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Ken Woodard
Director, Membership Services & Communications
Mutual Fund Dealers Association of Canada
121 King St. West, Suite 1000
Toronto, ON M5H 3T9
kwoodard@mfda.ca

Please find attached CARP's submission regarding the MFDA's Discussion Paper on Expanding Cost Reporting.

Yours sincerely,

W.W. Morris

Wanda Morris
VP of Advocacy

CARP's Response to MFDA's Discussion Paper on Expanding Cost Reporting

Summary

Background

Changes to securities legislation, (CRM2 Amendments) which came into effect July 15, 2016 require that investors be provided with an annual summary of the fees they paid to their investment firms. This includes commissions or other compensation paid to the investment firm, but does not include other costs paid by the investor.

For example, an investor who owns a mutual fund may pay total annual fees of 2.25% of assets with 1% of that amount paid to the investment firm. The statement the investor receives under CRM2 only discloses the 1% received by the investment firm, not the 2.25% total amount paid.

While some firms have adopted comprehensive reporting that exceeds this standard, most do not.

Educating Investors about Full Costs

In our conversations with CARP members and others following the implementation of CRM2, we noted widespread misunderstanding about the nature of costs reported. That is, we repeatedly heard from members and others who believed that the statements they received under CRM2 reflected *all* investment costs, not just one element (investment firm compensation) of them.

Controlling or reducing investment fees is widely recognized as one of the most critical methods investors can use to maximize their savings. Thus this misunderstanding may lead to sub-optimal behaviour and significant negative consequences for investors.

CARP believes that investors must receive clear and readily understandable information about the full cost of their investments. Educating them about the limitations of their current statements is at best an interim step.

Leveling the Playing Field

There are a number of financial institutions who are vertically integrated, that is, they create mutual funds or ETF products and sell them through their own networks. In those cases, there is no clear, external price set for product sales (as opposed to product creation). For purposes of CRM2 reporting, these firms must allocate part of their total costs to product sales.

Because allocations are subjective in nature, there will always be a temptation for those firms to make a comparatively smaller allocation to product sales (and a comparatively larger one to product costs). When an investor sees only partial disclosure, they may be swayed by what is essentially an arbitrary allocation.

CARP believes full cost disclosure is critical as it will remove the ability of vertically-integrated firms to show favourable costs simply by altering allocations. It will also ensure investors have the best possible information for making investment decisions.

Good Choices for Many or Optimal Choices for Few: A False Dichotomy

In any endeavour to educate consumers, there is always a tension between providing detailed information (to help people make optimal choices) and providing simple information (to help as many people as possible make good choices).

As an example, we can see this tension playing out with nutrition labeling around the world. Some countries have opted for simple, front of package warnings while others have chosen comprehensive back of package information.

When it comes to disclosure of key information to investors, these need not be mutually exclusive.

CARP recommends that every investor receive from MFDA members, and indeed all firms that sell products with an investment component, a simple, large font, easy to read info graphic that lists, in one place, both total returns and total costs.

Here is an example of such a graphic:

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Example of a Simple Investment Performance Graphic

	Your Investment Performance		
	1 year	5 year	Since you began investing with us
You earned (after all costs)	$50,000	$500,000	$750,000
You paid (*total* costs paid)	$5,000	$75,000	$125,000

Notes

This graphic includes both earnings and costs in one place, all costs are included (not just costs paid to MFDA member firms), and amounts are shown in dollars rather than as percentages.

Additional information such as percentage returns or fees, cost breakdowns, for example between advice and product can be provided separately, but we believe many investors will be far better served, and make better investment decisions when provided with this clear, information about their investment's performance.

This information should be provided on periodic statements and in any other places (such as online reports) where investors access information about investment performance. The information may be calculated and updated annually but must be disclosed more regularly.

MFDA and other regulators should issue plain language educational materials on how to use this information for better/smarter investing.

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The Case for Simple, Universal, Full Cost Reporting

MFDA members will understandably focus on and manage the costs they control. But this limited focus does not serve investors, as ultimately the rate of growth of their savings is dependent on the *total* fees they pay.

While CARP still strongly supports the banning of all embedded fees and the adoption of a Best Interest Standard, we believe full disclosure of fees would provide some aid to current and future seniors.

All Costs and Fees Paid to be Included

The MFDA's consultation document asks for comment on which costs should be included. CARP believes it is critical that all costs paid by the investor, directly or indirectly, must be reported. A mandate to report all costs ensures that firms are not incented to create new cost categories which effectively subvert full cost reporting.

Beyond the MFDA

CARP commends the MFDA for taking on this critical initiative. CARP believes that all firms and institutions that sell products with an investment component must disclose the full costs paid by their customers and have, accordingly, copied IIROC and the CSA on our response.

Timing for Implementation

There are 1,000 people turning 65 every day. There are now more individuals 65 and over than under 15. The fastest growing demographic in Canada is those aged 100+. All these statistics underscore the need for an increasing number of individuals to be able to maximize their savings and provide for their own retirement security.

The clock is ticking and the time for implementation is now. CARP believes that it is reasonable for not only MFDA members but all firms and institutions which sell products with an investment component should implement full cost reporting by January 1, 2020.