Joint Forum of Financial Market Regulators

Forum conjoint des autorités de réglementation du marché financier

Consultation Paper 81 - 403

Rethinking Point of Sale Disclosure for Segregated Funds and Mutual Funds

Prepared by
the Canadian Securities Administrators and
the Canadian Council of Insurance Regulators

February 13, 2003

Outline of this paper's contents

Executive summary

The purpose of this consultation paper

This consultation paper marks the latest step in the Joint Forum of Financial Market Regulators' (the Joint Forum) initiative to promote increased harmony between the regulation of segregated funds and mutual funds. The Canadian Securities Administrators (the CSA) and the Canadian Council of Insurance Regulators (CCIR), two of the Joint Forum's constituent members, have jointly developed these proposals to improve the way information about segregated funds and mutual funds is conveyed to consumers who are facing investment decisions. We hope you will provide us with your comments on these proposals.

The problems we intend to address

Our proposals grow out of our recognition that the point of sale disclosure regimes for segregated funds and mutual funds do not operate as we intended. We have learned that consumers do not use the information folder or prospectus to inform their purchase decisions because most do not realize the significance of the information they contain. Many do not read them at all before tossing them into the recycling bin. Sales representatives tend to dismiss the utility of these documents and most do not use them in the sales process. Insurance companies and mutual fund management companies find the current mandated disclosure documents costly to produce and deliver.

Although regulators and the industry have made significant strides over the past several years to improve and simplify disclosure documents, we believe our disclosure systems have become disconnected from industry practice and consumer needs. This disconnect means our systems do not meet our objective of providing consumers with the information necessary for informed decision-making. We see four primary reasons behind this disconnect.

1. *Our laws assume fund consumers need more information than other investors.* Our disclosure system is based on long-standing assumptions about the needs of segregated fund and mutual fund consumers. These assumptions may no longer be supportable, particularly when we consider the range of information available to consumers about their funds.

2. *The disclosure documents try to do too many things at once.* They are multi-purpose documents intended to be all things for all people. They contain not only a description of the funds and their management, but also basic educational information about investing, data on the fund's track record, a description of the consumer's legal rights, and distribution information. As a result, they are daunting to read and it is difficult for consumers to identify and digest the information contained in them.

3. *The information gets to consumers at the wrong time.* Consumers do not receive disclosure documents until the purchase decision has effectively been made. This makes it next to impossible for the information in these documents to factor into the decision-making process.

4. *The information is delivered to consumers in the wrong form.* Commercially printed disclosure documents are expensive to produce and deliver and they are too bulky to be an effective sales tool. Information in a printed document is soon out of date.

Matters are further complicated for mutual funds because securities legislation drafted with public offerings in mind is not well suited to the realities of mutual fund sales and because the legal requirements vary among the provinces.

Our proposals

To solve the disconnect, we must first break with traditional thinking about fund consumers and about funds and their disclosure. The realities of the marketplace must be recognized by any proposed changes. Our proposals are designed to bring information to consumers when they need it, in a form they can use, and in a cost-effective, practical manner. We believe consumers need reliable, accessible written information about individual funds and our proposals are about making sure our disclosure systems meet that need. The system of disclosure we propose rests on four cornerstones:

1. *Foundation document.* Each fund will have a base disclosure document. This document will contain all of the relatively static information about the features of the fund, the operator, and other service providers. It will define the fund and circumscribe the activities of industry participants with respect to the fund. Unlike current point of sale disclosure, the foundation document will not be called upon to educate consumers about investing, describe the track record of the fund, or describe sales options that consumers negotiate with their sales representatives. Operators will make this document available electronically (via web-based postings) and in paper at all times. We propose that access-equal-delivery for this document.

2. *Continuous disclosure record.* Each fund will prepare annual audited financial statements and unaudited semi-annual financial statements. Operators will also prepare regular discussions of each fund's performance during specified financial periods. The continuous disclosure record of the fund will be available electronically (for example, through web-based postings) and in paper at all times. Similar to the foundation document, we propose that access-equal-delivery for these documents.

3. *Fund summary document.* Each fund will prepare a one- or two-page fund summary to communicate key information that is unique to the fund. This document will also highlight the availability of more detailed information in the foundation document and the continuous disclosure record. Fund operators will make this document available to sales representatives and sales representatives will offer it to all consumers before a purchase is made. Fund operators may use electronic technologies to make the information contained in this document available to consumers and sales representatives.

4. *Consumers' guide.* Market participants will offer a consumers' guide to those consumers they believe will benefit from reading it. The consumers' guide will contain objective educational information about segregated funds and mutual funds. The consumers' guide will not be a fund specific document. It will be available electronically, as well as in paper.

Because all of the relevant information about a fund will be available to consumers before the point of sale, we recommend that the existing rights of withdrawal and rescission attached to the delivery of mutual fund prospectuses be eliminated.

How to read this paper

Plain language

We wrote this paper in plain language to make it easy to read. We avoided industry specific language and kept the paper as concise as possible. We present very little background information, legal analysis, or statistical data. We do not summarize earlier commentators' recommendations for reform in this paper, though we did review and consider them.

Text boxes contain background and explanatory information

Any background and explanatory information we give is presented in text boxes throughout the paper.

Terminology used in this paper

Segregated funds and IVICs
We use the popular term "segregated fund" to refer generically to a specialized insurance product. Legally, a consumer enters into an individual variable insurance contract (an IVIC), which is a life insurance contract, with an insurance company. This gives the consumer the right to choose among a number of segregated funds. The value of the IVIC depends on the value of the particular segregated fund chosen. When the context demands, we use the term IVIC to refer specifically to the contract of insurance.

Consumers, policyholders, and unitholders
Someone who enters into an IVIC is called a policyholder or a contractholder. Someone who buys a mutual fund is an investor and is a unitholder of that mutual fund. We refer to policyholders and unitholders generically as consumers in this paper.

Insurance companies and fund management companies
Insurance companies offer and manage IVICs and segregated funds. Mutual fund management companies sponsor and manage mutual funds. We refer to these companies generically as "operators".

Point of sale disclosure documents, information folders, and prospectuses
The point of sale disclosure document for a segregated fund is called an information folder. Legally, an information folder is in respect of each IVIC. The annual audited financial statements of the segregated fund are included in the information folder. The point of sale disclosure document for a mutual fund is its simplified prospectus. The annual information form and financial statements of the mutual fund are incorporated by reference into the simplified prospectus. When we refer to a mutual fund prospectus in this paper, we are referring to both the simplified prospectus and the annual information form. The document that gets delivered to mutual fund investors is referred to as the simplified prospectus. In this paper we refer collectively to information folders and prospectuses as point of sale disclosure documents.

Continuous disclosure
We refer to the information that funds and their operators are required to give or make available to consumers on a periodic basis following their purchase as continuous disclosure documents. Today, these documents include the annual audited financial statements and semi annual unaudited financial statements of the funds. For mutual funds, they also include press releases, material change reports and meeting materials. For segregated funds, they also include specified annual notices and notices of fundamental changes.

How to provide your comments

The importance of public comment

We want to have your input and continue our open dialogue with industry participants. We are particularly interested in hearing from consumers. We need to hear from you if we are to achieve our regulatory objectives while balancing the interests of all stakeholders.

Shadowed text boxes contain issues for comment

We have raised specific issues for you to comment on in shadowed text boxes throughout this paper, however we welcome your input on all aspects of the consultation paper. Please feel free to speak to some, or all, of our issues for comment or give us your overall impressions.

Due date

Your comments are due by April 30, 2003.

Where to send your comments

Comments should be sent to the Joint Forum and the members of the CSA and the CCIR care of:

Stephen Paglia, Senior Policy Analyst
Joint Forum Project Office
5160 Yonge Street,
Box 85, 17th floor
North York, ON, M2N 6L9
Telephone: 416-590-7054
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e-mail: spaglia@fsco.gov.on.ca

How to format your comments

Send your letters by electronic mail or send us two copies of your letter along with a diskette containing the document in either Word or WordPerfect format.

All comments are public

Please note that we cannot keep your submissions confidential because legislation in certain provinces requires us to publish a summary of written comments received during the comment period. All comments will also be posted to the OSC web-site at www.osc.gov.on.ca to improve the transparency of the policy-making process.

The evolution of our proposals

Harmonizing the regulation of segregated funds and mutual funds

As mutual funds and segregated funds gained in popularity with Canadian consumers, regulators realized that they needed to better understand the differences and similarities between these investment options and between their respective regulatory schemes. In May 1999, the Joint Forum released a *Comparative Study of Individual Variable Insurance Contracts (Segregated Funds) and Mutual Funds.*[1] Later that year, the Joint Forum published its *Recommendations for Changes in the Regulation of Mutual Funds and Individual Variable Insurance Contracts.*[2] In that report, the Joint Forum recommended that work be done in three areas to further harmonize segregated fund and mutual fund disclosure. These appear as recommendations 3, 4 and 5, as numbered in that report:

3. (A) It should be clear who is responsible for delivering the disclosure documents to consumers.
   (B) Consumers should be empowered to make informed purchasing decisions by having a reasonable opportunity to review the disclosure documents before making a binding purchase decision.

4. Consumer education would be enhanced and product disclosure simplified by delivering to the consumer a standardized consumers' guide upon opening an account to purchase a product.

5. Consumers are entitled to regular financial reports about the products they own. These reports should include audited annual financial statements and semi-annual unaudited statements, together with a discussion from the manufacturer about the past period's performance and operation of the product.

What is the Joint Forum of Financial Market Regulators?

The Joint Forum is a working forum formed in 1999 by the CSA, the CCIR, and the Canadian Association of Pension Supervisory Authorities (CAPSA). It seeks to pro-actively co-ordinate the development of harmonized (both cross-sectoral and cross-jurisdictional) approaches to financial services regulation. Its role is to support the CSA, CCIR and CAPSA to address gaps and areas of overlap in the regulation they administer.

The Joint Forum asked staff at the Ontario Securities Commission (OSC) and the Financial Services Commission of Ontario (FSCO) to co-chair a committee of CSA and CCIR staff to work towards implementing the recommendations for increased harmony between segregated fund and mutual fund regulation.

[1] Published, in Ontario, at (1999) 22 OSCB 2761. Available on the OSC web-site at www.osc.gov.on.ca.

[2] Published, in Ontario, at (1999) 22 OSCB 8067. Available on the OSC web-site at www.osc.gov.on.ca.

Industry consultation

To develop the proposals described in this consultation paper, staff of the OSC and FSCO carried out consultations with:

- The joint regulatory and industry group convened to develop the *Comparative Study of Individual Variable Insurance Contracts (Segregated Funds) and Mutual Funds* in 1999. Members of this group also wrote, edited and commented on versions of the draft consumers' guide that forms part of our proposals.

- A working group convened by The Investment Funds Institute of Canada (IFIC) to help us understand how the prospectus delivery requirements work in practice.

- A working group convened by the Canadian Life and Health Insurance Association (CLHIA) to help us understand how industry participants and consumers use information folders.

- Sales representatives (licensed to sell both mutual funds and segregated funds) who provided us with feedback on the sales process and how they use point of sale disclosure documents.

We greatly appreciate the input of these groups and we thank them for the time they spent with us. We will continue to work closely with these and other industry participants as we move forward.

Research on consumers and sales representatives

We believe that research on consumers and sales representatives is particularly important for a project of this nature because our proposals will have a direct impact on them. Our understanding of how consumers and sales representatives use disclosure documents is largely based on anecdotal information, together with information derived from the earlier research referred to in the text box below. We want to verify anecdotal information and update earlier research. We are very pleased that the Investor *e*.ducation Fund[3] has agreed to share the results of a major consumer and industry study it has recently undertaken. The Investor *e*.ducation Fund's research is designed to allow the Fund to develop a learning framework that will guide the Fund's adult education initiatives. As part of this work, the Fund will be capturing information about the use of disclosure documents by consumers and sales representatives, as well as their information needs. We will consider the research data obtained by the Fund, along with the comments we receive, before moving to our next steps.

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[3] The Investor *e.* ducation Fund was established by the OSC in 2000 to develop research, programs and partnerships to promote investor education. It is funded by enforcement settlements and governed by an independent board of directors. More information about the Fund is available at www.investoreducationfund.ca.

Earlier consumer research studies

The CSA and the OSC have periodically carried out consumer research since the mid-90's. The following studies consistently conclude that mutual fund prospectuses are not well used by consumers. Instead, most consumers rely on advice they receive from banks, their financial advisers, friends and family. They also look to information from the Internet, newspapers, magazines and books on investing.

Here are some consumer research reports of the OSC, CSA and other groups:

- Investment Behaviour & Awareness of the Ontario Securities Commission - Final Report for the OSC by Angus Reid Group, Inc. March 18, 1998.
- Fund Summary Research Report prepared for The Investment Funds Institute of Canada by AC Nielsen-DJC Research, November 1998.
- CSA Investor Education Week survey conducted for the Canadian Securities Administrators Investor Education Committee by Angus Reid Group, Inc, March 1999.
- Learning to Invest: A study of appropriate learning environments for the delivery of investor education, for the Investor *e*-ducation Fund by the University of British Columbia, March 29, 2001.
- A Study of Ontario Consumers' Investment Education Needs, for the Ontario Securities Commission by the Consumers Council of Canada, February 2002.
- Canadian Shareowners Study by The Toronto Stock Exchange, July 2002.

Our legal analysis—the background paper

We are publishing this consultation paper with a background paper entitled, *The Regulation of Point of Sale Disclosure for Segregated Funds and Mutual Funds*. In that paper, OSC and FSCO staff analyse the legal requirements governing how and when consumers receive information about their investments. This analysis reveals that the law is complex and confusing, particularly in the mutual fund area. The background paper contains compelling evidence that regulatory reform is needed to clarify and harmonize the laws across Canada and to ensure they keep pace with the changing marketplace. Both this consultation paper and the background paper are available on the OSC web-site at www.osc.gov.on.ca and the FSCO web-site at www.fsco.gov.on.ca.

How our proposals intersect with other initiatives

We are publishing this consultation paper during an active period of regulatory reform and we have benefited from the thinking that underlies the following projects:

- The OSC Fair Dealing Model. The OSC Fair Dealing Model can be viewed on-line at the Fair Dealing web-site www.fairdealingmodel.com or at the OSC web-site www.osc.gov.on.ca. Although our disclosure system can be implemented independently, it is compatible with and complementary to the OSC Fair Dealing Model. We note that the OSC Fair Dealing Model contemplates items of disclosure that overlap with parts of our proposed disclosure system. For example, information sheets providing educational information about the instruments chosen by consumers overlap with our consumers' guide. The OSC Fair Dealing Model also contemplates disclosure that supports our proposed system. For example, the Fair Dealing Document that outlines the dealer-client relationship should make it possible for us to streamline the way we handle distribution-related disclosure.

- The CSA's project to revamp continuous disclosure for investment funds. The CSA published proposed National Instrument 81-106 Investment Fund Continuous Disclosure for comment on September 20, 2002.[4] If adopted, the implementation of this National Instrument would complete the second cornerstone of our proposed disclosure system for mutual funds.

- The CSA's project to harmonize the continuous disclosure requirements as part of a move towards an integrated disclosure system for corporate finance issuers. The CSA published proposed National Instrument 51-102 Continuous Disclosure Obligations for comment on June 21, 2002.[5] Our initiative has strong parallels to the work that is being done in the area of corporate disclosure. It can be understood as integrated disclosure tailored for investment funds. The CSA are evolving away from a traditional emphasis on prospectuses towards an increased focus on continuous disclosure.

[4] In Ontario, at (2002) 25 OSCB 6273. Proposed National Instrument 81-106 can also be viewed on-line at the OSC web-site at www.osc.gov.on.ca.

[5] In Ontario, at (2002) 25 OSCB 3637. Proposed National Instrument 51-102 Continuous Disclosure Obligations was anticipated in January 2000 with the CSA's Concept Proposal for an Integrated Disclosure System (published in Ontario, at (2000) 23 OSCB 633). Both the proposed national instrument and the Integrated Disclosure System concept proposal can be viewed on-line at the OSC web-site at www.osc.gov.on.ca.

- The British Columbia Securities Commission's (BCSC) proposals entitled *New Proposals for Mutual Fund Regulation* released on November 11, 2002.[6] The BCSC has participated in the development of this consultation paper as part of the CSA and we collectively believe our proposed disclosure system is consistent with the spirit of the BCSC proposals. The BCSC heard from industry during consultations it had in December 2002 after it published its proposals. Based on what it learned during its consultations and on its subsequent discussions with other CSA members, the BCSC has decided to put its efforts into this Joint Forum proposal rather than to proceed with its own mutual fund proposals as a separate initiative.

- The CCIR's project to streamline and harmonize provincial insurance regulations. The CCIR are soliciting proposals from industry and other stakeholders. It will review and consult with industry on the proposals received, assess the implications of the requested changes and report on the priority of specific proposals. The CCIR expects to develop a work plan to address high priority proposals.

How our proposals relate to the regulation of other investment funds

Although this paper only deals with the disclosure requirements for segregated funds and mutual funds, we believe the concepts described here may be easily extended to other publicly offered investment funds, such as commodity pools, labour sponsored investment funds, exchange traded funds, closed-end funds and quasi closed-end funds. We will explore the applicability of our proposed disclosure system to other investment funds as follow-on work to this project. Proposed National Instrument 81-106 Investment Fund Continuous Disclosure applies to all investment funds and has, therefore, paved the way for the extension of our proposals.

[6] British Columbia Securities Commission *New Proposals for Mutual Fund Regulation* November 14, 2002. This document can be found at the BCSC web-site at www.bcsc.bc.ca.

Additional references

The following sources informed our thinking. Most are available on line at the OSC's web-site www.osc.gov.on.ca or at the web-site indicated.

Investment fund sources

- *Report of the Canadian Committee on Mutual Funds and Investment Contracts – Provincial and Federal Study*, 1969, Queen's Printer, 1969.
- *Regulatory Strategies for the Mid-'90s: Recommendations for Regulating Investment Funds in Canada*, prepared by Glorianne Stromberg for the Canadian Securities Administrators, January 1995.
- *The Stromberg Report: An Industry Perspective*, prepared by the Investment Funds Steering Group for the Canadian Securities Administrators, November 1996.
- *Investment Funds in Canada and Consumer Protection: Strategies for the Millennium*, prepared by Glorianne Stromberg for the Office of Consumer Affairs, Industry Canada, October 1998.
- Canadian Securities Administrators Notice 81-301 *Mutual Fund Prospectus Disclosure – Concept Proposal* Request for Comment (1997) 20 OSCB 559.
- Canadian Securities Administrators Notice of Proposed National Instrument 81-101 Mutual Fund Prospectus Disclosure Request for Comment (1998) 21 OSCB 1; and Notice of Proposed Changes to National Instrument 81-101 Request for Comment (1999) 22 OSCB 13 and Notice of Rules and Policy National Instrument 81-101 (1999) 22 OSCB (Supp.2).
- Canadian Securities Administrators Notice of Proposed National Instrument 81-106 Investment Fund Continuous Disclosure (2002) 25 OSCB 6273.
- British Columbia Securities Commission *New Concepts for Securities Regulation* February 18, 2002. British Columbia Securities Commission *New Proposals for Mutual Fund Regulation* November 14, 2002. These documents can be found at the BCSC web-site at www.bcsc.bc.ca

International sources

- *Report on Investment Management – Principles for the Regulation of Collective Investment Schemes and Explanatory Memorandum* Technical Committee of the International Organisation of Securities Commissions, July 1995. This document and the other IOSCO documents we cite can be found at IOSCO's web-site at www.iosco.org.
- *Objectives and Principles of Securities Regulation* Technical Committee of the International Organisation of Securities Commissions, September 1998.
- *Investor Disclosure and Informed Decisions: Use of Simplified Prospectuses by Collective Investment Schemes* Technical Committee of the International Organisation of Securities Commissions, March, 2002.
- The Australian Securities and Investments Commission Policy Statement 168, *Disclosure: Product Disclosure Statements (and other disclosure obligations)* November, 2001. This document can be found at ASIC's web-site at www.asic.gov.au.
- Discussion Paper, *Informing Consumers: a review of product information at the point of sale* Financial Services Authority (UK) November 2000. This document can be found at the FSA's web-site at www.fsa.gov.uk.

The disconnect between theory and practice

Disclosure has always been at the heart of securities and insurance regulation. Our consumer protection strategies aim for a well-informed consumer who understands the implications of a purchase decision. For this reason, we direct much regulatory effort towards ensuring sponsors of financial products provide complete and accurate disclosure.

Notwithstanding our commitment to point of sale disclosure as a regulatory strategy, it has become apparent to us that there is a significant disconnect between theory and practice. Industry participants tell us that:

- Consumers do not use point of sale disclosure documents to help them make their purchase decisions. They do not read the documents because they find them daunting. Most do not perceive the significance of these documents.

- Sales representatives tend to dismiss the utility of these documents and they do not use them in the sales process. They dislike the documents, in part, because they feel they are lengthy, legalistic documents containing stale-dated information. Marketing brochures and other documents, such as one-page summaries prepared by third party information providers (often available on-line), are thought to be more useful as sales documents.

- Operators find the mandated disclosure documents costly to write, produce and deliver.

It appears the existing disclosure regimes do not work particularly well in practice.

In this part of the paper, we examine both of the existing disclosure regimes in an attempt to understand why the disconnect occurs. We begin by identifying *why* we give consumers the information we do. As you will see, the underlying policy rationales are largely the same for information folders and prospectuses. We then discuss the form this information takes—*what* we deliver to consumers—and the mode of delivery—*how* delivery is effected. We conclude that the different point of sale documents are packaged and delivered in similar ways, although they vary somewhat in their content. Finally, we turn to the questions: *who* is responsible for delivery and *when* must delivery occur? Here, we explain how segregated fund and mutual fund regulations diverge in these areas and describe the issues relating to the delivery of mutual fund prospectuses.

Issues for comment

01. Do you agree with our description of the disconnect between theory and practice in this part of the consultation paper? Are there any differences between segregated funds and mutual funds that we should keep in mind as we work to improve their respective disclosure regimes?

Why do we ask for the disclosure we do?

The existing point of sale disclosure documents have several objectives. These include:

Informing consumers

As regulators, we believe it is crucial for consumers to have access to meaningful written information about segregated funds and mutual funds so they can make informed purchasing decisions. Consumers need to have reliable[7] accessible written information above and beyond verbal communications and sales materials. The existing point of sale disclosure documents contain the following information:

- *A description of what they are purchasing*. This includes all of the relatively static information about the features of the fund (including investment objectives, risks and fees), the operator, the other service providers and (on the segregated fund side) the terms of the IVIC.

- *A snap shot of the changing features of the fund*. Simplified prospectuses and information folders provide a picture of the fund's track record, including its past performance, financial highlights, and a snap shot of the fund's largest holdings as of a certain date.

- *An explanation of the mechanics*. This includes a description of the purchase options, an explanation of how to buy and sell the fund, how the fund is valued, and a summary of the consumer's legal rights.

- *Background and ancillary information*. This includes information about how the fund was formed, the material contracts, and (on the mutual fund side) how dealers are compensated.

Defining the fund and the duties of the operator

Information disclosed in point of sale disclosure documents must be accurate, complete and definitive—consumers must be able to rely on it, and operators must be accountable for it. The information folder and prospectus circumscribe the actions of operators, they ensure portfolio managers invest in accordance with stated objectives, and they limit what a sales representative can communicate in a sales pitch. These documents define how these funds will be managed and they allow regulators to monitor industry compliance with applicable rules. They also work to limit the liability of the operator—in the case of a misunderstanding between a consumer and a fund operator, a written document can work to substantiate the operator's position.

Using disclosure as a check and balance

Disclosure is sometimes used as a regulatory tool. Certain pieces of information are disclosed because they impose an additional check and balance on the fund and its operator. For example, disclosure about the business a fund placed with specific brokerage firms during the last year and any legal and administrative proceedings impose a discipline on operators to comply with laws governing such affairs. Fund governance disclosure for mutual funds is included in the annual information form because, among other things, it encourages the fund manager to codify informal

[7] Reliable because the information is certified to be "full, true and plain" in the mutual fund context and "full and plain" in the segregated fund context. Legal consequences flow if either of these certifications prove false.

practices. This type of information is largely mandated because regulators subscribe to the belief that sunshine is an effective disinfectant.

Educating consumers

Both the information folder and simplified prospectus contain some educational information about investing. The simplified prospectus opens with an explanation of what a mutual fund is. Both the information folder and simplified prospectus address the risks of investing and both describe the tax consequences for consumers.

Allowing for comparisons among funds

The simplified prospectus is specifically formatted to promote comparisons among mutual funds. The forms to National Instrument 81-101 Mutual Fund Prospectus Disclosure mandate specific content and encourage a catalogue approach. Thus, the information disclosed, the order in which it is presented, and the wording of headings are standardized to a large degree. Important figures, such as the management expense ratio, are calculated on a uniform basis. Charts, graphs, and tables are presented in a standardized format.

While most information folders are not specifically formatted to promote fund comparisons, they do tend to disclose the same sorts of information in the same ways. Important figures are calculated on a uniform basis and any charts, graphs and tables presenting financial information are presented in a standardized format.

What do we deliver to consumers?

A comprehensive document

Both the information folder and the simplified prospectus are intended to be comprehensive documents that contain all the information necessary for informed decision-making by consumers. The information contained in them is designed to flow to the consumer at one time. The theory is that all of the information necessary for informed decision-making should be found in one place and should be actually given to consumers. [8] Since most fund operators prefer to prepare disclosure documents that describe all of their funds, some information folders and simplified prospectuses are close to 300 pages long.

Both the information folder and simplified prospectus contain information that is repeated elsewhere. The information folder repeats the information in the IVIC because the contractual obligations under the IVIC are thought to be important to consumers. This means consumers receive some information twice—once before the point of sale in the information folder and once after the point of sale in the IVIC. The annual information form for mutual funds is intended to supplement the information contained in the simplified prospectus, however fund operators may

[8] Since 1986 when the CSA adopted National Policy Statement No. 36, the CSA recognized that some information important for “full, true and plain” disclosure purposes need not be given to mutual fund consumers at the point of sale in a simplified prospectus. The current annual information form is intended as a supplemental disclosure document available for those investors who want more information. Mutual fund financial statements are incorporated by reference – and need only be given to those consumers who ask for them. The information folder is not always a comprehensive document either because some of the mandated information can be delivered in separate documents—namely the financial highlights and the summary fact statement.

repeat information in the annual information form where this information is necessary to make it comprehensible as a free-standing document. The financial highlights in the simplified prospectus are derived from the financial statements.

A simplified document

Both the information folder and the simplified prospectus are simplified documents, designed to be read and considered by consumers. They are written in plain language and presented in a format that assists with readability and comprehension. Recent regulatory reforms on both sides have been directed towards simplifying the point of sale disclosure documents to increase their use by consumers. Today, point of sale disclosure documents are markedly easier to consult and read than the legalistic and dense documents we used to see.

How is delivery effected?

Physical delivery

Information folders and simplified prospectuses are both commercially printed and physically delivered to consumers. The law does not permit sales representatives or operators to discharge the delivery requirements by explaining the information verbally.

Electronic delivery

Although the CSA and the province of Ontario have permitted certain documents to be delivered electronically for the last several years,[9] we understand the industry has not yet embraced electronic delivery, notwithstanding the significant use that Canadian consumers make of the Internet.[10] Difficulties with obtaining consent from individual consumers may be behind the industry's reluctance in this area. Today's point of sale disclosure documents may also overwhelm the capacities of the home computer systems used by many consumers.

SEDAR (the System for Electronic Document Analysis and Retrieval) is the system used for electronically filing most securities related information with the Canadian securities regulatory authorities. Although the SEDAR system allows consumers to gain immediate web-based access to mutual fund prospectuses and the continuous disclosure record, the fact that the information is in the public domain does not alter the delivery requirements. Postings on SEDAR or any other Internet site cannot be relied upon to satisfy the current delivery requirements.

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[9] See our background paper for a more complete discussion of electronic delivery. The CSA adopted National Policy 11-201 Delivery of Documents by Electronic Means and the Ontario government enacted the *Electronic Commerce Act, 2000*, S.O. 2000, c. 17.

[10] Over 5.8 million Canadian households (49%) had at least one member who regularly used the Internet from home in 2001. 7.2 million households (60%) have at least one member who used the Internet regularly from home, work, school or any other location. Quebec, Ontario and British Columbia recorded the highest rates of growth in Internet use, with 65% of households in these provinces accessing the Internet from any location. Statistics Canada Household Internet Use Survey July 2002.

Who is responsible for delivery?

Divergent approaches: the manufacturer vs. the distribution firm

In the segregated fund context, the insurance company is responsible for delivering the information folder, although, in practice, sales agents actually give the document to consumers and obtain the required written acknowledgement. In the mutual fund context, the responsibility lies with the distribution firm rather than the fund manager.

The mutual fund requirements

Some market participants find the legislative provisions that set out the dealer's obligation to deliver the mutual fund prospectus to be confusing for a number of reasons:[11]

- The legal test is difficult to understand and apply due, in part, to the fact that it is framed using multiple negatives.

> **Example**
> The obligation to deliver a prospectus lies with the dealer not acting as agent of the purchaser. According to the legislation, "a dealer shall not be considered to be acting as agent of the purchaser unless the dealer is acting solely as agent of the purchaser with respect to the purchase and sale in question and has not received and has no agreement to receive compensation from or on behalf of the vendor with respect to the purchase and sale." R.S.O. 1990, c. S.5, s. 71(7).

- The test can give rise to idiosyncratic results.

> **Example**
> Some market participants have suggested that a dealer who receives a front-end load sales commission from a purchaser is not required to deliver the prospectus to the purchaser so long as the dealer has a copy pursuant to s. 71(5). We believe this interpretation is problematic—surely something as pivotal as the obligation to deliver a prospectus should not turn on the type of sales charge an investor chooses.

- There is a gap between what is required of the mutual fund manager who prepares the simplified prospectus and the dealer who delivers it. The dealer's obligation to deliver the prospectus is not supported by a corresponding obligation on the part of the mutual fund manager to ensure the dealer receives the prospectus once it has been prepared. The mutual fund manager appears to have no obligation to ensure the prospectus reaches the dealer or the consumer, unless the manager is also acting as the dealer.

[11] Please refer to the background paper for a complete discussion and analysis of the law.

When must delivery occur?

Divergent approaches: before the sale vs. after the sale

Consumers of segregated funds must acknowledge that they have received an information folder before they sign an application for an IVIC. On the other hand, mutual fund prospectuses, in most provinces, are only delivered within two days of the point of sale. In order to close the loop on the after-the-fact delivery system for mutual funds,[12] our law gives mutual fund consumers the right to get out of their purchases if they change their minds after they have a reasonable opportunity (usually two days) to read the prospectus. This right is called either a right of withdrawal or rescission depending on which provincial legislation you read. As we describe in the text box on the following page, the provincial delivery requirements and the rights of withdrawal and rescission given to mutual fund consumers overlap and are not uniform.[13]

Issues for comment

02. If you are a mutual fund industry participant (either a fund manager or a sales representative), please comment on your experiences with the rights of rescission and withdrawal. Have you or your clients ever exercised them? Do they work in practice to give consumers real (as opposed to theoretical) rights? If you are a consumer, please tell us whether you knew you had these rights and whether you have ever used them.

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[12] Because the mutual fund simplified prospectus is given to consumers after they make investment decisions, it has been described as being more of a "***retro***spectus" than a "***pro***spectus".

[13] Please see the background paper for a detailed analysis of the rights across the country.

The mutual fund legal rights and obligations across Canada						
	AB, BC, ON, NS, NFLD, SASK	**Manitoba**	**New Brunswick**	**Prince Edward Island**	**Quebec**	**Territories**
When must the dealer deliver the prospectus?	Within 2 days of placing order	Within 2 days of placing order	Before payment if dealer solicited. If dealer did not, no later than delivery of confirmation	Within 2 days of placing order	Within 2 days of placing order	Before delivery of trade confirmation
When must confirmation be delivered?	Promptly after trade	Promptly after trade	Promptly after trade	Not required	Promptly after trade	Within 7 days of the order being made
Do purchasers have any recourse if the prospectus is not delivered?	A right of action for rescission is available for 180 days after the plaintiff should have received prospectus. A right of action for damages is available for the lesser of 3 years from date prospectus should have been received or 180 days after the plaintiff first had knowledge of the facts giving rise to the action.*	Nothing express	A right of rescission (*ab initio*) so long as notice is given to the dealer within 60 days of delivery of the trade confirmation.	A right of action for rescission is available for 180 days after the plaintiff should have received prospectus. A right of action for damages is available for lesser of 3 years from the date of the transaction or one year after plaintiff first had knowledge of facts giving rise to action.	A right of action for rescission is available for 3 years from the date of transaction A right of action for damages is available for 3 years from date of transaction	A right of rescission (*ab inito*) so long as notice is given to the dealer within 60 days of delivery of the trade confirmation.
Do purchasers have any rights triggered by delivery of the prospectus?	A right of withdrawal. Must give notice no later than 2 days after receipt of prospectus.	A right of withdrawal Must give notice no later than 2 days after receipt of prospectus.	A right of rescission. Must give notice no later than 7 days after delivery of prospectus if it's delivered within 60 days of confirmation.	A right of withdrawal. Must give notice no later than 2 days after receipt of prospectus.	A right of rescission. Must give notice no later than 2 days after receipt of prospectus.	No
Do purchasers have any rights triggered by delivery of the trade confirmation?	A right of rescission for mutual funds under $50,000. Must give notice within 48 hours of receiving confirmation.	No	A right of rescission, but only if prospectus is not received. Must give notice within 60 days of receiving trade confirmation.	No	No	A right of rescission. Must give notice within 60 days of delivery of trade confirmation.

[*] In **Alberta**, the right of action in damages is available for the lesser of 180 days from the day the purchaser first had knowledge of the facts giving rise to the cause of action or one year from the day of the transaction. In **Saskatchewan**, it is available for the lesser of 1 year after the purchaser first had knowledge of the facts giving rise to the cause of action or 6 years after the date of the transaction.

The root of the problem

Our understanding of the disconnect between theory and practice leads us to conclude:

Our laws assume fund consumers need more information than other investors

As we describe in the text box below, our disclosure systems are based on long-standing assumptions about the types of consumers that invest in mutual funds and segregated funds. Because these consumers were seen as less sophisticated, they were offered greater protections and given more information than other investors and insurance purchasers. Given the changes in the market share of these types of funds and the increased awareness on the part of many investors means that these assumptions may not be supportable today, particularly given the range of information available to consumers about their funds.

Why do our laws give fund consumers more information?

Fund consumers are given more information than other sorts of investors and purchasers of insurance for four reasons:

1. Regulators have traditionally assumed that fund consumers have greater information needs than investors in other securities, such as corporate stocks, because they are less sophisticated players who need additional consumer protection.

2. When our disclosure systems were first developed, mutual funds and segregated funds were not the mainstream investment vehicles they are today. Regulators were influenced by the fact that fund consumers, unlike investors in corporate stocks, did not generally have the benefit of market analysis by experts. Analysts did not traditionally follow segregated funds and mutual funds and these funds were not typically sold through stock-brokers and full service dealers.

3. The fact that securities legislation was not drafted with mutual funds in mind gives rise to anomalous results. The law requires newly issued securities to be sold with a prospectus. Previously issued securities that are sold on the secondary market need not be sold with a prospectus because it is assumed that, by that time, there is already sufficient information in the public domain. Mutual funds are always caught by the prospectus requirements because mutual fund units are always issued from treasury. Mutual funds that have existed for many years will always be sold with a prospectus, even though there may be ample information about them in the public domain, while investment funds whose shares trade on stock exchanges (ETFs), need not be sold with a prospectus, even though they are no different from mutual funds in the eyes of investors.

4. When segregated funds were first developed, insurance regulators recognized the differences between segregated funds and other insurance products. They wanted to harmonize the disclosure systems for segregated funds with the disclosure systems for mutual funds and, therefore, chose to follow the point of sale disclosure requirements in place for mutual funds.

The information folder and simplified prospectus try to do too many things at once

They are multi-purpose documents containing not only a description of the funds and their management but also basic educational information on investing, track record and past performance data, a description of the consumer's legal rights, and information about the way the funds are distributed. As a result, disclosure documents can be daunting to read and it is difficult for consumers to identify and digest the information contained in them. Important facts are obscured and less important information receives more attention than it may deserve.

The disclosure documents are designed to give all consumers the same information no matter how sophisticated they are. Both regulators and fund operators intend for the documents to convey essential information at point of sale—however, views differ on what is essential.

The information gets to consumers at the wrong time

Consumers receive neither the information folder nor the simplified prospectus until the purchase decision has already been made. In practice, we believe neither a segregated fund consumer nor a mutual fund consumer has a real opportunity to actually read the relevant disclosure document before making his or her purchase. In our minds, a lengthy disclosure document delivered at, or just after, the point of sale cannot be of any real value in the decision-making process.

Consumers need some information much earlier than they receive it. Conversely, consumers don't need other information at all to make informed investment decisions. We question whether all consumers need the same level of information. Some consumers may want more details on their investment, while others only need to understand the basic features of their chosen fund.

Certain information just comes too late to benefit consumers. For example, consumers need to learn about the basics of investing before they make their first purchase. If they don't know what a mutual fund is, we believe they would be well advised to find out before spending their retirement savings on one. Any dealer-related information also comes too late. By the time the mutual fund investor has learned from the simplified prospectus that he or she has the ability to negotiate the front-end sales charge with his or her dealer, the deal is already done.

The information is delivered to consumers in the wrong form

Reliance on physical delivery presents a challenge because commercial copies of disclosure documents are expensive to produce and deliver. They are also cumbersome for sales representatives to use as a reference during the sales process. The information in a printed document is soon stale-dated. Many fund consumers do not see any value in reading through these printed documents and, as such, resent paying for their printing and delivery.

Securities regulation is not uniform and is not well suited to mutual funds

On the mutual fund side, matters are further complicated by the lack of uniformity among the pieces of provincial legislation and the fact that there is an uneasy fit between the delivery requirements and the realities of the mutual fund business.

The rights of withdrawal and rescission for mutual fund consumers, which are described only in the prospectus, are based on unrealistic assumptions about consumer behavior. Most consumers do not read legal documents immediately upon receiving them in the mail.[14] Those who do not immediately read the prospectus, but do so later, will find themselves out of time before they even learn of their rights. Furthermore, the right of withdrawal given to mutual fund consumers is potentially open to abuse and can be open-ended.

Examples
Securities legislation in Ontario does not clarify how, and from where, the money is to flow back to the purchaser once the right of withdrawal has been exercised. It is also silent on how the fund is to be "made whole" if the purchaser exercises the subsection 71(2) right and the NAV drops after the trade date. The right can be used as a put-option because market losses are absorbed by either the mutual fund or the dealer, rather than the purchaser.

This right of rescission is tied to receipt of the confirmation which—unlike the prospectus which must be delivered within 2 business days—must only be delivered "promptly". A purchaser who receives the confirmation after 5 days has a longer "cooling-off" period than one who receives the confirmation after 2 days.

[14] Even for those consumers who do read the simplified prospectus in the applicable time, we question whether they are looking for what they *don't like* about the investment they have made. Conventional theory about consumers' cognitive biases tells us that they are more likely looking for confirmation that they have made the right decision.

Reconnecting theory and practice

The basis for a solution

Any solution we develop must grow from our understanding of the disconnect and its causes. To resolve the disconnect, we believe we must:

Unbundle the documents

The first step is to unbundle the contents of the information folder and simplified prospectus so that we can think about each item independently. Only information that is useful to consumers who are facing an investment decision should be communicated to them at the point of sale.

Think about timing

Once we decide what we need to communicate to consumers to help them make informed decisions, we must think about when they should receive this information. Some information must be received and understood before a consumer makes a purchase decision. Other pieces of information are not needed until afterwards. We must also keep in mind that not all consumers are the same—they have different information needs.

Think about the mode of delivery

In addition to thinking about timing of information, we must also think about its mode of delivery. If information is not packaged in a usable way, it will not be used—the medium is as important as the message.

Be realistic

Solutions must be flexible to accommodate both the insurance and mutual fund industries. They must make economic sense and be aligned with consumers' needs. We believe we can capitalize on advances in technology and consumers' access to that technology. We must also recognize the tremendous increase in information about funds and investing in general that is available today. Much of this information is objective and non-product specific.

Ensure it happens on a national basis

Segregated funds and mutual funds are sold in all provinces and territories of Canada. Solutions must be uniformly applied in all regions.

Our proposals

An overview

To solve the disconnect, we must break with traditional thinking and recognize the realities of the marketplace. Our proposals are designed to bring information to consumers when they need it, in a form they can use, and in a cost-effective, practical manner. We believe consumers need reliable accessible information about individual funds—our proposals are about making sure our disclosure systems meet that need.

We propose to replace the existing point of sale disclosure documents with two new documents that the operator will be responsible for—a very short fund summary document that is offered to consumers before they make an investment decision and a longer foundation document that is available electronically and in paper for those consumers who want it. Documents forming part of a fund's continuous disclosure record will also be available for those consumers who want to learn about the past performance of the fund. We recommend that educational information be made available for those consumers who need and want it.

The documents described here form the cornerstones of our proposed disclosure system. In the following pages, we describe each of the cornerstones in more detail. We also describe how we propose to deal with the following questions:

- Who should make the various documents available to consumers?
- Who should be accountable for the contents of these documents and to whom should they be accountable?
- What legal rights will flow to consumers from the delivery and content of these documents?
- In what manner should these documents be filed with regulators?
- How should industry participants keep the information in these documents up-to-date?
- Should the regulators review these documents for compliance purposes? How will they do this?
- How can regulators maintain their discretion to stop a particular fund from being sold to the public under our new disclosure system?

Appendix 2 to this consultation paper contains a matrix illustrating where the disclosure currently contained in the simplified prospectus, annual information form, and information folder would fit in our proposed disclosure system.

The cornerstones of our proposed system

The foundation document

A foundation document for each fund, together with each fund's continuous disclosure record, will form the backbone of our proposed disclosure regime. The foundation document will serve as a fund's base disclosure document. It will define how the fund will be managed. The operator will create and be responsible, together with the fund, for the contents of the foundation document. Consumers will have legal rights should there be any misstatement or material error contained in the document.

The foundation document will describe the static features of the fund, including:

- investment objectives and strategies
- risks of investing in the fund
- the service providers to the fund
- how the fund is valued
- how the fund can be purchased and redeemed
- the fees paid by the fund (including any fees payable directly to operators by consumers).

Each segregated fund's IVIC will be incorporated by reference into its foundation document. The foundation document will tell consumers where they can get a copy of the IVIC used by the fund's operator. The IVIC used by an operator will be available electronically and in paper, in the same way we propose for the foundation document.

The foundation document will not contain generic educational information nor will it contain financial information and performance-related history. This information will be contained in an educational document and the continuous disclosure record, respectively. The foundation document will be short, concise and written in plain language. We expect it to be no longer than 10-15 pages long. You can refer to Appendix 2 for more information on the contents of the foundation document.

Because the foundation document will be evergreen, we recommend that our annual re-filing requirements be dropped.[15] Once a fund has prepared its foundation document, we see no reason

[15] The CSA first introduced the concept of an evergreen disclosure document in 1986 when National Policy Statement No. 36 was adopted. The simplified prospectus under that system was anticipated to be the same from year to year, but it never achieved that status—perhaps because the CSA did not ask legislatures to consider changing securities legislation which requires continuous offering prospectuses to be re-filed annually. The wide-spread industry practice of consolidating information about more than one mutual fund into one document meant that this document changed constantly.

why it will need to be updated or changed annually unless material changes are made to the fund's operations. We will continue to require operators to amend the foundation document when material or significant changes occur to a fund's operations. If amendments are made, we will require the entire foundation document to be re-filed to make it easier for consumers to access the document.

A new fund will deposit a draft foundation document with the regulators for their review. Once the regulator is satisfied with the fund and its operator, a receipt will be issued. A receipt must be received before a fund can begin operations. A final foundation document will be publicly filed with the regulators.[16]

We believe access should equal delivery for this document. Rather than calling on sales representatives to deliver the foundation document to consumers, we will require operators to make the document available electronically through web-based postings at all times. Operators will also be required to deliver a printed copy of the document to those consumers who ask for it. Delivery will be required to take place within a specified number of days after the request is received. Although sales representatives will not be required to deliver the document, they will be required to make consumers aware of it and where they can obtain it (either electronically or in paper format). This will occur before the purchase is made. We expect sales representatives will do this in a meaningful way giving consumers enough time to access the information if they want it.

Issues for comment

03. Our proposals will require operators to post the foundation document and the continuous disclosure documents for each fund they manage on their web-sites. The IVIC used by an insurance company for its segregated funds will also be available electronically and in paper (on demand). Please comment on the pros and cons of this approach.

04. We recommend that consumers have access (either electronically or if they wish, in paper) to an individual foundation document for the fund of their choice. Would it be possible or advisable to allow a foundation document to describe more than one fund—for example, all of the funds in a fund family? Why or why not? How would such a document work?

05. We propose that mutual fund managers make the various documents available on their own web-sites, notwithstanding their availability on SEDAR. Are SEDAR postings, alone, sufficient? Is the SEDAR system structured appropriately to fulfil this function? Please comment on the usefulness of SEDAR for accessing individual disclosure documents about a mutual fund.

[16] We will consider how we can build on our continuing efforts to streamline filing requirements and our review of disclosure documents on a national basis. The CSA are considering building on the mutual reliance review system through a delegation model. This model would see one regulator reviewing disclosure documents on behalf of the other provincial regulators. The CCIR are considering similar concepts for segregated fund disclosure documents.

The continuous disclosure record

Consumers need meaningful access to the track record of their mutual funds or segregated funds. We believe this information should be contained in a continuous disclosure record. The continuous disclosure record will show investors how their funds have been managed over a particular financial period. The operator will prepare and be responsible for the contents of the continuous disclosure documents. This means consumers will have legal rights should there be any misstatement or material error contained in them.

The continuous disclosure record for each fund will consist of:

- audited annual financial statements
- unaudited semi-annual financial statements
- regular statements of fund performance for specified financial periods.[17]

The financial statements will be prepared in accordance with industry standards and practices. The statements of fund performance will contain information about the performance and management of the fund over the specified financial period. The CSA have described specific information requirements for financial statements and statements of fund performance for mutual funds in proposed NI 81-106.

Our laws about the filing requirements for the continuous disclosure record will continue to operate.[18] We recommend that regulators integrate disclosure reviews so that a fund's entire disclosure record is reviewed periodically for compliance purposes.[19]

Like the foundation document, we recommend that access-equal-delivery for continuous disclosure documents, in the context of point of sale. Rather than calling on sales representatives to deliver them to consumers, we will require operators to make these documents available electronically through web-based postings at all times. Operators will also be required to deliver a printed copy of the document to those consumers who request it. Delivery will be required to take place within a specified number of days after the request is received. Sales representatives will be required to make consumers aware of these documents and where they can be obtained before the purchase is made.

The continuous disclosure record at point of sale

Information in the continuous disclosure record serves two different purposes. It lets consumers who have already made their investment know how their funds are doing. When the information is used in this way, it becomes important after the point of sale. The information also plays a role at the point of sale because it helps consumers to decide which funds to buy.

[17] In proposed NI 81-106, the CSA have proposed that these statements be prepared quarterly for mutual funds.

[18] The CSA have proposed changes to the filing requirements for mutual fund financial statements in NI 81-106.

[19] See footnote 16 above.

The fund summary document

Although consumers will have access to the information in the foundation document and continuous disclosure record of a fund, we need to introduce another document that will be used during the sales process. This document, which we call a fund summary document, will meet our goal of giving consumers readily digestible information that is necessary for making investment decisions. We contemplate a one- or two-page fund summary document prepared by operators who will then make them available to sales representatives.

We want to empower consumers to make informed investing decisions based on accurate and reliable information. A short and simple fund summary document, prepared by operators to describe their fund, will allow consumers to do this. These documents will inform consumers of their rights and will tell them where they can get additional information if they need it.

Simplicity, conciseness and the use of plain language will be key to the success of a fund summary document. At minimum, it will contain the following information in point form or tabular formats:

- investment objectives and strategies
- risks
- the management expense ratio of the fund, including its key components
- identity of the operator and portfolio adviser and any other key service provider
- important information about the IVIC
- key past performance information
- where the consumer can locate more information—namely, the foundation document, the continuous disclosure record and the consumers' guide.

The fund specific information in mutual fund simplified prospectuses and the executive summary in an information folder both illustrate the type of information that we anticipate being included in a fund summary document—although we expect the fund summary document will be much shorter. Many operators already have marketing and dealer-use-only materials that contain such summary disclosure. The fund summary document will not contain any generic or explanatory information that is not specific to the fund in question. You can refer to Appendix 2 for more information on the contents of the fund summary document.

Sales representatives will either offer the document, or review its contents with consumers before they make their final investment decision. Sales representatives will take consumers through these documents in a meaningful way as part of the sales process and will tell them about the other, more detailed, information that is available about the fund.

Fund summaries will be filed with regulators. We anticipate filing requirements similar to those for the continuous disclosure record. Since these documents are summaries of information contained in the foundation document and the continuous disclosure record, we do not expect that regulators will need any specified review period before they can be used. Fund operators will be permitted—but not required—to prepare these documents on a periodic basis, tied to the timing of the fund performance updates. This will allow the performance information contained in these documents to be kept updated.

Some practical issues surrounding fund summary documents

This part of our proposal presents some challenges, both to the regulators and to industry participants. We must turn our minds to the following issues:

a. Operators will be required to prepare a separate fund summary document for each fund. How will they ensure sales representatives receive copies of these documents? How can this aspect of our proposals be handled administratively? Will technology assist? For example, can operators make these documents available on their web-sites for sales representatives to access?

b. How will operators update these documents? How will they ensure the updated versions of the documents are used appropriately by sales representatives?

c. How will the proposed document work when sales are carried out by telephone or through another means that does not involve face-to-face meetings? We think there are several options. A sales representative could tell a consumer the information in the fund summary. We think that consumers who make their own investment decisions without further advice from sales representatives will already have done their homework and won't need anything further.

d. What about consumers investing on a periodic basis (monthly, quarterly, annual debits for example)—what are their information needs? We do not think consumers need to receive a fund summary before each periodic purchase, for example. Won't consumers be kept informed about their fund through access to continuous disclosure?

e. These documents will be filed with regulators. Should they be reviewed and receipted?

Issues for comment

06. Please give us feedback on the practical issues we outline in the text box above. Please explain how marketing brochures or other sales communications are distributed and kept up-to-date today, both at the operator and sales representative levels.

07. Please tell us about your business practices now using the existing disclosure documents. Do you use them in the sales process? Do you give them to consumers before a sale is completed? If we require you to give a printed fund summary to consumers before the sale, what impact will this have on your existing business practices? What about telling consumers what the fund summary says rather than always giving them a printed copy? Can we achieve our objectives of empowering consumers to make informed investment decisions without mandating a fund summary?

08. Please give us your views on the proposed content of the fund summary document.

09. What are the pros and cons of a fund summary document that includes information on more than one fund? Why is a consolidated document desirable, having regard to the potential for consolidated documents becoming unwieldy?

The consumers' guide

We believe some consumers will benefit from access to a standardized consumers' guide that describes the important features of both segregated funds and mutual funds. Furthermore, we believe that industry participants have a responsibility to educate consumers about their investments, particularly those consumers who identify themselves as novice or less sophisticated consumers. When industry participants recommend segregated funds and mutual funds to novice consumers, we believe those consumers should receive more than verbal advice and fund-specific information. For this reason, we propose that industry participants offer novice consumers a consumers' guide that explains segregated funds and mutual funds before the purchase decision is made.

We envision a joint regulatory-industry document. It will be updated at regular intervals and will be available electronically to industry participants and consumers. Industry participants using it will not be permitted to alter it. As a joint regulatory-industry document, it will not be a "liability" document, that is, industry participants using it (whether fund operators or dealers) will not be accountable for its contents.

We propose that sales representatives will offer the consumers' guide to novice consumers at an early stage in the sales process. Today, sales representatives ask consumers about their investment knowledge so they can understand their needs and recommend investments. We would like to build on this process. At account opening, sales representatives will offer the consumers' guide to novice consumers (particularly those who have not invested in mutual funds or segregated funds before) so they can better understand subsequent investment recommendations. Sales representatives will take these consumers through the consumers' guide in a meaningful way to aid in their understanding.

After we published our 1999 Recommendations,[20] OSC and FSCO staff convened a committee of representatives from both the mutual fund and segregated fund industries to prepare a draft consumers' guide. The draft consumers' guide that appears as Appendix 1 to this paper is substantially based on the draft we received from that joint industry group. This document is drafted with our current disclosure regimes in mind. It will need to be amended to include any changes that arise from this initiative.

[20] *Supra* note 2.

Practical issues raised by the consumers' guide

Although the concept of a standardized consumers' guide is an important one, we recognize that our proposals raise several practical issues:

a. We need to agree on an approval mechanism whereby the regulators will approve and the industry will endorse the contents of the consumers' guide. We need to work out how this document would be periodically updated.

b. How will the consumers' guide be made available for use by industry participants and consumers?

c. Who will make the decision about which consumers should be offered the document? The consumer? The dealer firm? The sales representative? What consequences will flow when a novice consumer is not offered the document?

Issues for comment

10. Please provide us with feedback on the practical questions we note in the text box above.

11. Please comment on the content of the draft consumers' guide in Appendix 1.

Consumers' rights

Rights in the case of a misrepresentation

Our proposals will continue to give consumers the rights they have today in respect of misrepresentations in the disclosure record viewed together (foundation document, continuous disclosure record, fund summary document, and any disclosure required because of material or fundamental changes to the fund). As today, the entire package of disclosure must give consumers the required full, true and plain disclosure of all material facts about the fund (brief and plain disclosure in the case of segregated funds). Mutual fund investors will have the rights of rescission or damages given to them under securities legislation.

The rights of withdrawal and rescission

We recommend that the withdrawal and rescission rights (other than for misrepresentations) attached to mutual fund purchases be eliminated under our proposed system. As we explained earlier in this paper, the rights are part of a complex mechanism that has grown up around the delivery after-the-fact disclosure regime for mutual funds. If information on a mutual fund is widely available before the point of sale, we believe the existing rights of withdrawal and rescission serve no real purpose. We believe investors will not be prejudiced by the removal of these rights and the industry will benefit from the added certainty this will bring.

Do consumers need a cooling-off period?

Some international regulators, most notably the U.K. and Australia, give consumers a cooling–off period after they make a decision to purchase certain managed funds. Consumer protection legislation generally gives consumers a cooling-off period when they are exposed to high-pressure sales or are entering into contracts for future benefits in exchange for significant future financial exposure. Consumers are given a 10-15 day window to re-consider their purchases without any sales pressure. Today's mutual fund right of rescission is not intended to give mutual fund investors a free put right, but allows investors to decide whether they really wish to invest in the particular fund.

Issues for comment

12. Please comment on cooling-off periods in the context of mutual fund and segregated fund sales. If you believe one should be retained (or introduced in the case of segregated fund sales) please explain why. How should a cooling-off period work given the changes in the market value of funds? How can we prevent market players from using a cooling-off period to play the markets? What would be a correct period for consumers to re-consider their investment?

The costs versus the benefits of our proposals

We will prepare a cost-benefit analysis of our proposals once we review your feedback on this consultation paper and further develop them based on your input. We expect to significantly reduce costs to industry participants by eliminating the requirement to deliver printed documents. We may, however, introduce new costs because the industry will need to revise its existing disclosure documents, change the way they manage their web-sites and introduce new fund summary documents. We understand that we need to weigh the costs of our proposals against the benefits, both qualitative and quantitative, we see accruing to fund consumers and industry participants. We will only proceed with our proposals if we are able to identify a net benefit.

Issues for comment

13. Although we will be preparing a formal cost-benefit analysis, we are interested in your views on the costs versus the benefits of our proposals. Please comment and explain your analysis.

Our next steps

Comments are due by April 30, 2003

As we explained earlier, we will accept your comments until April 30, 2003. If you have any questions about our proposals, you may contact the co-chairs of our staff working group:

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We will complete our research and review your comments

We will carefully review your comments as we receive them. We will analyse your comments along with the information we receive from the consumer research study we described earlier in this paper. Once we have done that and completed any additional consultation we think is necessary, including focus groups on mock-ups of our proposed disclosure documents, we will proceed to draft changes to our regulation. We expect to recommend changes to provincial securities and insurance legislation, since changes are necessary to fully implement our proposals.

We will publish draft rules for comment

We expect to release for comment draft rules or regulations and policy statements setting out our proposals for a new point of sale disclosure system. We also expect to release for comment draft legislation that reflects our proposals before we recommend changes to our provincial legislation. We will set out the form and content requirements of each of the documents that make up our proposed system. We expect to prepare mock-ups of our proposed disclosure documents so consumers and industry alike can better visualize and understand what we propose.

Appendix 1

Note to reader: This guide is written based on the laws that applied to mutual funds and segregated funds as of April 2002.

Guide to
Mutual Funds and Segregated Funds

[date to be inserted]

What this guide does

This guide explains key aspects of mutual funds and segregated funds, two important investment options for many people. The guide offers general information to investors, but it does not replace the **prospectus** of a mutual fund or the **information folder** of a segregated fund. You will still need to read these documents carefully and consult your mutual fund salesperson or life insurance representative before you make your investment decision.

1. What are mutual funds and segregated funds?

Pooled investments of many

Mutual funds and segregated funds are types of investments. When you invest in one of these funds, your money is pooled with that of other investors. You and the other investors share in the fund's earnings, losses, and expenses. These funds spread your money among several investments (diversification) and provide professional management, regardless of how much money you have to invest. Generally, you can cash-in (redeem) your investment at any time.

Stocks, bonds, cash

Mutual funds and segregated funds invest in securities such as stocks, bonds, and cash. Exactly what they invest in depends on their objectives and the strategies used to achieve their objectives. For example, there are funds for people who want their investment to provide them with a steady income and funds for those who want their investment to increase in value for when they redeem. There are funds that invest in shares from a particular sector, such as the biotechnology industry, and others that invest in specific geographical regions, such as Asia or Latin America.

Value changes daily

Prices of securities change every day, reflecting changes in interest rates, economic conditions, and market and company news. So, the value of your investment in a fund also goes up and down—it may be worth more or less when you sell it, compared to when you bought it.

2. What are the important features of mutual funds and segregated funds?

Mutual funds

Mutual funds are created and marketed by mutual fund management companies. They may be legally set-up as trusts that sell units, or corporations that sell shares, to investors.

As an investor, you have a proportional interest in the value of your mutual fund's assets minus its liabilities. The value of your mutual fund will vary up or down depending on the value of the fund's assets and expenses. You have a right to vote on important changes in the management, fees, and objectives of your mutual fund.

Segregated funds

Segregated funds are created and marketed by life insurance companies. They are referred to as segregated funds because their assets are kept separate from the insurance company's other assets. When you invest in a segregated fund, you are actually buying a life insurance contract, which is known legally as an individual variable insurance contract (IVIC).

Your contract entitles you to choose a specific segregated fund. The value of your contract will vary up or down depending on the value of the fund's assets and its liabilities. The insurance company you buy your contract from will guarantee a minimum value for your investment on the contract's maturity date(s), which will be at least 10 years from the date you invest, or on the date of your death (guaranteed death benefit), whichever comes first. You must hold your investment until your contract's maturity date(s) to take advantage of the guarantee. If you redeem your investment before the maturity date, the guarantee will not apply and you will receive the current value of your investment in the segregated fund. You must be told about important changes to the management, the management fees, and objectives of your chosen segregated fund. Some of these changes give you the right to choose another fund or, in certain circumstances, redeem your investment in a fund without charge. Your guaranteed death benefit will be paid directly to the beneficiary you choose, without probate fees and in some cases, your investment will be protected from your creditors.

3. What types of funds are there?

Four basic types:

- *growth*
- *income*

There are many types of fund categories, which are useful for comparing funds, but there are four basic kinds of funds. These are classified according to their investment objectives:

- *balanced*
- *money market*

- **Growth funds** invest mainly in securities that have the potential to grow in value—producing capital gains.
- **Income funds** invest mainly in securities that pay interest or dividend income while still protecting investors' capital.
- **Balanced funds** invest in a mix of growth and income securities that provide a blend of capital gains and income while still protecting investors' capital.
- **Money market funds** are often an alternative to cash. They invest in short-term debt securities to provide a steady income.

4. What are the risks of investing?

Risk of loss

Whenever you invest your money, you are putting it at risk. The risk that comes along with investing in a fund depends on what the fund invests in and its investment strategies.

Although segregated funds guarantee a minimum value on their maturity date, or upon your death, they don't protect you against market losses if you redeem before then. Read the information folder for details of the guarantee.

Investigate before you invest

You should select funds based on how much risk you are comfortable with and how well it matches your investment goals. The prospectus and the information folder explain the risks of investing in a fund. Consider all the risks before you invest.

5. How do I learn about a fund?

Specific information

You learn about a mutual fund from its **prospectus** and you learn about a segregated fund from its **information folder**. These documents explain your investments and their risks, describe the companies who manage and administer the funds, and explain your legal rights. Ask for and review these documents before you invest. Learn about the securities the fund holds, its investment goals and strategies, its management style, the risks of investing, its sales fees, any guarantees it offers, and the fees you will pay directly and those the fund pays on your behalf.

The websites of mutual fund companies and insurance companies often have information about your investment. You can also read various mutual fund documents including prospectuses, annual information forms, and fund financial statements on the website of the regulators' electronic filing system known as SEDAR (www.sedar.com). You can ask for these to be mailed to you free of charge by contacting the mutual fund company.

General information

There are many sources of general information on investing in funds. Talk to your financial advisor or sales representative, visit your local library or industry websites such as:

- www.ific.ca
- www.clhia.ca

The government regulators of funds also offer information about investing:

- www.csa-acvm.ca
- www.ccir-ccrra.org

Self-regulating organizations, which are organized for the purpose of regulating the operations and the standards of practice and business conduct of their members, also have useful information:

- www.ida.ca
- www.mfda.ca

Many newspapers, magazines, books, and websites offer information and advice about mutual fund and segregated funds. Be careful about relying only on that advice when you decide to invest.

6. How do I invest in a fund?

From sales people or companies

You can buy mutual funds from a registered mutual fund salesperson and directly from some mutual fund companies. You can buy segregated funds from licensed life insurance representatives and some insurance companies. Many salespeople are licensed to sell both mutual funds and segregated funds. You can also invest in these funds through discount brokers or at a variety of other financial institutions. Funds can be bought in person, by phone, by fax, or on-line.

Both registered mutual fund salespeople and licensed life insurance representatives can help you choose the funds that best match your investment goals and the risk tolerance.

Application forms

When you make your first purchase of a mutual fund or segregated fund, you will be asked to fill out one or more application forms. These may include a new account application for the dealer your salesperson works with and application forms from the mutual fund management company (for mutual funds) or life insurance company (for segregated funds). The information required will generally include personal information, information about your financial situation, information about your investment goals, the type of account (registered or non-registered), and your fund selections. When you purchase a segregated fund, you will also be asked to specify your beneficiaries and guarantees.

7. If I invest in a fund, what information do I get?

Key documents

Prospectus and information folder

The mutual fund prospectus and the segregated fund information folder give you important information about your fund. The mutual fund prospectus must be mailed to you within two business days of the date you first invest in a fund—but remember that you are entitled to ask for it before you make your investment decision. The segregated fund information folder must be given to you before you invest in a fund.

Segregated fund contract

This important document sets out your rights to guarantees and other benefits, and the terms of the relationship between you and the insurance company. You will receive the contract from the insurance company at the time you invest or shortly afterwards.

Confirmation

You will generally receive a confirmation when you first invest in a fund. You may also receive additional confirmations when you make further investments. Check that any confirmations accurately state details including the fund, the sales fee option, any fees you paid, and the amount you bought.

Account statements

You will receive annual account statements giving you information on your investments. You may also receive account statements more frequently . Read them carefully and keep them for your tax records.

Financial statements of the fund

You will receive annual financial statements describing a fund’s size, income, fees and expenses over the previous five years, and listing the fund's investments. Semi-annual statements are also available upon request.

Other material

You can often get more information if you ask for it. For example, segregated funds prepare detailed investment policies and mutual funds prepare annual information forms with detailed information about the mutual fund management company.

8. What will it cost to own a fund?

When you invest in a mutual fund or segregated fund, you pay fees to cover the costs of management, sales, marketing, accounting, and administration. For segregated funds, you also pay for insurance features such as the guaranteed minimum value on maturity and the guaranteed death benefit. The information folder and prospectus explain these costs and whether you pay them directly or if they are deducted from the fund.

Three types of fees

The three types of fees are:

- management fees and administrative expenses
- sales charges
- special fees

Management fees and administrative expenses

Management Expense Ratio (MER)

The Management Expense Ratio (MER) represents the total cost of managing the fund. The MER is expressed as a percentage of the fund's total value and it includes administrative expenses and portfolio management costs, legal and accounting fees, the cost of sending reports to investors and the cost of sales and marketing. For segregated funds, it normally includes the cost of the insurance features. You should know that the fees and expenses associated with managing the fund are charged directly to the fund and they will reduce the return on your investment.

Sales charges

Types of sales charges

Additional costs of sales and marketing—which includes compensation for your mutual fund sales person or life insurance agent—may be charged to you directly. You can often choose the type of sales charge you pay. The two most common types of sales charge are:

- **Front load fees,** which are deducted from the amount you invest and are paid to the mutual fund dealer or insurance agent. You may be able to negotiate these fees with your sales representative.
- **Deferred sales charges** (also known as **back-end loads** or **redemption fees**), which are deducted from the amount you receive if you cash in before a certain time, usually six years. These fees decline each year during that time. These fees go to the mutual fund management company or insurance company that paid the sales charges to your dealer for your purchase at the time of your original investment. Some mutual fund management companies and life insurance companies allow you to cash in up to 10% of your investment each year during this period without paying these fees.

No load funds

Some funds have neither front load fees nor deferred sales charges. These funds are called **no load funds**. With no load funds, as with other funds, sales and marketing costs are included in the fund's MER, but you are not charged directly for any additional sales costs.

A note on adviser compensation

Mutual fund sales persons or life insurance representatives are paid commissions based on your investment, or receive a salary, or receive a combination of a salary and commission. Their compensation can vary based on the amount of your investment, the product you select, and the sales charge you select—but they will be compensated regardless of the kind of sales charge attached to the fund. Mutual fund management companies and insurance companies may also pay sales incentives, including trailing commissions (which are paid periodically and based on the value of your account) to people who sell their funds.

Other fees

Other fees

You may have to pay other fees, directly, or by deductions from your account. They can include:

- annual trustee fees for registered savings plans (RSP), registered retirement income funds or registered education savings plans
- one-time account set-up fees
- short-term trading fees on amounts you cash-out within 90 days of when you invest in the funds
- transfer fees for switching among funds managed by the same mutual fund management company or insurance company
- processing fees for transactions such as closing an account or wiring money to a bank account
- advisory fees, and
- account management fees and special reporting fees

9. How can I measure the value of my investment?

Unit value NAV

Multiply the unit value times the number of units you own

A mutual fund or segregated fund's unit value is described as the net asset value per unit (NAV). The NAV is the value of the assets in the fund, less fees, expenses and taxes, divided by the number of units in the fund. It is calculated at the close of each trading day using that day's prices. The value of your investment is the NAV times the number of units you own.

Change in NAV

Fund performance is measured by the change in NAV over time

Fund performance is measured by the change in NAV over a set time, whether a day, three months, or a year. Many newspapers and websites publish mutual fund and segregated fund NAVs daily. They also publish monthly tables showing fund performance over different times.

Published returns

Mutual fund companies and life insurance companies also publish performance information in their prospectus or information folder, and in advertisements, brochures, posters, reports to investors, and financial statements.

The performance of your investment probably won't match the numbers you see in newspapers or websites. That's because the published returns don't include any direct fees you pay (they include fees and expenses included in the MER), and usually don't cover the same time period that you have owned the fund.

Some companies now calculate your personal rate of return and show it in your account statements.

General tax overview

10. How will my investment in a fund be taxed?

This section gives only an overview of general principles and alerts you to certain tax issues related to your investment. You will find more detailed tax information in the prospectus and information folder. Consult your sales representative, life insurance agent, the mutual fund or life insurance company, Canada Customs and Revenue Agency, or a tax adviser if you have questions.

Tax rate varies

Funds may produce interest, dividends, and capital gains, which are all taxed at different rates.

Taxable earnings

Mutual funds distribute earnings to you periodically. They typically distribute these earnings to you by issuing you more units, but you can ask for your earnings in cash. Segregated funds do not normally distribute earnings, but rather allocate them to you by increasing your unit values.

Registered accounts

Earnings are taxable the year you receive them unless your fund is in a registered account like an RSP. RSP earnings accumulate tax-free until you withdraw them, at which point they are taxable as income. The prospectus and information folder will tell you whether or not a fund can be included in a registered account.

Non-registered account

If your fund is in a non-registered account, the tax treatment of earnings depends on the type of income earned and how often the fund distributes or allocates it. The date you invest, compared with the date a fund distributes or allocates earnings, may have important tax consequences.

Capital gains

If you receive a guaranteed minimum value from a segregated fund that is higher than the current market value, part of the difference is generally taxed as a capital gain.

A portion of the money you receive when you redeem your fund will be taxed as a capital gain or loss, depending on whether the market value of the investment has gone up or down since you bought it. You may also create a capital gain or loss when you transfer your investment from one fund to another fund managed by the same fund manager or insurance company.

11. Do I have any protection against losing my money?

No deposit insurance

The money you put in a fund is not a deposit, and is not covered by deposit insurance.

No protection from drops in market value

You have no protection from declines in the market value of your mutual fund or segregated fund (other than the protection offered by your IVIC).

Bankruptcy

If a life insurance company goes bankrupt, your segregated fund investment is protected because its assets are separate from the insurance company's other assets.

If a mutual fund management company goes bankrupt, your right to the assets of the fund is not affected because the fund's assets are not owned by the management company and a custodian holds the assets on your behalf.

Compensation plans

There are industry compensation plans that help investors if a mutual fund dealer or an insurance company that sells segregated funds go bankrupt. You should note that these plans do not protect you from a decline in the market value of your mutual fund or segregated fund.

The plans are:

Segregated funds

CompCorp

The Canadian Life and Health Insurance Compensation Corporation (CompCorp) protects the guaranteed minimum value of the segregated funds, subject to certain limits. Contact CompCorp for details of coverage.

The Canadian Life and Health Insurance Compensation Corporation
Consumer Assistance Centre
Canadian Life and Health Insurance Association Inc.
1 Queen St. East Suite 1700
Toronto Ontario M5C 2X9
Phone: 1-800-268-8099 (English); 1-800-361-8070 (French);
416-777-2344 (in Toronto)
Website: www.compcorp.ca

Mutual funds bought through an investment dealer

CIPF

The Canadian Investor Protection Fund (CIPF) protects customers against losses if an investment dealer becomes insolvent or unable to return securities and related cash which it holds in its name for you, subject to certain limits. Contact CIPF for details of coverage.

The Canadian Investor Protection Fund
PO Box 192, 200 Bay Street
Toronto Ontario M5J 2J4
Phone: 416-866-8366
Fax: 416-360-8441
Website: www.cipf.ca

Provincial compensation plans

Mutual funds bought through a mutual fund dealer

Several provinces require mutual fund dealers to participate in a compensation plan. For example, the Ontario Contingency Trust Fund protects customers from losses that result from the insolvency of a mutual fund dealer, subject to certain limits.

12. Can I change my mind about a purchase?

Mutual Funds

Two business days to withdraw

In most provinces and territories, you can cancel your first purchase of a specific mutual fund by giving written notice to your dealer within two business days of receiving the prospectus. This is called the *right of withdrawal*. You get back the full purchase price plus any fees you paid.

48 hours to rescind

In most provinces and territories, you can also cancel mutual fund purchases of less than $50,000 by giving written notice to your dealer within 48 hours of when you receive written confirmation of your purchase. This is called the *right of rescission*. You get back the lower of what you paid and your investment's value calculated when you cancel. You will also get back any fees you paid.

Segregated Funds

Information received before investment

You must receive a copy of the information folder before you sign a purchase application. This is to ensure that you have received all the information you need before making an informed purchasing decision. There is no right of withdrawal or rescission for segregated funds, so read the information folder carefully and ask any questions before you sign.

Redeeming mutual funds and segregated funds

Selling your investment

If you change your mind, you can sell your investment at any time. The price you receive is the net asset value per unit calculated after you place your order to sell. That may be more or less than you paid. You may have to pay sales fees and there may be tax implications.

13. What can I do if I have a problem with a fund?

Keep records

Keep a written record of all your actions (with the time, date, names and titles of people you speak with, cheques and letters you write, and contracts you sign).

CFSON

You can contact the Centre for the Financial Services OmbudsNetwork (CFSON) [insert contact information] for information about consumer assistance and referrals if you have problems with your fund or any of the companies that manage the fund or that sold you your fund.

Mutual funds

Contact salesperson or mutual fund manager

- Try to solve the problem with your mutual fund salesperson or his/her supervisor. If that doesn't work, contact the compliance officer at the head office of the mutual fund dealer.
- If you have a problem with your mutual fund or the mutual fund manager, contact the mutual fund manager's compliance officer.

Trade association or self-regulating organization

- If the firm belongs to the Mutual Fund Dealers Association of Canada (phone 416-943-5827) or the Investment Dealers Association of Canada (IDA), (phone 416-364-6133), they will investigate. They can enforce rules and regulations among their members. The IDA also has an arbitration program for disputes.
- The Ombudsman for Banking Services and Investments provides consumer assistance for clients of banks, members of the IDA, the MFDA and the Investment Funds Institute of Canada and most federally regulated trust and loan companies. You can contact them at [insert contact information].

Provincial Securities Commissions

If you still can't solve the problem, contact your provincial securities commission. It will investigate to see if any securities laws have been broken. Securities commissions can penalize firms and individuals for breaking the law but cannot help you get your money back. You may wish to consult a lawyer on what to do. The Canadian Securities Administrators (www.csa-acvm.ca) has contact information for provincial securities commissions.

Segregated funds

Contact salesperson

- Try to solve the problem with your life insurance representative. If that doesn't work, contact the compliance officer of the insurance company. Describe the problem clearly and concisely.

Trade association

- You can also contact the CLHIA Consumer Assistance Centre (1-800-268-8099; 416-777-2344 in Toronto). This industry-funded help line will answer your questions and help solve disputes. It may write the president of the insurance company about your situation. You can also contact the Canadian Life and Health Insurance OmbudService (at the same number) for assistance.

Provincial Insurance Regulator

If you still can't solve the problem, contact your provincial insurance regulator. Insurance regulators don't mediate disputes, but they can investigate and discipline firms and individuals that break provincial laws for segregated funds. Ontario has an insurance ombudsman. You may wish to consult a lawyer on what to do. You can get contact information for your provincial insurance regulator from the Canadian Council of Insurance Regulators (www.ccir-crra.org).

Comparing mutual funds and segregated funds

	Mutual funds	Segregated funds
What it is	A pool of investments managed for investors by professional money managers.	A pool of investments managed for investors by professional money managers.
What I own	Units of a trust or shares of a corporation. A proportional interest in the fund's assets, earnings, losses and expenses. A right to vote on important changes in the management, fees, and objectives of the fund, before they happen.	A type of insurance contract known as an individual variable insurance contract. A right to participate in the fund's earnings, losses and expenses. A right to know about important changes in the management, fees and objectives of the fund, before they happen and the right to exit from the fund without redemption charges when they occur. The guaranteed minimum value is paid directly to your beneficiary without probate fees upon your death. Your investment may be protected from your creditors if you become insolvent.
Guarantees	Not normally, but some funds offer limited guarantees.	A guaranteed minimum value for the policy on its maturity date.
Changing my mind about buying	Right to withdraw within two days of receiving the prospectus. Right to rescind within 48 hours of receiving a written confirmation of purchase. Right to redeem at any time.	No right to withdraw or rescind once you sign the purchase application. It is important that you review the information folder before signing. Right to redeem at any time.
Important documents	▪ Prospectus ▪ Annual Information Form ▪ Account Statements ▪ Financial Statements	▪ Information folder ▪ Insurance Contract ▪ Account Statements ▪ Financial Statements

Roles and Responsibilities

Life insurance companies

- create segregated funds and issue individual variable insurance contracts
- ensure the accuracy and completeness of the information folder and any promotional materials
- instruct and supervise their employees or licensed **life insurance agents** who sell the contracts
- invest the assets of the segregated fund based on the Canadian Life and Health Insurance Association (CLHIA) Guidelines on Individual Variable Insurance Contracts and the investment objectives and policies of the specific fund (or delegate this function to an **investment manager**)
- protect the assets of the segregated fund or delegate this role to a **custodian**
- organize, manage and operate the segregated fund and administer your individual variable insurance contract
- select parties to manage delegated functions and ensure the functions are properly carried out
- make good on the guarantees in the contract

Mutual fund management companies

- create mutual funds
- ensure the accuracy and completeness of the contents of the prospectus and any promotional materials
- distribute mutual fund units or shares through registered employees or **dealers** that are licensed to sell mutual funds
- invest the assets of the mutual fund based on securities regulations and the investment objectives and policies of the specific fund (or delegate this function to another **investment manager**)
- engage a qualified **custodian** to hold the assets of the mutual fund
- organize, manage and operate the mutual fund and administer your account
- select parties to manage delegated functions and ensure the functions are properly carried out

Agents

- deliver an information folder to you before they sell you an individual variable insurance contract and explain the contract consistently with the information folder

Registered dealers

- give you a copy of the prospectus within 48 hours of your purchase
- instruct and supervise their **sales representatives** who sell mutual funds

Sales representatives

- explain the mutual fund consistently with the prospectus

Appendix 2

Disclosure Matrix:
An Illustration

Mutual funds presently prepare a simplified prospectus and an annual information form (as well as continuous disclosure documents). National Instrument 81-101 Mutual Fund Prospectus Disclosure prescribes the forms for both documents. Segregated funds presently prepare an information folder (as well as continuous disclosure documents). The CLHIA Guidelines prescribes the form for the information folder.

The following two tables illustrate where each item of disclosure currently contained in the current disclosure documents *might* fit into the new disclosure system described in our consultation paper.

The tables are intended as a preliminary illustration to give readers a better feel for the contents of the disclosure documents we propose. If we decide to move forward with our proposals following the comment period, we will analyse the disclosure items for these documents in greater detail.

Mutual Funds:

Current disclosure item	Foundation document	Financial statements	Statement of fund performance	Fund summary document	Consumers' guide	Status to be determined
SP Part A Item 1- Front cover disclosure						✓
SP Part A – Item 2 Table of contents	✓					
SP Part A – Item 3 Introductory Disclosure				✓	✓	
SP Part A – Item 4 – General Investment Risks					✓	

Current disclosure item	Foundation document	Financial statements	Statement of fund performance	Fund summary document	Consumers' guide	Status to be determined
SP Part A – Item 5 Organization and Management Details	✓			✓		
SP Part A – Item 6 Purchases, Switches and Redemptions	✓					
SP Part A – Item 7 Optional Services	✓					
SP Part A – Item 8 Fees and Expenses	✓ (8.1)				✓ (8.2)	
SP Part A – Item 9 Dealer Compensation	✓ (9.1)		✓ (9.2)			
SP Part A – Item 10 – Income Tax Considerations	✓				✓	
SP Part A – Item 11 Statement of Rights	✓				✓	
SP Part A – Item 12 – Additional Information	✓					
SP Part A – Item 13 – Part B Introduction						✓
SP Part A – Item 14 – Back Cover					✓	✓
SP Part B – Item 1 General						✓
SP Part B – Item 2 Introductory						✓
SP Part B – Item 3 – General Information						✓

Current disclosure item	Foundation document	Financial statements	Statement of fund performance	Fund summary document	Consumers' guide	Status to be determined
SP Part B – Item 4 – Organization and Management Details	✓			✓		
SP Part B – Item 5 Fund Details	✓			✓		
SP Part B – Item 6 – Fundamental Investment Objectives	✓			✓		
SP Part B – Item 7 – Investment Strategies	✓			✓		
SP Part B – Item 8 – Top Ten Holdings			✓			
SP Part B – Item 9 - Risks	✓		✓ (ss 6)	✓	✓	
SP Part B – Item 10 Suitability	✓			✓		
SP Part B – Item 11 – Past Performance			✓	✓		
SP Part B – Item 12 – Distribution Policy	✓					
SP Part B – Item 13 Financial Highlights			✓	✓		
SP Part B – Item 14 – Additional Information	✓					
AIF – Item 1 Front Cover Disclosure						✓
AIF – Item 2 Table of Contents	✓					

Current disclosure item	Foundation document	Financial statements	Statement of fund performance	Fund summary document	Consumers' guide	Status to be determined
AIF – Item 3 Name, Formation and History of the Mutual Fund	✓					
AIF – Item 4 Investment Restrictions	✓ (2) ✓ (4)				✓ (1,3)	✓ (5,6)
AIF – Item 5 Description of Securities	✓				✓	
AIF – Item 6 – Valuation of Portfolio Securities	✓ (1)		✓ (2)			
AIF – Item 7 – Calculation of NAV	✓					
AIF – Item 8 – Purchases and Switches	✓					
AIF – Item 9 – Redemption of Securities	✓					
AIF – Item 10 – Responsibility for Mutual Fund Operations	✓					✓ (non static information)
AIF – Item 11 – Conflicts of Interest	✓					✓ (non static information)
AIF – Item 12 – Fund Governance	✓					
AIF – Item 13 – Fees and Expenses	✓					
AIF – Item 14 – Income Tax Considerations	✓					

Current disclosure item	Foundation document	Financial statements	Statement of fund performance	Fund summary document	Consumers' guide	Status to be determined
AIF – Item 15 – Remuneration of Directors, Officers and Trustees	✓					✓ (non static information)
AIF – Item 17 – Legal and Administrative Proceedings	✓					✓ (non static information)
AIF – Item 18 – Other Material Information	✓					
AIF – Items 19, 20, 21 , 22 Certificates						✓ (how and where)
AIF – Item 23 Exemptions and Approvals						✓
Item 24 – Back Cover						✓

Segregated Funds (IVICS):

Current disclosure item	Foundation document	Financial statements	Statement of fund performance	Fund summary document	Consumers' guide	Status to be determined
Form1 Part A Item 1 description of IVIC	✓			✓		
Form1 Part A Item 2 value of units	✓		✓			
Form1 Part A Item 3 continuous marketing	✓					
Part B Item 4 description of the insurer	✓			✓		
Part B Item 5 custody of securities	✓					
Part B Item 6 policies with respect to investments	✓			✓		
Part B Item 7 tax status of the seg..fund	✓					
Part B Item 8 tax status of the contract holders	✓					

Current disclosure item	Foundation document	Financial statements	Statement of fund performance	Fund summary document	Consumers' guide	Status to be determined
Part B Item 9 segregated fund manager and advisor	✓					
Part B Item 10 interest of management and others in material transactions	✓					
Part C Item 11 management fees and incentives	✓					
Part C Item 12 other fees and charges	✓					
Part D Item 13 investments in mortgages, real estate derivatives	✓					
Part D Item 14 material facts	✓					
Part D Item 15 other material facts	✓					
Part E financial statements Item 16 statement of operations		✓				
Part E Item 17 statement of changes in net assets		✓				

Current disclosure item	Foundation document	Financial statements	Statement of fund performance	Fund summary document	Consumers' guide	Status to be determined
Part E Item 18 statement of net assets		✓				
Part E Item 19 statement of investment portfolio		✓				
Part E Item 20 notes to the audited financial statements		✓				
Part E Item 21 financial highlights			✓	✓		
Part E Item 22 auditor	✓					