported and used in the calculation of the fund expenses for the purposes of the annual report on charges and other compensation.**

Although there may be some disadvantages associated with reporting TER, on balance we consider that reporting MER alone would not allow investors to compare a full and accurate picture of the costs associated with different products. Further, listing both MER and TER separately (instead of as a single combined ratio) provides investors with information about how the different features of products drive costs. There is a wide divergence in the TER for products with different features, especially ETFs. For example, TER is higher for ETFs that hold a higher proportion of equities as opposed to fixed income securities. TER is also higher for ETFs that have a higher portfolio turnover rate. TER is also generally higher for an ETF class or series of a conventional mutual fund than for an otherwise comparable standalone ETF. Consequently, reporting MER and TER separately provides investors with superior information, as compared with reporting MER alone or reporting a fund expense ratio (**FER**) that combines MER and TER.

2. A longer transition timeframe for the Proposed Securities Amendments is warranted, in light of the other complex industry initiatives scheduled for implementation in or about 2024 and the operational and logistical hurdles the industry will need to address prior to implementation.

The CSA has proposed that the Proposed Securities Amendments will come into force in September 2024. For the securities sector, investors would receive the first quarterly account statements containing the newly required information for the period ending in December 2024, and the first annual reports containing the newly required information for the reporting period ending in December 2025. In December 2021, the Canadian Capital Markets Association announced its plans to facilitate shortening Canada's standard securities settlement cycle from two days after the date of trade (T+2) to one day after the date of the trade (T+1) within the first half of 2024.¹ Further, the CDS Post-Trade Modernization project is scheduled for implementation in late 2024. This project will deliver an integrated technology platform for the TMX-CDS systems including: clearing, settlement, depository, corporate actions and risk.

The investment fund manager (**IFM**) of an ETF does not have access to any information regarding the identities of the investors in the ETF; only advisers and dealers have access to this information. While an ETF's IFM can provide annualized historical MER and TER figures for the ETF to advisers and dealers, the IFM cannot apply those figures against each investor's holdings in order to provide the information required by the Proposed Securities Amendments. Only the adviser or dealer through which an investor holds ETF securities is able to perform the requisite calculations for that investor. Building the systems infrastructure necessary to automate the required calculations is likely a significant undertaking for advisers and dealers that will require substantial time and resources.

It is not clear how the MER and TER figures for each product will flow from IFMs to advisers and dealers. It should be noted that, unlike conventional mutual funds, ETFs do not trade on Fundserv. Consequently, to the extent Fundserv will facilitate the flow of information for conventional mutual funds, an alternative mechanism will be required for ETFs.

¹ The announcement can be found at: <https://ccma-acmc.ca/en/wp-content/uploads/Canada-Announces-Faster-Securities-Settlement-December-1-2021.pdf>

The Proposed Securities Amendments do not address foreign ETFs. Advisers and dealers will need to determine whether it is possible to compel foreign IFMs to provide the required information in the required format and, if it is possible, the appropriate methodology for doing so. The Proposed Securities Amendments should provide guidance to advisers and dealers in this regard and the implementation timeframe should account for the time and resources that will be required to address this issue. Further, it should be noted that foreign ETFs may be reluctant to provide the required information and, if an exemption from these requirements is not provided for foreign ETFs, dealers may no longer permit their clients to hold foreign ETFs.

As at December 2021, 15.5% or \$63.9 billion of the \$412.5 billion of ETFs owned by Canadian investors (retail and institutional) were U.S.-listed ETFs. Of the 15.5% nearly 40% were U.S.-listed ETFs of ETF providers with no Canadian affiliate. It will be difficult to enforce a Canadian regulation on U.S. ETF providers, their service providers or depositories, to provide the required information. Further, the concept of a MER does not exist in the U.S.; instead, the U.S. concept is a total expense ratio (TER) which is a distinct concept from the trading expense ratio (TER) connoted by the same acronym in Canada. Incorporating the U.S. total expense ratio concept into investor statements would further confuse investors.

Significant resources will be required to facilitate each of the complex industry initiatives scheduled for implementation in or about 2024 simultaneously. Further, significant time and resources will be required to address the operational and logistical hurdles the industry will need to address prior to implementing the Proposed Securities Amendments. A longer transition timeframe for the Proposed Securities Amendments is warranted.

3. Disclosure clarifying that the cost figures reported are annualized estimates based on the historical MER and TER of the fund and actual costs incurred may be materially different should be included. In addition, clarification on disclosure requirements for new products is needed.

As a result of the calculation methods prescribed by securities regulations, the MER and TER figures IFMs provide for existing products will necessarily be historical and represent annualized figures. Additionally, the time period a given investor has held securities of an ETF for will not always align with the time period used for calculating the MER and TER. This is particularly relevant if the reporting period of an ETF ends prior to the reporting period of the statement disclosing costs. For example, where an ETF has a September 30 year-end but the statement covers the calendar year ending December 31, the December 31 statement will use MER and TER figures as of the prior September 30 to calculate the cost figures. As a consequence, the cost figures will necessarily be estimates and investors should be made aware of this fact.

From a disclosure perspective, we suggest adding a footnote to clarify that the figures are estimates based on the historical MER and TER of the fund and reflect the estimated costs that could be incurred in connection with the investor's holdings. The footnote should also explain that actual costs could be materially different than those listed. Actual costs could be lower due to the impact of householding and management fee rebates.

Further, the Proposed Securities Amendments do not account for new products where such historical information may not be available. Clarification on disclosure requirements for new products would be helpful.

4. The requirement that an IFM must not rely on the previously publicly disclosed MER and TER information if it is outdated or if the IFM reasonably believes doing so would cause the information in the statement or report to be misleading should be struck from the Proposed Securities Amendments.

The Proposed Securities Amendments would allow IFMs to rely on publicly available information disclosed in an investment fund's most recently published fund facts document, ETF facts document, prospectus or management report of fund performance, unless this information is outdated, or the IFM reasonably believes that doing so would cause the information reported in the statement or report to be misleading.

Current regulation requires an ETF's MER and TER are disclosed twice a year in the ETF's management reports of fund performance (**MRFPs**). Audited MER and TER figures are reported once per year in an ETF's annual MFRP, which must be filed within 90 days of the ETF's year-end. Unaudited MER and TER are reported once per year in an ETF's interim MRFP, which must be filed within 60 days after an ETF's second quarter-end. Since most ETFs have a December 31 year-end, each year most ETFs report MER and TER (as of December 31) in or about the end of March and MER and TER (as of June 30) in or about the end of August. ETF facts documents are required to disclose the MER and TER figures as disclosed in the most recently filed MRFP.

The requirement that an IFM must not rely on previously publicly disclosed MER and TER information if it is outdated or if the IFM reasonably believes doing so would cause the information in the statement or report to be misleading should be struck. As a result of the regulated MRFP disclosure intervals discussed above, at the time dealers and advisers prepare their December 31 client statements, the most recent MER and TER figures available for most ETFs will be as of the previous June 30 (i.e. six months old).

Consequently, the requirement would, in some circumstances, require IFMs to revise the MER and TER figures for an ETF between already regulated disclosure intervals. For example, performance fees can cause the MER of an ETF to change depending on when the performance fee is paid. Further, if a certain expense is eliminated between regulated disclosure intervals, such elimination will not be accounted for. In such instances, the proposed rule would require IFMs to revise MER and TER between regulated disclosure intervals to account for these changes. This is an unnecessary additional regulatory burden.

We also note that TER is driven by portfolio transactions executed by ETFs. The number of portfolio transactions will vary from year to year and it is not possible for an IFM to determine at any point whether the current TER will be the same as the publicly disclosed TER.

5. Annual reporting may be more appropriate than monthly or quarterly reporting.

As discussed above, current regulation requires ETFs to report MER and TER twice per year in the ETF's annual and interim MRFPs. Requiring monthly/ quarterly reporting of FER, MER and/or TER in account statements and additional statements is burdensome and could be misleading. Monthly or quarterly statements are intended to disclose transaction activity and do not contain cost information. Including cost information on these statements may not provide a complete picture of all costs. For example, an ETF's FER, MER and/or TER may not reflect all fees paid by the investor (e.g. adviser fees that are paid outside the fund). As a result, the investor may be misled as to the total costs they are paying. Conversely, disclosing FER, MER and/or TER in the annual report would align with investors' expectations that such report contains information on the costs associated with their investment. For this reason, annual reporting of FER, MER and/ or TER may be more meaningful for investors.

Thank you for this opportunity to express our comments about the Proposed Securities Amendments.

If you have any questions or if we can be of any other assistance, please do not hesitate to contact Pat Dunwoody, Executive Director of the CETFA, at (647) 256-6637 or at patdunwoody@cetfa.ca.

Yours truly,

CANADIAN ETF ASSOCIATION

By: _____

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