DISCLOSURE OF FEES AND CHARGES IN MANAGED INVESTMENTS

Review of Current Australian Requirements and Options for Reform

Report to the Australian Securities and Investments Commission

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Executive Summary

Introduction

This report has been prepared at the request of ASIC as part of its ongoing commitment to ensure that the objectives of the Financial Services Reform Act 2001 ("**FSRA**") are achieved. The report focuses upon one aspect of disclosure – disclosure of fees and charges in Product Disclosure Statements ("**PDSs**") and member or investor periodic statements. As requested by ASIC, the report reviews current Australian disclosure requirements as well as international disclosure requirements, and proposes a number of options for improved disclosure.

As part of this project, 17 meetings were held with key stakeholders to discuss disclosure of fees and charges in PDSs and investor statements. The stakeholders included industry bodies, financial product issuers and consumer associations.

Disclosure Principles and Statistics on Managed Funds

Part 2 of the report provides an overview of the FSRA disclosure principles. These principles, as identified by ASIC in Policy Statement 168, are that disclosure should be timely, relevant and complete; promote product understanding; promote comparison of products; highlight important information; and have regard to consumers' needs. Part 2 also provides a description of typical fees and charges that relate to financial products. It also provides statistics on managed funds – both for Australia and internationally. As at 31 December 2001, total consolidated assets of managed funds institutions in Australia were $654.4 billion. Of this total amount, consolidated assets of superannuation funds stood at $303.4 billion; life insurance offices had consolidated assets of $176.6 billion; public unit trusts $130.9 billion and cash management trusts $30.1 billion. Growth of managed funds in Australia has been dramatic. Between June 1998 and December 2001, the consolidated assets of managed funds grew from $453.9 billion to $654.4 billion, an increase of 44 per cent.

Problems With Disclosure of Fees and Charges

Part 3 of the report identifies problems with disclosure of fees and charges. It is divided into two sections. The first section presents the results of surveys of the adequacy of disclosure of fees and charges in prospectuses. As part of this project, 30 prospectuses relating to various types of superannuation and managed funds were reviewed in order to obtain insight into the adequacy of disclosure of fees and charges. All prospectuses are recent and all have been issued by well-known product issuers. The following general comments can be made in relation to these prospectuses:

- There is significant variation with respect to the degree to which fees and charges are disclosed. This is evident not just in relation to a comparison of prospectuses for superannuation and prospectuses for managed funds, but also in relation to a comparison of prospectuses for the same products. For example, in some prospectuses, there is identification of fees and charges at a broad level. In other prospectuses, considerably more detail is provided concerning specific types of fees.
- There is significant variation with respect to how the same fee is described in different prospectuses. The use of different terminology to describe identical fees detracts from the ability to compare prospectuses.
- In some prospectuses, fees and charges are referred to but not defined.
- There is significant variation in relation to what the management expense ratio/ongoing management charge represents and how it is calculated.
- In some prospectuses, not all relevant fees are disclosed in the fees section of the prospectus which means that a potential investor must review all of the prospectus to see what fees apply.
- Many prospectuses do not disclose how much notice is required to investors in relation to an increase in fees and charges.
- There is significant variation in relation to whether prospectuses disclose the maximum fees or charges that can be levied under the trust deed.
- There is significant variation in relation to disclosure of the purpose for which fees are imposed.

The second section of Part 3 is a summary of the results of surveys which have been undertaken in the last few years with the objective of testing investors' understanding of fees and charges in prospectuses and other selling documents. These surveys have found that substantial numbers of investors fail to understand the fees that are disclosed in prospectuses. For many investors, the results show that it is difficult to understand the fee structure and it is not easy for them to work out exactly how much an investment will cost. For example, in one survey of 500 people who had invested in managed investments, 61 per cent agreed with the statement that "it is difficult to understand the fee structures". Another finding of this survey is that approximately one-third of those participating in the survey were unable to define the types of fees and charges they are paying in relation to their investment.

The review of prospectuses undertaken for this project and the results of the surveys of investors' understanding of fees and charges indicate considerable scope for improvement of the disclosure of fees and charges.

The Law Governing Disclosure of Fees and Charges in Australia

Part 4 of the report provides an analysis of the law governing disclosure of fees and charges in Australia. It highlights the important changes that have been made under the FSRA and focuses upon the enhanced disclosure requirements for superannuation.

International Review of Laws Governing Disclosure of Fees and Charges

Part 5 of the report provides a detailed review of the regulatory framework for disclosure of fees and charges in managed investments in the United Kingdom, New Zealand, Canada and the USA. This Part includes extracts from the fees sections of actual prospectuses in these countries in order to facilitate comparison with the Australian requirements. Part 5 also includes discussion of a recent development in a number of other countries – the implementation of fee calculators on the websites of regulators. This is an important initiative and in Part 6 of the report a recommendation is made for ASIC to consider the introduction of a fee calculator on its website.

Options For Improved Disclosure

Part 6 of the report identifies options for improved disclosure of fees and charges. It is divided into three sections:

- options for improved disclosure in PDSs;
- options for improved disclosure in periodic member statements; and
- options for implementation and the role of ASIC and industry.

Options for Improved Disclosure in PDSs

I make the following recommendations regarding improved disclosure of fees in PDSs.

Standardised descriptions and definitions of fees

- All relevant fees are to be referred to in the fees section of the PDS (this does not always occur currently).
- Even if a fee which is commonly imposed is not imposed in relation to a particular financial product, the fact that this fee is not imposed should be disclosed in the fees section of the PDS (this has the advantage of enhancing comparability of PDSs and eliminates the need on the part of a potential investor to search the entire PDS to identify whether a fee is imposed).
- The purpose of any fee which is imposed should be disclosed in the fees section of the PDS.
- To the maximum extent possible, there should be standardised descriptions and definitions of fees.
- A standardised fees table across all PDSs for financial products should be introduced which would identify significant fees (such as entry, exit, switching and investment management fees). Such a table could include the following (although the reference to establishment fee may need to be removed for non-superannuation products):

Type of Fee	**Amount (state Nil if not applicable)**
Establishment fee Contribution fee Administration fee Investment management fee Switching fee Withdrawal fee	

To what extent should fees be broken down?

I do not believe it is practical to disclose in a PDS a single global figure which contains all fees. As explained in more detail in Part 6, some fees are discretionary in the sense that some investors may pay them while others may not. In these circumstances, to include such discretionary fees in a single global figure can be misleading.

Neither do I believe it appropriate for every single fee which is paid to be disclosed in a PDS. A number of fees which are paid are very small and it would be unusual for these fees to impact upon the investment decision of a potential investor. However, I see merit in disclosing separately fees for administration and fees for investment management. This is for several reasons. First, they are different functions. Second, the separate disclosure of both administration and investment fees enables investors to compare how efficient each of these aspects is across a variety of financial products. Third, it is typically the case that investment management fees are the largest ongoing fees. It is important that the fee which is most directly related to the performance of the fund be separately disclosed. Finally, the distinction between administration and investment has become more important with the growth of master funds and IDPSs.

Entry/contribution fees and exit/withdrawal fees

Currently, there is a lack of consistent terminology for these fees across financial products. I therefore make the following recommendations:

- There is merit in having common terminology across both superannuation and managed funds products to enhance comparability.
- It may be, for the reasons outlined in Part 6, that the term contribution fee is more accurate than entry fee and that the term withdrawal fee is more accurate than exit fee. Consideration should be given to whether there can be uniform terminology across all products.
- If any of these fees are not applicable, this should be clearly stated as part of the fee disclosure table recommended above.
- The purpose of these fees should be disclosed in the fees section of the PDS.

Capacity to increase fees/maximum fees

I recommend that the capacity to increase fees and the maximum fees applicable be disclosed in the fees section of the PDS. Given that fees can typically be increased (and perhaps substantially) without the approval of investors it is important that investors be aware of this capacity to increase fees. It becomes even more important if a particular financial product has significant exit/withdrawal fees. If the capacity to increase fees and the maximum amount to which they can be increased is not disclosed, then an investor can be severely disadvantaged if fees are increased and an investor who wishes to withdraw is then subject to a high exit fee.

Ongoing management charge(OMC)/management expense ratio (MER)

These two ratios are designed as a measure of ongoing management expenses or charges in superannuation (OMC) and managed funds (MER). I make several recommendations for improved disclosure concerning the ratios:

- Comparability across superannuation and managed funds is reduced because different terminology for the two ratios is used and there is also a difference in the calculation of the two ratios (in particular, the MER excludes expenses that would have been incurred by a direct investor such as brokerage, stamp duty and costs in maintaining a property investment, while these expenses are included in the calculation of the OMC). I see merit in having the same terminology used across both superannuation and managed funds. Because both the ratios reflect ongoing management charges, the use of the term OMC would seem to be more accurate than MER. Consideration should be given to whether the terminology OMC can be used across all products.
- The fact that the two ratios are calculated differently but have as their objective measuring ongoing management charges detracts from the ability to compare products. I see merit in the Investment and Financial Services Association (which has published Standard No 4.00 for the calculation of the MER for its members) being invited to consider amending this Standard so that expenses which would be incurred by a direct investor are included in the MER. This

would align the MER with the OMC. It has the advantage of making the MER a more comprehensive ratio of ongoing charges. It also makes the MER a more straightforward and clearly explained ratio as it is not necessary to explain that it excludes expenses that would have been incurred by a direct investor.

- I see merit in having a standardised description of the OMC/MER for all financial products. My review of disclosure documents reveals a wide variation in the way these ratios are currently described. This is not helpful for investors. I suggest the following may be a useful starting point as a possible precedent which could be discussed with industry participants:

> The Management Expense Ratio/Ongoing Management Charge is a measure of the ongoing expenses associated with your investment. It is expressed as a percentage of the total assets of the fund (excluding liabilities). It includes:
>
> - **The ongoing investment management fee** – this is the annual fee the fund pays to [……] to manage your investment. In 2002 this fee was [……%] – see page [……]; and
> - **Other fees and expenses paid from the fund** – this includes certain administration costs associated with managing your investment such as the cost of maintaining the registry of members; printing costs of product disclosure statements, annual reports and member statements; the cost of producing cheques; postage expenses; fees charged by the fund's auditor and fees paid to custodians who hold the assets of the fund.
>
> The MER/OMC excludes entry/contribution fees, exit/withdrawal fees and switching fees.

- I also see merit in requiring a statement in all PDSs that past fees should not be taken as an indication of future fees. Currently, this statement is required only for superannuation products.
- The new requirements for superannuation require the OMC to be converted to a dollar amount for an account balance of $10,000. I see merit in having this type of disclosure for managed funds and note that a major product producer has recently done this in relation to one of the first PDSs for managed funds produced under the FSRA. This PDS shows the dollar effect of the MER by applying it to an account balance of $10,000 for each of the 15 investment options to which the PDS relates. I recommend that ASIC facilitate industry discussion with a view to determining whether industry is prepared to include this type of disclosure in PDSs for managed funds.

Showing the effect of fees on returns

An important issue is whether the effect of fees on returns should be disclosed in PDSs. Currently, this is not required for either superannuation or managed funds.

The key stakeholders consulted as part of this review expressed a broad range of views on this issue. On the one hand, the view was expressed that this is essential information for investors. The contrary view is that while it may be useful in theory, because of the assumptions required, which may prove to be inaccurate, the information cannot be rendered useful. The types of assumptions that need to be made are:

- the likely future returns;
- the likely future fees; and
- the likely future contributions by the investor.

Despite these difficulties, I note that some major countries require this type of disclosure. In particular, as noted in the international survey in Part 5 of the report, the United Kingdom, the United States and Canada require this type of disclosure for certain of their financial products. There are reasons why showing the effect of fees on returns can be useful. First, an increase in fees can reduce substantially future returns. For example, a 1 per cent increase in a fund's annual fees and charges can reduce an investor's final account balance in that fund by 18 per cent after 20 years.

A second reason why disclosure of the effect of fees on returns is important for investors is that some investment choices require this sort of information. For example, it is increasingly popular to offer investors different fee choices in relation to the same financial products. For example, a particular financial product may offer investors two choices concerning fees – (i) a nil entry fee with a higher OMC option or (ii) an entry fee with a lower OMC option. The investor cannot tell which is the preferred option without having some insight into the effect of the different fee options on returns.

I therefore see merit in ASIC facilitating industry discussion about disclosure of the effect of fees on returns subject to:

- a specified rate of return being set for industry participants; and
- appropriate disclosure about the assumptions which have been made.

I note that the Australian Consumers' Association has recently put forward for discussion a fee table relating to superannuation which discloses the effect of fees on returns. Ageing Agendas, in its report to the Australian Superannuation Funds of Australia ("**ASFA**"), has also recommended the use of a table showing the effect of fees on returns for superannuation products. In addition, Colin Grenfell, an actuary, has proposed a series of tables showing the effect of expenses on returns for superannuation products. I see merit in ASIC facilitating industry discussion about the merits of a table, which would show the effect of fees on returns, being included in PDSs relating to all superannuation products. This information could also be disclosed on a fee calculator on the ASIC website.

Disclosure in dollars versus disclosure in percentages

I recommend that ASIC facilitate industry discussion about achieving, to the maximum extent possible, disclosure of fees and charges expressed in dollars and not only in percentages. There is strong evidence that investors better understand and feel more comfortable with disclosure which is in dollars rather than percentages.

Disclosure of fees paid to advisers

I recommend that the fees section of PDSs contain disclosure of fees paid to advisers – both upon an initial investment and on an ongoing basis. I note that a number of PDSs already contain this type of disclosure. However, others do not and there is considerable variation in the quality of disclosure. I also recommend that the source for the payment of these fees to advisers be stated in PDSs. In the case of the ongoing trail, this will be the investment management fee. In the case of the initial investment, this will typically be the entry/contribution fee.

There is also the question about disclosure of "soft commissions" ie, other payments made to advisers which may include things such as bonuses for having clients invest specified amounts in certain financial products. Where these exist, I recommend that

the PDS draws attention to the fact that arrangements may exist between the fund manager and financial advisers. Because of the variety of these arrangements and the fact that a fund manager may have different arrangements with financial advisers, it may be that only a general statement concerning the existence of such arrangements can be made in the PDS together with a statement that the investor should refer to the Financial Services Guide and Statement of Advice received from the adviser for specific details of these arrangements.

The buy/sell spread

A matter of confusion in disclosure documents is the so-called buy/sell spread. There is considerable variation in disclosure documents concerning this and, based upon consultations with key stakeholders conducted as part of this project, I am advised that it is a continuing source of concern for investors.

I see scope for improved disclosure in PDSs concerning the buy/sell spread and propose in Part 6 what I see as a useful precedent which could be discussed with industry so that there is a standardised description of the buy/sell spread.

Disclosure of ability to negotiate rebates with advisers

My review of current disclosure documents reveals a variety of practices concerning the extent to which they discuss the ability of investors to negotiate rebates with advisers. I see merit in having more standardised disclosure in this area. It is appropriate to have some statement to the effect that, where applicable, it is the adviser who determines the amount of the entry/contribution fee paid.

Options for improved disclosure in periodic member statements

Disclosure of fees and charges in periodic member statements varies to an extraordinary degree. Some periodic member statements make no disclosure to investors about fees and charges. This is unfortunate because it is this document which provides the opportunity for an investor to ascertain precisely what fees and charges have been paid in relation to their investment. This cannot be done in a PDS where there is a limit to the information that can be tailored to individual circumstances.

I view this situation with the utmost concern. I also note there is international interest in improving disclosure of fees and charges in periodic member statements.

I see considerable scope for improved disclosure of fees and charges in periodic member statements. I recommend that where actual fees relating to a member's investment can be calculated, then these fees should be disclosed in the statement. I was advised during the course of the consultations conducted as part of this project that for some funds the calculation of such fees might prove to be very costly in terms of the need to change computer systems. I recognise that these costs would be borne by investors. I therefore recommend that ASIC obtain information from industry about the costs of providing this disclosure. This would allow a cost/benefit analysis to be undertaken. I note in Part 6 of the report that the United States General Accounting Office has calculated that the cost of providing improved disclosure of fees and charges in investor annual statements would be less than $1 per investor per year. It would be important to ascertain what the costs of improved disclosure would be in the Australian context.

However, even if the costs of providing precise disclosure are significant, such is the importance of improving disclosure of fees in periodic member statements, that I make a further recommendation. I recommend that ASIC facilitate discussions with industry about recent proposals of the United States Securities and Exchange Commission and the United States General Accounting Office which are designed to deal with this situation. One proposal is to multiply the fund's per share (unit) asset value by the fund's expense ratio, multiply the result by the average number of shares (units) an investor owned during the period, and show the result in the investor's statement.

The second (and less costly) proposal to provide improved information about actual fees is to require member periodic statements to contain information about the dollar amount of fees that were paid during the relevant period for preset investment amounts. Periodic member statements would be required to include a table showing the cost in dollars incurred by an investor who invested a standardised amount (eg $10,000) in the fund, paid the fund's actual expenses, and earned the fund's actual return for the period. The Securities and Exchange Commission proposes there could be an additional table which would include the cost in dollars, based on the fund's actual expenses, of a

standardised investment amount (eg $10,000) that earned a standardised return (eg 5%). Because the only variable for this calculation would be the level of expenses, investors could easily compare funds to one another.

Options for implementation and the role of ASIC and industry

I see an important role for ASIC and industry in ensuring there is improved disclosure of fees and charges in both PDSs and periodic member statements. Many of the recommendations made above to improve disclosure of fees and charges involve ASIC facilitating industry discussion.

I also make three further recommendations. These are:

- Consumer testing of the recommendations contained in this report.
- The possible introduction of a fee calculator on the ASIC website. I note that a number of regulators in other countries have made fee calculators available on their websites. I see significant merit in ASIC having a similar fee calculator and suggest this would contribute significantly to ASIC's educative mandate. Part 5 of the report provides detailed discussion of the fee calculators made available on the websites of the United States Securities and Exchange Commission and the Ontario Securities Commission and the Comparative Tables made available on the website of the United Kingdom Financial Services Authority. These provide useful precedents although I suggest in Part 6 that the fee calculator provided by the Ontario Securities Commission has a number of advantages.
- Facilitation of industry discussion concerning disclosure of information concerning fees and charges to trustees. I note the recent publication of the UK Pension Fund Disclosure Code. The objective of the Code is transparency in order to assist pension fund trustees' understanding of the fees and charges levied on pension fund assets for which they have responsibility. The background to the Code is a concern that a lack of comprehensive, clear and standardised disclosure has not allowed trustees and their advisers to monitor and compare all costs incurred during the management of fund assets. Because:

- a number of the key issues raised in the Code are similar to those which lie at the heart of this project; and
- improved disclosure of fees and charges to trustees has the potential to improve disclosure to retail investors;

I raise for the consideration of trustee and other industry bodies the desirability or otherwise of industry adopting a Code which would be similar to the UK Pension Fund Disclosure Code.

Part 2

Introduction

INTRODUCTION

This report has been prepared at the request of ASIC as part of its ongoing commitment to ensure that the objectives of the Financial Services Reform Act 2001 ("**FSRA**") are achieved. In November 2001, ASIC released Policy Statement 168, *Disclosure: Product Disclosure Statements (and Other Disclosure Obligations)*. It is stated in this Policy Statement that ASIC would be undertaking further work to achieve the objectives set out in the Statement – those objectives including comparability of fees and returns for investment products. It is stated in PS 168.39 that ASIC anticipates that this further work would include:

- undertaking research projects; and
- undertaking further consultation with industry and consumer representatives about the best way to achieve the disclosure objectives and related outcomes (for example, detailed policy guidance or development of effective industry standards).

As noted below, extensive consultations with key stakeholders were undertaken as part of the preparation of this report. I thank those organisations and individuals who participated in the consultation process.

This report focuses upon one aspect of disclosure under the FSRA – disclosure of fees and charges. The focus of the report is upon disclosure of fees and charges in product disclosure statements ("**PDSs**") and member or investor periodic statements. The report does not examine disclosure of fees and charges in Financial Services Guides and Statements of Advice. This accords with the initial emphasis of ASIC on disclosure in PDSs as outlined in PS 168. The consultation meetings with stakeholders discussed not only PDSs but also ongoing disclosure to investors. This ongoing disclosure is typically through quarterly, six-monthly or yearly member statements or investor statements.

These statements will be the means by which investors are informed of their actual investment. It may be where they are also informed about the actual fees and charges that have been paid. Yet many of the stakeholders consulted were of the opinion that these statements could be improved in relation to disclosure of fees and charges. Consequently, this report makes recommendations in relation to both PDSs and investor statements.

Part 2 of the report contains the following sections:

- acknowledgments
- overview of the FSRA disclosure principles;
- overview of the consultation process forming part of this project;
- statistics on managed funds; and
- description of typical fees and charges that relate to financial products.

ACKNOWLEDGMENTS

The expert assistance of several people in the preparation of this report is gratefully acknowledged. Joel Vernon, Senior Research Associate, Centre for Corporate Law and Securities Regulation, played an important role by preparing drafts of Parts 4 and 5 of the report. Angela Longo of ASIC arranged and attended all of the consultation meetings with key stakeholders, assisted in obtaining research materials, liaised on behalf of ASIC with international regulators, and was the key liaison person at ASIC in relation to the project. Justin Sam of ASIC attended all of the consultation meetings with key stakeholders and drafted notes of the consultation meetings.

FSRA DISCLOSURE PRINCIPLES

The Collective Investments Scheme Principles which have been promulgated by the International Organisation of Securities Commissions require full, accurate and timely disclosure to investors in order for them to make informed investment decisions. The disclosure must be clear, comprehensible, consistent and not misleading.[1]

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[1] Technical Committee of the International Organisation of Securities Commissions, *Principles for the Supervision of Operators of Collective Investment Schemes*, September 1997, para 8.1.

The FSRA has, as one of its core objectives, providing such disclosure to investors across a range of financial products. Paragraph 14.28 of the Explanatory Memorandum to the Financial Services Reform Bill 2001 states that:

> The broad objective of point of sale obligations is to provide consumers with sufficient information to make informed decisions in relation to the acquisition of financial products, including the ability to compare a range of products.

In PS 168 ASIC outlines six Good Disclosure Principles which it encourages financial product issuers to consider when preparing a PDS. The Good Disclosure Principles are:

- disclosure should be timely;
- disclosure should be relevant and complete;
- disclosure should promote product understanding;
- disclosure should promote comparison;
- disclosure should highlight important information; and
- disclosure should have regard to consumers' needs.

ASIC states that an example of a disclosure issue that may benefit from clarification, particularly if greater comparability of products is to be achieved, is standardised descriptions of like fees and charges (such as commissions), including the basis for showing the future impact of fees and charges [PS 168.30].

Under the heading "Disclosure Should Promote Product Understanding" in PS 168, ASIC provides the following information:

> **Disclosing fees, charges and returns**
>
> **[PS 168.58]** We believe that the need for clear, concise and effective disclosure is most relevant in relation to the disclosure of fees and charges and, in the case of investment-based products, the disclosure of returns. Information about fees, charges and investment returns is a key consideration for consumers when making decisions about financial products, and research shows that it is often the most difficult information for consumers to understand.
>
> **[PS 168.59]** The types of product information that a consumer should be able to easily understand and compare include:

(a) what the fees and charges are (eg fees expressed in dollar amounts may be better understood by consumers), who the fees are paid to, what the fees are paid for, and how fees impact on returns;

(b) whether fees are variable and, if so, how and when they vary, including through negotiation or the impact of rebates or discounts (eg group life rebates);

(c) how returns are calculated and whether they are shown on a consistent basis…

(d) typical and material factors that may affect returns, including risks.

[PS 168.60] If information about fees, charges and returns is not clear, concise and effective, comparability of products is harder to achieve. This has been recognised in the regulations in relation to superannuation and RSA products by the imposition of more detailed PDS requirements: see reg 7.9.11.

[PS 168.61] Issuers of products other than superannuation and RSA products are not prevented from following any of the more detailed relevant PDS requirements for superannuation and RSA products set out in the regulations (see [PS 168.60] above) in order to improve consistency of disclosure. For example, see the more detailed requirements dealing with disclosure of fees and returns in items 5-8 of Schedule 10B in the regulations.

Under the heading "Disclosure Should Promote Product Comparison" in PS 168, ASIC states that:

[PS 168.62] We believe the clarity and effectiveness of PDS disclosure is also improved by being drafted in a way that makes it easier for consumers to make comparisons…about options that may be available to them under the terms of a particular financial product. For example, where a consumer has the option to pay fees in two different ways, a comparison might be given to show the relative charges made for each option after various durations (eg 1, 3, 5 and 10 years).

The regulations to the FSRA which ASIC refers to in PS 168, and which require detailed disclosure of fees and charges for superannuation and RSA products, are outlined in Part 4 of this report.

The issues which ASIC identifies in this extract from PS 168 are further discussed in Part 6 of this report where a number of options for reform are identified.

THE CONSULTATION PROCESS

As noted above, in PS 168 ASIC states that it intends to undertake further consultation with industry and consumer representatives about the best way to ensure that the Good Disclosure Principles are being implemented.

As part of this project, 17 meetings were held with key stakeholders to discuss disclosure of fees and charges in PDSs and investor statements. The stakeholders included industry bodies, financial product producers and consumer associations. Those attending each of the meetings were Professor Ian Ramsay, and, from ASIC, Angela Longo and Justin Sam. Some of the meetings were also attended by other ASIC officers.

The organisations and individuals who were consulted were:

- Australian Consumers Association (ACA)
- Australian Institute of Superannuation Trustees (AIST)
- AMP
- Australian Retirement Fund (ARF)
- Australian Shareholders Association (ASA)
- Australian Superannuation Funds of Australia (ASFA)
- AXA
- BT
- Corporate Super Association (CSA)
- Financial Planning Association (FPA)
- Colin Grenfell – actuary and director of ASFA
- Institute of Actuaries Australia (IAA)
- Investment and Financial Services Association (IFSA)
- MLC
- Sealcorp
- Van Eyk Research
- Westpac

STATISTICS ON MANAGED FUNDS

In order to place the discussion of fees and charges in context, it is important to have insight into the significance of the managed funds industry. Managed funds have grown

substantially in Australia in recent years, both in terms of number and in terms of assets under management. Table 1 is extracted from the Australian Bureau of Statistics publication *Managed Funds – December Quarter 2001* (No 5655.0). As at 31 December 2001, total consolidated assets of managed funds institutions were $654.4 billion. Of this total amount, consolidated assets of superannuation funds stood at $303.4 billion; life insurance offices had consolidated assets of $176.6 billion; public unit trusts $130.9 billion and cash management trusts $30.1 billion.[2] Figure 2.1 graphs the data contained in Table 1.

Further evidence of the growth in consolidated assets of managed funds is provided in Table 2 which is also extracted from the same Australian Bureau of Statistics publication. It can be seen that between June 1998 and December 2001, the consolidated assets of managed funds grew from $453.9 billion to $654.4 billion, an increase of 44 per cent.

In terms of the type of asset held by the managed funds, Table 2 indicates that of the $654.4 billion in total assets, the largest three categories as at December 2001 were equities and units in trusts ($237.7 billion); assets overseas ($126.7 billion); and land and buildings ($68 billion). Figure 2.2 graphs the data contained in Table 2.

How do these statistics for Australian managed funds compare to other countries? Table 3 provides some statistics on the characteristics of US and European major mutual fund markets. As at December 1997, total assets of mutual funds in the United States were US$4.465 trillion while at the same time, total assets in European mutual funds totalled US$1.36 trillion. By 1999 total assets of US mutual funds reached US$6.8 trillion.

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[2] Some other sources identify more assets in superannuation funds. For example, in its recent report on superannuation, the Productivity Commission states that as of June 2001, there was $527 billion in assets in superannuation funds: Productivity Commission, *Review of the Superannuation Industry (Supervision) Act 1993 and Certain Other Superannuation Legislation*, Report No 18, December 2001, p xvi and chapter 2. A reason for the difference is the method of classification employed. In the Australian Bureau of Statistics managed funds data, superannuation funds held in the statutory funds of life insurance offices are classified under the life insurance offices category and not the superannuation funds category. In addition, the Australian Bureau of Statistics excludes investments by superannuation funds in public unit trusts from the assets of superannuation funds in its consolidated presentation.

In the United States, ownership of stock, bond and money market mutual funds rose from 6 per cent of US households in 1980 to 45 per cent in 1999. Over the same period, total assets held by US mutual funds increased by 5,000 per cent, rising from US$135 billion to US$6.8 trillion. Between 1980 and 1999, the number of US mutual funds increased by nearly 1,300 per cent, from 564 to 7,791.[3]

TABLE 1

Consolidated Assets of Australian Managed Funds

Consolidated Assets (a)	**Dec Qtr 2000 $m**	**Dec Qtr 2001 $m**
Superannuation funds	294,186	303,353
Life insurance offices (b)	170,873	176,579
Other managed funds	155,045	174,487
Total	**620,104**	**654,420**

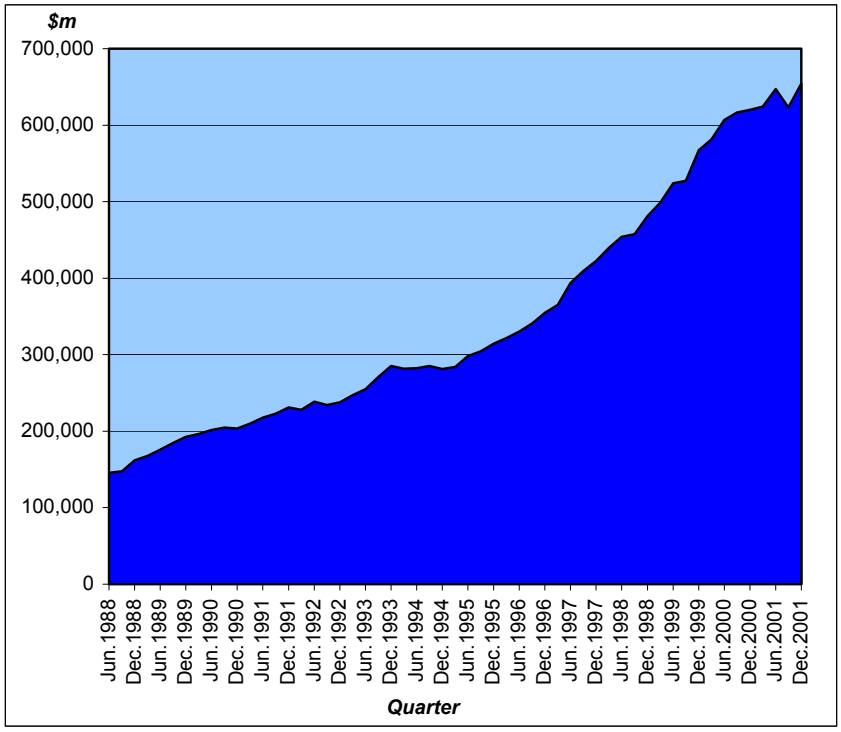
(a) Estimates of the consolidated assets of managed funds are derived by eliminating any cross-investments that take place between the various types of funds. For example, investments by superannuation funds in public unit trusts are excluded from assets of superannuation funds in a consolidated presentation.

(b) Investments by superannuation funds which are held and administered by life insurance offices are included under life insurance offices.

Source: Australian Bureau of Statistics, *Managed Funds - December Quarter 2001* (No. 5655.0).

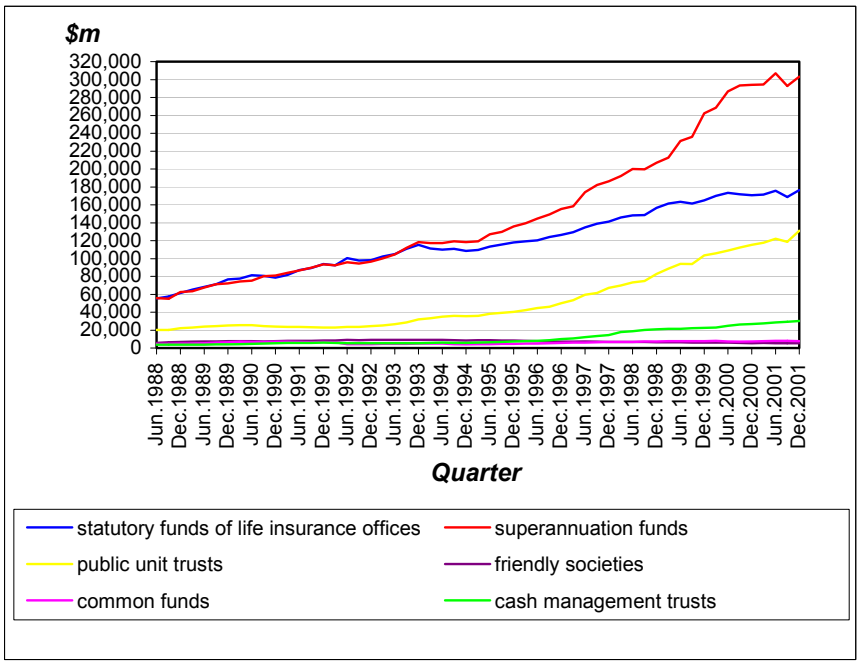
[3] The statistics in this paragraph are extracted from G Alexander, J Jones and P Nigro, "Does Mutual Fund Disclosure at Banks Matter? Evidence from a Survey of Investors" (2001) 41 *Quarterly Review of Economics and Finance* 387 at 388.

FIGURE 2.1: TOTAL CONSOLIDATED ASSETS OF MANAGED FUNDS



**Source: Derived from Australian Bureau of Statistics, Managed Funds - December Quarter 2001* (No. 5655.0)

FIGURE 2.2: CONSOLIDATED ASSETS OF MANAGED FUNDS BY INSTITUTION



**Source: Derived from Australian Bureau of Statistics, Managed Funds - December Quarter 2001* (No. 5655.0)

TABLE 2

AUSTRALIAN MANAGED FUNDS

CONSOLIDATED ASSETS

Institution/asset	Jun Qtr 1998 $m	Jun Qtr 1999 $m	Mar Qtr 2000 $m	Jun Qtr 2000 $m	Sep Qtr 2000 $m	Dec Qtr 2001 $m	Mar Qtr 2001 $m	June Qtr 2001 $m	Sep Qtr 2001 $m	Dec Qtr 2001 $m
Type of institution										
Life insurance offices(a)	148 170	163 384	170 152	173 522	171 755	170 873	171 495	175 789	168 763	176 579
Superannuation funds	199 969	231 205	268 450	286 673	293 344	294 186	294 355	306 957	292 739	303 353
Public unit trusts	73 435	93 968	106 018	108 750	112 360	115 432	117 564	121 953	118 698	130 939
Friendly societies	6 769	6 415	5 910	5 895	5 697	5 543	5 555	5 523	5 477	5 510
Common funds	6 845	7 568	7 940	7 434	7 058	7 242	7 734	8 126	8 138	7 897
Cash management trusts	18 676	21 531	22 794	24 776	26 102	26 828	27 490	28 693	29 138	30 141
Total	**453 865**	**524 070**	**581 264**	**607 050**	**616 315**	**620 104**	**624 193**	**647 041**	**622 952**	**654 420**
Type of asset										
Cash and deposits(b)	32 681	35 192	36 833	39 721	40 449	39 766	42 168	46 234	44 789	44 779
Loans and placements	24 025	27 714	31 661	32 390	31 902	28 883	28 968	30 484	28 229	28 387
Short term securities(b)	54 498	67 627	59 461	63 752	62 564	63 311	61 525	62 775	58 541	62 502
Long term securities	66 059	70 319	72 643	72 729	69 394	69 768	68 521	66 313	64 246	63 192
Equities and units in trusts	133 703	154 798	181 508	197 712	208 217	216 284	216 177	232 313	214 761	237 668
Land and buildings	47 867	56 708	62 875	64 258	64 527	64 336	65 970	67 053	65 843	68 018
Assets overseas	77 785	90 876	117 202	115 267	120 476	116 776	120 112	119 513	122 419	126 668
Other assets	17 248	20 837	19 081	21 221	18 787	20 980	20 752	22 356	24 124	23 207
Total	**453 865**	**524 070**	**581 264**	**607 050**	**616 315**	**620 104**	**624 193**	**647 041**	**622 952**	**654 420**

(a) Figures include superannuation funds held in the statutory funds of life insurance offices.
(b) Bank certificates of deposit held by public unit trusts are included in 'Cash and deposits' at banks.

Source: Australian Bureau of Statistics, *Managed Funds – December Quarter 2001* (No. 5655.0).

TABLE 3

CHARACTERISTICS OF UNITED STATES AND EUROPEAN MAJOR MUTUAL FUND MARKETS

DECEMBER 1997

	Total assets (US billion $)	**Number of Funds**	**Average Size** (US million $)	**Asset allocation (in %)** Equity	Bond	Balanced	Money	Others
United States	**4,465**	**6,900**	**647**	**53.0**	**19.5**	**2.8**	**24.1**	**0.6**
Europe	**1,360**	**10,269**	**226**	**31.8**	**30.4**	**11.3**	**25.7**	**0.8**
France	505	5,836	87	13.6	27.2	18.7	40.4	0.1
United Kingdom	237	1,455	163	85.8	6.1	7.6	0.5	0.0
Italy	210	626	337	20.4	44.0	6.3	25.0	4.3
Spain	179	1,456	123	10.5	40.9	11.1	37.5	0.0
German	148	717	207	37.9	48.2	2.8	11.1	0.0
Netherlands	78	179	440	53.8	30.2	5.7	10.1	0.2

This table presents the characteristics of the major European mutual fund markets and the United States. All figures are at 31 December 1997. The first column presents the total market value (billion US dollar), the second column the number of funds, the third column the average size (million US dollar) and the last five columns the asset allocation of all mutual funds.

Source: R Otten and M Schweitzer, *A Comparison Between the European and US Mutual Fund Industry*, Limburg Institute of Financial Economics, Maastricht University, Working Paper, December 1998.

Table 4 shows assets (in millions of US dollars) for open-end mutual funds for 37 countries, where data is available, as of September 30, 2001.

TABLE 4

Assets of Open-end Mutual Funds

September 2001

(in millions of US dollars)

Argentina	7,357
Australia	304,145
Austria	53,927
Belgium	64,449
Brazil	126,833
Canada	244,025
Chile	4,743
Costa Rica	1,428
Czech Republic	1,644
Denmark	30,462
Finland	12,131
France	700,944
Germany	192,617
Greece	21,885
Hong Kong	183,030
Hungary	2,202
India	13,490
Ireland[1]	166,979
Italy	352,415
Japan	465,962
Korea	137,056
Luxembourg	694,183

Mexico	27,608
New Zealand	6,796
Norway	13,861
Philippines	170
Poland	1,317
Portugal	15,840
Romania	11
Russia	249
South Africa	15,557
Spain	154,670
Sweden	56,157
Switzerland	72,556
Taiwan	43,641
United Kingdom	333,887
United States	6,414,505
Total[2]	$10,938,731

[1]**Figures are as of 8/31/2001.**
[2]**Figures may not sum to total due to rounding.**

Source: Investment Company Institute, *International Mutual Funds Survey*, *Third Quarter 2001*. The Institute notes that reporting coverage, periods covered and definitions are not consistent across countries.

DESCRIPTION OF FEES AND CHARGES

The following section is a description of the typical fees and charges applicable to financial products. It is extracted from Phillips Fox, *Financial Services Reform Act: Product Disclosure of Fees, Charges and Commissions*, Report Prepared for ASIC, November 2000, pp 10-15.

An analysis of the law governing the disclosure of fees and charges following the commencement of the FSRA is contained in Part 4 of this report.

DESCRIPTION OF FEES AND CHARGES

Fees and charges on investment products can be allocated to the following broad groups:

- Items related to investment management;
- Items related to financial advice;
- Items related to administration of the investment product;
- Items related to administration of the fund;
- Taxes and government charges.

A table showing the typical fees that apply to each product type is set out in the Appendix.

Definitions and Standard Terms

We have endeavoured to use standardised terminology and maintain a consistency in our fee disclosure across the breadth of financial products reported. This is a challenging task as the terminology used and the classifications of fees are various and often 'bundled'. For example the use of the term "administration charge" may or may not be inter-changeable with terms such as "ongoing management charge" or "MER" depending on the situation.

We have included a brief definition of the terms used and described the range of charging terminology that is used within the financial products industry.

Investment Management Charges

These charges are made to recover the costs of investment management.

<u>Investment Management Charges</u>

This charge is levied on the total assets under management in order to recover the costs of providing the investment management service. That is, this fee is the charge made by the investment manager for providing these services.

The rationale for charging in this manner is that many investment costs are crudely related to the funds under management (FUM). In practice, trading costs (brokerage and stamp duty) are minor compared to salaries and rent, so costs fall significantly as FUM increases. Accordingly, fees charged to master trusts, superannuation funds or Wrap accounts by wholesale managers are far lower than retail charges. This reflects the expectation of higher volumes of business.

Where the fee is disclosed, it is sometimes combined with other asset-based fees such as trail commission and asset-based administration charges. This makes it difficult to evaluate the actual cost of providing the investment service.

The investment fee charged is sometimes deducted from the calculation of the unit price and expressed as a lower earning rate. In these cases, it does not appear as an explicit charge. Many prospectus-based funds have undisclosed charges arising from this practice – typically between 0.2% to 0.9% or more of assets under management. Sometimes, the charges are hidden as details on the investment options are set out in a separate document.

Switching Charges

Charges are usually imposed for switching between investment portfolios within the product. Some companies vary the charge for each portfolio. The charge is usually expressed either as a percentage of the amount switched (to cover trading costs) or as a fixed dollar amount which is indexed to CPI annually (to cover administration costs).

Buy/Sell Margins

Many products have separate unit prices for purchases (buy price) and redemption (sell price). Buy/sell margins provide a spread between the quoted buy and sell unit prices. This is imposed to recover the notional trading costs (brokerage and stamp duty) of buying and selling the underlying assets of the fund whenever an investment transaction is made.

Contribution charges (see below) are sometimes recovered by widening the gap between buy and sell prices. The cost is then hidden in the unit price, rather than shown as an explicit fee.

Financial Advice

Almost all advisers are remunerated from commission paid by financial institutions. Even those advisers who charge fees usually keep the renewal commissions (also called trail or ongoing commissions).

Product fees need to be loaded to cover the costs of paying commission. It is common to set the fee at a level that will allow recovery of the full commission. If an adviser agrees with the investor to take a reduced commission, the fee may be reduced or the foregone commission could be rebated to the client.

Both initial and ongoing commissions can be flexible. Initial commission is expressed as a percentage of the deposit (normally up to 5%) of the deposit (establishment charge), or, more commonly, of all contributions received.
Ongoing commission is expressed *as a percentage of assets*, typically between 0.25% to 1.0% p.a.

Contribution Charges

In recent years, there has been a shift from contribution-based charges to asset-related charges. Prior to this, up-front charges (used to pay initial commission) on life policies were often disguised as a contribution charge for the term of the contract. On termination, the "outstanding payments" were deducted as a surrender penalty.

For most products, a significant portion (perhaps all) of a contribution charge is passed onto the intermediary. Many products now offer variable contribution charge facilities so that the intermediary can reduce the level of charges imposed when in competition with other products. The average charge is now about 2% of deposits, which is half the level of 5 years ago (though average deposits are also bigger).

Contribution charges are sometimes disguised by issuing a no-entry fee contract. This terminology is very misleading as there is an entry fee, but it is deducted differently. For example, a product with an entry fee of 5% of the deposit (contribution) might have an alternate fee structure for its no-entry fee product. This alternative could have an additional asset fee of 1.25% p.a. for the first four years, coupled with a termination fee to recover the residual establishment charge. Hence, termination after two years might attract a fee of 2.5% of the account balance.

Generally, no-entry fee products are dearer, which has the opposite effect to that implied by the terminology. They are dearer partly because the administrative cost of deducting the entry fee is increased when it is disguised as the combination of an additional asset fee and a termination fee.

Asset Commission

Most advisers take asset-based commissions as this provides a regular income stream. Not only does this help pay the fixed costs of running their business, it is also a tradeable asset. Other advisers will buy a portfolio of clients based on a multiple of the renewal commissions.

Adviser Service Fee

A number of institutions now allow an adviser to include an explicit fee for their services as negotiated between the adviser and the client. The administrator deducts this fee from the account and remits it to the adviser.

These charges were introduced to cater for fee-based advisers. However, the charges are made in addition to any other commissions taken by the adviser. Few funds that offer this facility place any upper limit on the adviser service fee that may be paid. To some extent this facility represents an open-ended adviser-driven commission scale.

Terminating Member Charge

Commission-related early termination charges and withdrawal charges are now rare for new products (other than as part of a disguised entry fee).

Administration Charges - Investments

These are deducted to cover the administration costs and reporting expenses of the product or fund.

Establishment Charges

These charges fall into two types, those that are imposed to cover payment to the adviser as described above and those that cover the administrative cost of setting up a contract such as an employer-sponsored superannuation fund. Most superannuation funds now absorb all these costs and market the facility as having no entry fees.

Member Fee

Most superannuation funds have a member fee, which is a fixed dollar amount deducted from investors' accounts to cover the maintenance of member records. Stand-alone contracts will also have a policy fee (life) or administration fee (unit trust).

Terminating Plan Charge

Charges imposed on plan termination are usually made to recover initial expenses (commission) not yet recovered. These are becoming less frequent.

However, it is becoming common for public-offer superannuation funds to charge fees where a fund is transferred to a new trustee. There are significant costs involved in liquidating assets and transferring member records. Some companies treat these transfers as benefit payments and then charge the fee that would then apply. This might only be $60 per member, but the total can be a sizeable amount on a large fund.

Trustee Fee

Most products (apart from life policies) still have a separate trustee fee even if the manager is the single responsible entity. This charge is usually expressed as a percentage of assets and amalgamated with any other asset-based fee.

Custodian Fee

Under the single responsible entity regime, an increasing number of financial institutions now use a custodial trustee for their products. These fees are usually asset-based (but are much lower than trustee fees).

Administration Charges - WRAP

A Wrap account or non-super master trust (or master fund) is a combined administration and investment service. There is a single set of fees covering administration, investment, advice and other services. It is not possible to separate the costs of any particular service and compare it against alternative products.

Most Wrap accounts have an asset-based administration fee to cover both administration and the adviser's income. These can be significant relative to fees on other products.

Administration Charges - Superannuation

Superannuation is complicated and there are a number of special charges related to compliance. For example, benefit payments must be accompanied by an Eligible Termination Payment (ETP) and it is usual to charge a fee of $20 to $70 for preparing these.

There are also special conditions (*member protection*) relating to fees on small accounts (under $1,000). This means that funds have cross-subsidies in their fee bases.

Stamp Duties and Taxes

Stamp duties are almost always absorbed as part of the general expenses of a fund or policy. Taxes are passed onto investors, usually equitably.

Superannuation tax is usually separated into components. The tax on deductible contributions is normally deducted from each member's account. Some companies deduct premiums and fees from each member's own contributions; others spread these costs amongst all accounts. The tax on investment income is usually deducted from earnings.

When deriving unit prices, capital gains taxes are calculated as if the asset were to be sold. A provision for the tax at that time is then made and the unit price is adjusted. This ensures that tax is paid over the period in which the asset is held, and is not transferred from one group of unit holders to the next.

Risk Products

Policy Fee

Most policies have a small annual fee to cover policy maintenance.

Premiums

The major cost is contained in the premium. This includes the cost of covering the risks, administering the policy, paying the adviser and profit margins. These items are not segregated.

Annuities

Term certain and lifetime annuities do not have an explicit fee since the expenses are effectively deducted before quoting the annual payment per dollar of purchase price. The investor cannot ascertain the components of the expenses.

Income Payment Charges

The income payment charge is applied to each income payment under an annuity and pension product. This is usually a small fee to cover administration of the policy payments. Again, the fee is not disclosed.

Other Charges

Fund Expenses

Unit trusts normally have provision to recover a range of expenses. These expenses are often listed without being quantified. Such items include audit costs and stamp duties.

Source for above "Description of Fees and Charges" is Phillips Fox, *Financial Services Reform Act: Product Disclosure of Fees, Charges and Commissions*, Report Prepared for ASIC, November 2000, pp 10-15.

APPENDIX

TABLE OF TYPICAL FEES FOR FINANCIAL PRODUCTS

FEE TYPE	Insurance Bonds	Unit Trusts	WRAP Accounts	Personal Super	Allocated Pensions	Employer Super (Retail)	Non-Profit Super Funds	Life Insurance *(charges not disclosed)*	
								Annuities	Risk
Asset Based									
Investment Management Charges	✓	✓	✓	✓	✓	✓	✓	X	X
Switching Charges	✓	✓	✓	✓	✓	✓	X	X	X
Buy / sell margins	✓	✓	✓	✓	✓	✓	X	X	X
Entry / Exit									
Contribution Charges	✓	✓	✓	✓	✓	✓	X	X	X
Terminating Member Charge	X	X	✓	✓	X	✓	✓	X	X
Establishment Charges	✓	✓	✓	✓	✓	✓	X	X	X
Member Fee	✓	✓	✓	✓	✓	✓	✓	X	X
Terminating Plan Charge	X	X	X	X	X	✓	✓	X	X
Early Withdrawal Charge	✓	✓	✓	✓	✓	✓	X	X	X
Financial Advice									
Adviser service fee	✓	✓	✓	✓	✓	✓	X	✓	✓
Asset Based Commission	✓	✓	✓	✓	✓	✓	X	✓	✓
Fund Expense									
Trustee Fee	X	✓	✓	✓	X	✓	✓	X	X
Custodian fee	X	✓	✓	✓	X	✓	✓	X	X
Policy fee	✓	X	X	✓	✓	✓	X	X	✓
Premium Loadings	X	X	X	X	X	✓	X	X	✓
Income payment Charges	X	X	X	X	X	X	X	✓	X

Note: (1) The Establishment fee is now usually expressed as a contribution charge
(2) Where a fee applies, it is ticked. However not all products in this category would have this charge.

Source: Phillips Fox, *Financial Services Reform Act: Product Disclosure of Fees, Charges and Commissions*, Report Prepared for ASIC, November 2000.

Part 3

Problems with Disclosure of Fees and Charges

INTRODUCTION

In this part of the report a number of problems with disclosure of fees and charges in Australian disclosure documents for financial products are examined. There is a widely held view that there is a need for improved disclosure of fees and charges. This was a common theme running through the meetings with key stakeholders although not all stakeholders agreed in relation to the degree of improvement needed and what should be done to improve disclosure. There is further discussion of the views of stakeholders in Part 6 of this report.

There is international interest in improving disclosure of fees and charges relating to financial products, as is evident with the recent publication of reports in the UK and USA, to name just two countries: Ron Sandler, *Medium and Long-Term Retail Savings in the UK: A Review*, Report Prepared for the UK Government, July 2002; United States Securities and Exchange Commission, *Report on Mutual Fund Fees and Expenses*, December 2000.

Part 3 of the report is divided into two sections. First, I present the results of two surveys of the adequacy of disclosure of fees and charges. Second, I summarise the results of a number of surveys which have tested consumers' understanding of fees and charges.

The analysis in Part 3 of the report is limited to initial disclosure documents such as prospectuses or product disclosure statements. However, as noted in Part 2, this project includes not only disclosure of fees and charges in selling documents but also disclosure in investor or member statements. Disclosure of fees and charges in these types of statements varies to an extraordinary degree. This type of variation is unfortunate because it is this document which provides an opportunity for an investor to ascertain precisely what fees and charges have been paid in relation to their investment. This cannot be done in a selling document where there is a limit to the

information that can be tailored to individual circumstances. In addition, it seems sensible to assume that investor statements may be more closely read than many selling documents. This can be for several reasons. First, the typical member statement is considerably shorter than the typical selling document. Second, it is the investor statement which gives details of the value of the investment and the investor therefore has a financial incentive to review the statement.

A review of investor statements reveals that on some of these statements, a precise dollar figure is given in relation to fees and charges for the period of time which the statement covers. In addition, there is a description of the fees and charges. These statements will provide a dollar value for the returns for the relevant period, then a dollar value for the fees and charges, and then a dollar value for the net returns.

This can be contrasted with those investor statements which provide no details concerning fees and charges. These statements may only provide a dollar value for the opening balance at the beginning of the period and a dollar value for the closing balance at the end of the relevant period, with no indication of the amount of fees and charges which have been paid. Although investor statements may be given quarterly, six monthly or yearly, once a year the investor will receive, along with the investor statement, an annual report. In this annual report, there can be expected to be reference to the Management Expense Ratio ("**MER**"). However, it is often the case that there is no reference on the investor statement to the fact that the MER is disclosed in the annual report and, in any event, the MER, as noted in Part 6 of this report, will typically be an imprecise measure of the actual fees and charges relevant to a particular investor.

SURVEYS OF ADEQUACY OF DISCLOSURE OF FEES AND CHARGES

This part of the report is divided into two sections. First, I summarise the results of a study undertaken in 2000 for ASIC of disclosure of fees and charges in prospectuses. Second, I present the results of a survey of prospectuses undertaken for the purposes of this project.

The most recent analysis of fees for superannuation products has been undertaken by Phillips Fox for IFSA and published in April 2002.[4] Although the main focus of the Phillips Fox report is on competition and fees, there is some brief discussion concerning disclosure of fees. The following is an extract from this section of the Phillips Fox report:[5]

> Our review of the annual reports of superannuation funds confirms that it is extremely difficult for any member to understand the fees charged to them. The range and quality of services varies significantly amongst the funds and it would not be easy for a member to evaluate these differences.

The authors of the report note that disclosure should improve under the Financial Services Reform Act in relation to superannuation products and that a competitive market can assist in forcing superannuation funds to minimise fees and charges and disclose fees and charges.

PHILLIPS FOX SURVEY

In November 2000 Phillips Fox presented a report to ASIC which dealt with disclosure of fees, charges and commissions.[6]

Phillips Fox reviewed a number of prospectuses relating to financial products including prospectuses for unit trusts, Wrap accounts and various types of superannuation products. An important point made in the report is the lack of uniform terminology in prospectuses:

> There is no standard for investment terms. This hinders any educational process as consumers have no familiarity with the terms used. Terminology can vary even within a disclosure document (as described in some of the examples later in this report). In addition, terms can be confusing. For example, an investment management fee could represent the fee charged by the fund manager for undertaking the management of the investments. It can also be the asset-based fee charged on the product, which can include the investment manager's fee, part

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[4] Phillips Fox, *Superannuation Fees and Competition*, Report Prepared for the Investment and Financial Services Association, April 2002.

[5] Ibid, section 3.1.

[6] Phillips Fox, *Financial Services Reform Act: Product Disclosure of Fees, Charges and Commissions*, Report Prepared for the Australian Securities and Investments Commission, November 2000.

> of the administration fee as well as ongoing commission to an adviser. The disclosure of this fee can vary. It might be deducted from the earnings rate or expressed as an explicit fee.[7]

Other points made in the report in relation specific prospectuses reviewed are as follows:

- The MER is not always explained sufficiently.
- It is not always clear when specific fees are payable.
- In one prospectus maximum fees for the fund are stated yet in the same prospectus it is disclosed that this maximum was exceeded but without any explanation.
- In one prospectus it is stated that a monthly investment of $100 will grow to a specified amount over five years. However, the calculation is accurate only if no fees or taxes are paid.
- It is not always made clear that entry fees or contribution fees are payable not just on the initial investment but may also be payable on subsequent investments.
- Some fees are shown as monthly and others as annually.
- The circumstances in which fees can be varied is not always disclosed.
- It is not always disclosed what fees are paid to advisers.

SURVEY OF PROSPECTUSES FOR THIS PROJECT[8]

For the purposes of this project, 30 prospectuses relating to various types of superannuation and managed funds were reviewed in order to obtain insight into the adequacy of disclosure of fees and charges. The prospectuses were selected at random. All prospectuses are recent (and current as of March 2002) and all have been issued by well-known product issuers.

Some general observations can initially be made concerning the overall quality of disclosure of fees and charges. This is followed by some specific observations. The following general comments can be made:

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[7] Ibid, section 2.4.3.

- There is significant variation with respect to the degree to which fees and charges are disclosed. This is evident not just in relation to a comparison of prospectuses for superannuation and prospectuses for managed funds, but also in relation to a comparison of prospectuses for the same products. For example, in some prospectuses, there is identification of fees and charges at a broad level. In other prospectuses, more detail is provided concerning specific types of fees.
- There is significant variation with respect to how the same fee is described in different prospectuses. The use of different terminology to describe identical fees detracts from the ability to compare prospectuses.
- In some prospectuses, fees and charges are referred to, but not defined.
- There is significant variation in relation to what the MER represents and how it is calculated.
- In some prospectuses, not all relevant fees are disclosed in the one section of the prospectus which means that a potential investor must review all of the prospectus to see what fees apply.
- Many prospectuses do not disclose how much notice is required to investors in relation to an increase in fees and charges.
- There is significant variation in relation to whether prospectuses disclose the maximum fees or charges that can be levied under the trust deed.
- There is significant variation in relation to disclosure of the purpose for which fees are imposed.

Apart from these general observations concerning disclosure of fees and charges, some specific examples of problems in particular prospectuses are worth identifying:

- In the fees and charges section of one prospectus it is stated that the ongoing management fee is a percentage of "total tangible assets". In the same section it is then stated that the custody and compliance fee is a percentage of the "total gross investments of the Fund". These terms, particularly the reference

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[8] The term "prospectus" is used rather than "Product Disclosure Statement" in this section of the report as the term Product Disclosure Statement applies only from March 2002, with the commencement of the Financial Services Reform Act 2001.

to total tangible assets, would be difficult for the typical investor to understand. Just as importantly, any difference between the two terms is not explained.

- Specific fees are referred to in prospectuses but are not defined or explained. For example, in one prospectus, a fee described as "a group asset transfer fee of up to 1% of the amount transferred to your account" is identified but not defined or explained. In another prospectus, there is reference to a "sector fee" which is not defined.
- In one prospectus there is reference to both ongoing management charges and management expense ratios which an investor may find confusing.
- In some prospectuses significant fees are not disclosed in the fees section but are disclosed in other parts of the prospectus. For example, in several prospectuses, switching fees are not mentioned in the fees section of the prospectus but are mentioned in other sections of the prospectus – such as the "Other information" section. In another prospectus, the maximum fees which can be charged under the trust deed are not disclosed in the fees section but in the section of the prospectus titled "What else do you need to know?"
- In some prospectuses, the actual management fee which has been paid in prior years is not disclosed in the section which deals with fees and charges. For example, in one prospectus, the actual management fee for the past two years is in the section titled "What else you need to know?" which is on page 19 of the prospectus, with the section on fees being on page 12 of the prospectus, with no cross-reference.

In summary, it can be seen that there is considerable scope for the improvement of disclosure of fees and charges in prospectuses. This conclusion is reinforced by an examination of surveys which have tested consumers' understanding of fees and charges.

SURVEYS TESTING CONSUMERS' UNDERSTANDING OF FEES AND CHARGES

A number of surveys have been undertaken in the last few years with the objective of testing consumers' understanding of fees and charges in prospectuses and other

selling documents for financial products. In this section of the report a summary of the results of these surveys is presented.

COMMUNICATIONS RESEARCH INSTITUTE STUDY

In March 1997 the Communications Research Institute of Australia presented its report on the accessibility of prospectuses which it had prepared for the Investment Funds Association and the Australian Securities Commission (as it then was).[9] The methodology employed was to engage in in-depth interviews with both experienced and inexperienced investors. There were 16 experienced investors and 16 inexperienced investors. Two different prospectuses for managed investment funds were selected for testing. They were selected to reflect differences in information and design in order to capture the range of differences across many managed funds prospectuses. One was a short prospectus of 40 pages offering only a few funds. The second prospectus was 72 pages offering many funds.

Those interviewed were asked to identify information in the prospectuses about particular items of information. One of these items was expenses (fees and charges). In relation to the first prospectus, 75% had some problem finding and understanding this section. Twenty-five per cent did not find or understand this section. In relation to the second prospectus, 38.5% had some problem finding or understanding this section. Fifty-four per cent did not find or understand this section.

EUREKA STUDY

In June 1998 Eureka Strategic Research presented the results of a research project that it conducted on behalf of the Investment and Financial Services Association and the Australian Securities Commission.[10] The research project had, as its objective, obtaining information about the level of readership and comprehension of prospectuses. The methodology involved testing respondents' understanding of four matched pairs of short form and long form prospectuses for managed funds. A

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[9] Communications Research Institute of Australia, *Developing a Performance-Based Approach to Prospectuses*, Report to the Investment Funds Association and the Australian Securities Commission, March 1997.

[10] Eureka Strategic Research, *Simpler Managed Investment Prospectuses*, Report to the Investment and Financial Services Association and the Australian Securities Commission, June 1998.

sample of 1005 investors was broken into matched groups and each group responded to questions about one of the eight prospectuses.

One question asked of the respondents was the relative importance of particular items of information contained in the prospectus. Fees and charges were ranked by the respondents as the third most important part of the prospectus. The most important part of the prospectus was the likely level of return on the investment followed by the risk of the investment losing value.

In relation to fees and charges, respondents were asked a specific question – whether entry fees applied. The result was that all but one of the short form prospectuses were superior to the long form prospectuses in explaining whether entry fees applied.

Another part of the research undertaken by Eureka was one on one in-depth interviews with investors regarding the use of prospectuses to make investment decisions. There were 16 of these interviews, with participants reflecting a variety of investor backgrounds and experience levels. One of the specific findings of this part of the research was that investors stated that they wanted clearer information on fees. Eureka also undertook two group discussions with investment advisers. There was a consensus view from one group of advisers that information concerning fees and charges should be presented in a clearer and more prominent manner.

AGEING AGENDAS STUDY

In December 2000 Ageing Agendas presented its report to the Association of Superannuation Funds of Australia (ASFA) on Key Features Statements (KFSs).[11] The purpose of this research was to test several KFS documents in order to determine consumers' understanding of these documents. The research involved a three stage process:

(1) A review and revision of a KFS developed by ASFA. This was followed by diagnostic testing with a sample of consumers.

(2) Revision of the KFS in the light of the test outcomes, the development of two other KFS documents to test consumers' capacity to make informed decisions and diagnostic testing of the three documents.

(3) Revision of a unitised KFS with entry and exit fees in light of the stage 2 testing. This was followed by diagnostic testing of the original and unitised fund to determine whether the KFS model could support a more complex fund structure and whether consumers could make fee and other comparisons using the two documents.

Twenty-four participants were interviewed for each of the three stages of the research project. Each interview lasted 30 minutes. The emphasis was upon those who did not hold tertiary qualifications. In each of the three stages, copies of the KFSs were sent to the consumers a week before the interview to allow them to read them as they would if they were choosing a fund.

One of the questions asked of the participants was to identify the information they would consider most important in choosing a superannuation fund. Fees and charges was ranked by the participants as the second most important information, with investment options being nominated as the most important and performance as the third most important. Some of the other findings of the research were:

- Issues of unitisation, fees and charges, and tax were the most troublesome for consumers.
- The use of percentages in fee information is a barrier to understanding, whether consumers are considering one fund only, or making comparisons. Where percentages are used, illustrating their effect in dollar terms improves understanding.
- The fee summary and comparison tables need to be moved to the beginning of the fees and charges section so that consumers recognise their significance and tables should be simplified.

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[11] Ageing Agendas, *Summary of the Outcomes of Consumer Testing of the ASFA Super Choice Key Features Statements*, Report Prepared for the Association of Superannuation Funds of Australia Ltd, December 2000.

- The warning about future investment performance needs to be more explicit and placed next to the performance data so that consumers see its significance.

In relation to a table showing the effect of fees, Ageing Agendas recommended in its report that the following table be used to show the effect of fees for superannuation funds.

Effect of fees on account balance – no entry fee option

Impact on account balance from	**Compulsory employer contributions of 9% on annual pay of $20,000 ($1,800)**	**Compulsory employer contributions of 9% on annual pay of $40,000 ($3,600)**
If withdrawn	Impact of Fees	Impact of Fees
after 2 years	$ 250	$ 410
after 5 years	$ 490	$ 730
after 10 years	$1,440	$2,260
after 20 years	$5,720	$9,630

SWEENEY RESEARCH STUDY

In July 2001 Sweeney Research presented its report on consumer perceptions of fees and charges which it had prepared for the Investment and Financial Services Association.[12] The objective of this research was to assess the understanding and perceptions of fees and charges by consumers who had invested in managed investments. Five hundred telephone interviews were conducted with those who had invested in managed investments. In addition, four focus group discussions were held with managed investment consumers and two focus group discussions were held with financial planners.

The profile of those who participated was different to a number of the previous research studies as the Sweeney Research study tended to have more sophisticated participants and all were already investors. For example, 31% of those who participated had invested $100,000 or more in managed investments. Another 14% had invested between $50,000 and $99,999. With respect to the household income of those who participated in the research, 30% had a household income of $90,000 or more with another 22% having a household income of between $60,000 and $89,999.

With respect to the occupation of the main income earner, 45% were classified as professional/executive; 27% as white collar; 11% as blue collar; and 13% as retired.

The 500 investors who participated in the telephone interviews were asked to consider the importance of a number of factors that they used to select managed investments. 86% of the consumers considered fees and charges to be either "important" or "very important" when evaluating managed investments. Factors which were considered to be more important were reputation of the fund manager (96%); long-term performance of the fund (96%); and risk associated with the investment (88%). When the consumers were asked to identify the single most important factor in choosing a managed investment, only 2% of consumers said that fees and charges were the most important factor in their decision-making process. The factors ranked as more important were long-term performance of the fund (54%); risk associated with the investment (17%); reputation of the fund manager (14%); advice/recommendation from financial adviser (5%); short-term return on investment (4%); and awards or ratings (3%).

Consumers were asked the extent to which they were "comfortable" with the information they had on the fees and charges at the time they selected the most recent managed investment. The replies were as follows:

- very comfortable (30%);
- somewhat comfortable (46%);
- somewhat uncomfortable (20%); and
- very uncomfortable (4%)

It is to be noted when interpreting this data that the information the consumers had about fees and charges relates to all sources of information. When asked to identify the sources of their information about fees and charges, 42% replied that it was advice from their financial adviser with 35% stating that it was the prospectus. Consequently, it is important to note that the responses concerning the extent to which consumers are comfortable with information about fees and charges must be

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[12] Sweeney Research Pty Ltd, *The IFSA Fees and Charges Consumer Perceptions Study: A Summary*

interpreted in light of the fact that the major source of information about fees and charges for the consumers was not a prospectus but a financial adviser.

Sweeney Research then asked more detailed questions concerning consumers' understanding of fees and charges. A number of the results revealed difficulty in consumers' understanding. As noted by Sweeney Research, for many consumers, the results show that it is difficult to understand the fee structure and that it is not easy for consumers to work out exactly how much a managed investment will cost. For example:

- 61% agreed with the statement that "it is difficult to understand the fee structures";
- 59% agreed with the statement that "as so many of the costs are hidden it is difficult to know how much you are paying"; and
- 53% disagreed with the statement "it's easy to work out how much the fees and charges associated with the fund will cost me".

Consumers were asked how confident they were they knew what the actual fees and charges were applying to their managed investment. The replies were:

- very confident (31%);
- somewhat confident (39%);
- somewhat unsure (18%); and
- very unsure (12%).

Consumers were asked to identify what type of fees and charges apply to their managed investments. Sweeney Research states that "perhaps the most striking finding is that close to one-third (32%) of consumers were unable to define the types of fees and charges they are paying". In order to further test consumers' knowledge of specific fees, consumers were asked to estimate what percentage of their total investment was charged (a) as an entry fee and (b) as an ongoing management/administration fee. Thirty-two per cent replied that they did not know

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Report, Report Prepared for the Investment and Financial Services Association, July 2001.

what they were charged as an entry fee while 40% of consumers replied that they did not know what were the ongoing fee levels.

Consumers were asked their preferred means of fee disclosure in prospectuses. Fifty-two per cent stated that they preferred the fees to be expressed in dollar terms. Forty-two per cent stated that they preferred fees to be itemised as a percentage/management expense ratio.

Consumers were then asked their preference for the reporting of fees and charges in ongoing statements. They were presented with four different reporting options and asked to put forward a preference. The results were:

- expressing fees both as a percentage of the investment and in actual dollar terms (54%);
- expressing fees in actual dollar terms (24%);
- showing the investment balance after fees have been deducted (12%);
- expressing fees as a percentage of the investment (7%); and
- don't know (3%).

SUMMARY

This review of the results of a number of studies which had, as their objective, testing consumers' understanding of fees and charges, reveals that a significant number of consumers fail to understand basic information about fees and charges. It can therefore be concluded that there is significant scope for improvement in the disclosure of fees and charges. Options for improved disclosure are discussed in Part 6.

Part 4

The law governing disclosure of fees and charges in Australia

FEES AND CHARGES DEFINED

DEFINITION OF MAIN TERMS AND DESCRIPTION OF TYPICAL FEES

Part 7.9 of the Corporations Regulations 2001 defines the following terms relating to fees and charges. As a general rule, these definitions apply only to superannuation products and retirement savings accounts ("RSAs"). Some of the definitions have been summarised:

- **Charge**: includes a charge made by a product issuer, service provider or other person and does not include a government charge, tax, or duty.
- **Contribution charge**: a charge which is not a death and disability insurance charge and is made either against contributions in respect of a product holder or against the holder or the holder's benefits in a fund or financial product upon joining.
- **Death and disability insurance charge**: a charge against contributions, fund or product benefits, earnings or assets which the product issuer uses solely to pay insurance premiums (including stamp duty) or any charge by the product issuer for insurance against the product issuer's liability to pay death or disability benefits.
- **Direct account charge**: a charge against product holder's benefits which is not a contribution charge, death and disability insurance charge or exit charge.
- **Exit charge**: a charge against a product holder's benefits which is only made when a payment is made in respect of a product holder or transferred.
- **Investment management charge**: a charge against a fund's assets or investment earnings where fund expenses exceed direct account charges and which is not a transaction cost, direct account charge, contribution charge, death and disability insurance charge or exit charge.

- **Ongoing management charge ("OMC")**: a charge against a product holder's benefits in a fund or product, or against assets or earnings of the fund or product, and which is not a contribution charge, death and disability insurance charge, exit charge or switching charge, and which is made for a service that a product holder would not otherwise receive if the product holder had not requested and paid for the service, which is provided by the provider and is reasonable, and which is calculated in accordance with Schedule 10.[13]
- **Switching charge**: a charge against a product holder or the holder's benefits in a fund or product made for the transfer of all or part of the holder's benefits from one investment strategy to another.
- **Transaction cost**: brokerage, stamp duty or costs arising from maintenance of a property investment.

AUSTRALIAN FINANCIAL PRODUCT DISCLOSURE

FINANCIAL PRODUCTS

The Corporations Act 2001, as amended by the Financial Services Reform Act ("**FSRA**") ("**the Act**"), defines a "financial product" in s 763A as:

> [A] facility through which, or through the acquisition of which, a person does one or more of the following:
>
> (a) makes a financial investment (see section 763B);
>
> (b) manages financial risk (see section 763C);
>
> (c) makes non-cash payments (see section 763D).

[13] Schedule 10 essentially provides as follows:

The formula is: **MC/AV** where:

AV = average value of fund assets during the income year, determined by mean average of net asset valuations made during that year.

MC = total amount of ongoing management charges for the year, excluding charges paid by a standard employer-sponsor of the fund.

If the underlying investments are managed by someone other than the product issuer (eg: external manager) and a charge is deducted from returns before the return is computed and credited, then that charge must be included in **MC**. A reasonable estimate of the charge must be made if the precise amount cannot be determined. Direct investment in shares or other securities listed in Australia is excluded.

Section 763B provides that a "financial investment" arises if:

(a) the investor gives money or money's worth (the ***contribution***) to another person and any of the following apply:

(i) the other person uses the contribution to generate a financial return, or other benefit, for the investor;

(ii) the investor intends that the other person will use the contribution to generate a financial return, or other benefit, for the investor (even if no return or benefit is in fact generated);

(iii) the other person intends that the contribution will be used to generate a financial return, or other benefit, for the investor (even if no return or benefit is in fact generated); and

(b) the investor has no day-to-day control over the use of the contribution to generate the return or benefit.

Section 763C provides that a person "manages financial risk" if they:

(a) manage the financial consequences to them of particular circumstances happening; or

(b) avoid or limit the financial consequences of fluctuations in, or in the value of, receipts or costs (including prices and interest rates).

The Act provides, in each of the above cases, examples of situations that are both within and outside the scope of the definitions; it is not necessary to reproduce those examples here. Additionally, the Act defines, at s 764D, when a person makes a "non-cash payment"; again, it is not necessary for the purposes of this report to examine that situation. Section 763E applies to those situations where a financial product is merely incidental to other facilities that are not within the s 763A definition of financial product.

Section 764A provides a list of things that are specifically prescribed as financial products. Of the broad range of financial products included in s 764A, those of most

interest are a security,[14] an interest in a registered scheme,[15] an interest in a managed investment scheme,[16] a superannuation interest[17] and a retirement savings account.[18]

Section 765A provides a list of things that are specifically prescribed as *not* financial products. This provision has effect despite anything previously stated to be specifically included within the definition of a financial product. Again, the list is quite extensive, but includes such things as health insurance,[19] reinsurance,[20] credit facilities,[21] facilities for settling non-cash payments[22] and currency exchange contracts.[23]

The analysis in this report is confined to the following products: superannuation and superannuation-like products (eg: annuities, RSAs, capital guaranteed funds, rollover funds and the like), and managed investment schemes (eg: managed funds, public offer unit trusts, cash management trusts, property trusts and the like).[24]

FINANCIAL PRODUCT DISCLOSURE

Part 7.9 deals with disclosure and some other matters relating to the issue and sale of financial products. Section 1010A provides that Part 7.9 does not generally apply in relation to securities; for provisions covering disclosure in relation to securities, the Act signposts Chapters 6CA and 6D, which cover prospectuses and related matters.

Section 1010B states initially that the Part does not apply to issues that are not made in the course of a business of issuing financial products. Section 1010B(2), however, states that the issue of any managed investment product or any superannuation product *is* taken to occur in the course of such a business.

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[14] Section 764A(1)(a).
[15] Section 764A(1)(b).
[16] Section 764A(1)(c).
[17] Section 764A(1)(g).
[18] Section 764A(1)(h).
[19] Section 765A(1)(c).
[20] Section 765A(1)(g).
[21] Section 765A(1)(h).
[22] Section 765A(1)(i) and (k).
[23] Section 765A(1)(m).

Sections 1012A, 1012B and 1012C establish the obligation to give a Product Disclosure Statement ("**PDS**"), respectively, when personal advice is given recommending a particular financial product, when an issue of or an offer to issue a financial product is made, or when an offer to sell a financial product is made.

CONTENT OF PRODUCT DISCLOSURE STATEMENTS

The information in the PDS must be up to date as at the time at which the PDS is given (s 1012J). Section 1013A defines who is obliged to prepare the PDS: in the case of advice or the issuing (or offering thereof) of a financial product, the issuer is required to prepare the PDS; in the case of the sale (or offering thereof) of a financial product, the person making the sale or the offer to sell is required to prepare the PDS.

General Disclosure Requirements

Section 1013B requires that the PDS be endorsed "Product Disclosure Statement" on its cover, or at or near the front of the PDS; in any other part of the PDS, the abbreviation "PDS" may be used.

Section 1013C is the general provision setting out the content requirements for PDSs. In sum, the PDS must contain:

- the statements and information required by s 1013D;
- the information required by s 1013E; and
- the information required by other provisions of this subdivision (namely, subdivision C).

Section 1013C(3) states that the information in the PDS "must be **worded and presented** in a clear, concise and effective manner" (emphasis added).

Presentation can be taken to include such matters as layout, format, typeface, graphics, colour, indexation, ordering, and lexicon. It can also be a reference to the use of appropriate and useful examples, tables and illustrations, or any other thing that

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[24] But not interests in unregistered management investment schemes which, generally, are small-scale offerings and comprise no more than 20 issues or sales in a 12-month period: r 7.9.16A, prescribing the same for the purposes of s 1012E(1)(b).

aids comprehension. Additionally, it can encompass the consideration of giving appropriate weight and prominence to those matters which require to be elevated in prominence due to their significance or nature. "Effective" also requires a consideration of the type of person who will read the PDS. It is to be noted that projections (ie, showing the effect of fees on returns) are not required by the Act or by the regulations made under the Act.

Specific Disclosure Requirements

Section 1013D provides, relevantly, that a PDS must include "the following statements, and such of the following information as a person would reasonably require for the purpose of making a decision, as a retail client, whether to acquire the financial product":

> (d) information about:
>
> (i) the cost of the product; and
>
> (ii) any amounts that will or may be payable by a holder of the product in respect of the product after its acquisition, and the times at which those amounts will or may be payable;[25] and
>
> (iii) if the amounts paid in respect of the financial product and the amounts paid in respect of other financial products are paid into a common fund—any amounts that will or may be deducted from the fund by way of fees, expenses or charges;

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[25] Section 1013D(2) defines when an amount "will or may be payable":

> For the purposes of paragraph (1)(d), an amount will or may be payable in respect of a financial product by the holder of the financial product if:
>
> (a) the holder will or may have to pay an amount in respect of the product; or
>
> (b) an amount will or may be deducted from:
>
> (i) a payment to be made by the holder; or
>
> (ii) a payment to be made to the holder; or
>
> (iii) an amount held on the holder's behalf under the financial product; or
>
> (c) an account representing the holder's interest in the financial product will or may be debited with an amount.
>
> It includes an amount that the holder will or may have to pay, or that will or may be deducted or debited, as a fee, expense or charge in relation to a particular transaction in relation to the financial product.

Regulation 7.9.72A modifies the effect of s 1013D(1)(d) as if that section provides that information about amounts that will or may be payable state, instead, the basis on which the amount of liability would be calculated rather than specifying an amount.

(e) if the product will or may generate a return to a holder of the product—information about any commission, or other similar payments, that will or may impact on the amount of such a return;

(f) information about any other significant characteristics or features of the product or of the rights, terms, conditions and obligations attaching to the product;

…

(k) any other statements or information required by the regulations.[26]

Section 1013E is a general provision requiring the PDS to contain "any other information that might reasonably be expected to have a material influence on the decision of a reasonable person, as a retail client, whether to acquire the product". The important point is that the provision requires such a decision to be made from the perspective of the retail client, not the issuer.

Section 1013F limits the extent to which information is required to be included. The provision is the flip-side of s 1013E and allows information to be left out of a PDS if it would not be reasonable to expect to find it in the PDS. Section 1013F(2) provides a non-exhaustive list of the matters that may be considered in determining whether it would not be reasonable to expect to find the information in the PDS:

(a) the nature of the product (including its risk profile); and

(b) the extent to which the product is well understood by the kinds of person who commonly acquire products of that kind as retail clients; and

(c) the kinds of things such persons may reasonably be expected to know; and

…

(e) the way in which the product is promoted, sold or distributed; and

(f) any other matters specified in the regulations.

The reference in s 1013F(2)(b) to how "well understood" a product is might, on occasions, be taken to require product issuers to consider consumer testing surveys if

[26] Section 1013D(4) gives some indication of the extent to which the regulations may (and do) dictate the requisite information of a PDS:

The regulations may:

(a) provide that a provision of subsection (1) does not apply in a particular situation; or

(b) provide that particular information is not required by a provision of subsection (1), either in a particular situation or generally; or

wanting to take advantage of this exemption from disclosure. Consideration of consumer understanding of product disclosure appears in Part 3 of this report.

THE REGULATIONS

Many of the statutory provisions governing material to be included in a PDS make reference to the Corporations Regulations 2001 (as amended) ("**the Regulations**").

Regulation 7.9.01 defines many of the terms used in the subsequent Regulations. As noted above, as a general rule these definitions apply only to superannuation products and RSA products. Without expanding unnecessarily, r 7.9.01 provides definitions of charge, contribution charge, death and disability insurance charge, direct account charge, exit charge, investment management charge, ongoing management charge, switching charge, and transaction cost.

Division 4 of the Regulations provides for the content of PDSs. The note to r 7.9.09 states that the Regulations set out the more-detailed information requirements pursuant to s 1013D(1). Regulation 7.9.09(1) limits the application of the Division to superannuation, RSA products and annuity products.[27]

Regulation 7.9.11 states that Schedule 10B sets out the additional information required by s 1013D(4)(c) in respect of superannuation and annuities that meet the standard set by r 1.05(4) of the Superannuation Industry (Supervision) Regulations 1994 ("**SIS**"). In respect of capital guaranteed funds, RSAs or annuities that do not meet the standard set by r 1.05(4) of SIS, the additional information is found in Schedule 10C.

(c) provide a more detailed statement of the information that is required by a provision of subsection (1), either in a particular situation or generally.

[27] "Annuity" is defined by r 7.9.01 to have the same meaning as in r 1.05 of the Superannuation Industry (Supervision) Regulations 1994. The definition there is somewhat lengthy and technical but essentially an annuity is a contract under which the product holder is paid at least annually for the holder's life, and thereafter to reversionary beneficiaries of the holder, subject to a number of requirements in respect of variations to the size, frequency and commutation of payments.

Part 5 of Schedule 10A of the Regulations provides that the Regulations may also make other arrangements for the format of a PDS, including the location of particular statements or information.

Schedule 10B: Superannuation and Some Annuities

Clause 1.8 requires the PDS to bear on its front or cover or first page:

> A statement that a person who leaves the fund within a few years of joining may get back less than the amount of contributions paid because of the level of investment returns earned by the fund and the fund's charges.

Clause 6.1(c) requires the following:

> [A] statement that the net earnings rate may not be the same as the rate credited to particular members because of the effect of charges made by the fund and, if relevant, the reserving policy of the fund;

Item 7, which covers fund charges, is extensive and is only reproduced below in part. Clause 7.1 states that, for any contribution charge, direct account charge, investment management charge, exit charge or switching charge, the PDS must give a description of the charge and:

> (b) the amount of the charge:
>
> (i) expressed as a fixed amount; or
>
> (ii) if it is not practicable to express [a] fixed amount, expressed as a percentage of:
>
> (A) the contributions made in respect of a member; or
>
> (B) the member's benefits in the fund; or
>
> (C) the assets of the fund; and
>
> (c) against what, or to whom, the amount or percentage will be charged (for example, against contributions made in respect of the member to the fund or against the assets of the fund);…

Clause 7.2 requires the information in cl. 7.1 to be provided for any death and disability insurance charge of the fund.

Clause 7.3 requires a statement outlining the circumstances in which and the times when any charge may be increased or decreased, as well as any maximum limits on any charges.

For any of the charges in cl. 7.1, cl. 7.4 requires the product issuer to explain how a charge is to be determined if it cannot be expressed as an amount or a percentage.

In the case of a product offering different investment strategies, cl. 7.5 directs the product issuer to disclose the fee and charge information required by cl. 7.1 if those fees and charges differ as between each strategy.

If a death and disability charge is determined by a premium rate table, cl. 7.6 permits the PDS to attach that premium rate table and refer to it in respect of any such charge.

Ongoing Management Charges

Disclosure of OMC varies depending on whether the financial product offers a single investment strategy or whether it offers a choice of investment strategies (eg: a superannuation fund that offers "conservative", "balanced" and "growth" options for the investment of member funds, each option respectively having a higher risk/return profile than the preceding option).

Disclosure for financial products is best understood in terms of general and specific parts. All products, irrespective of investment strategy category, must disclose the general part. The specific part will vary depending on whether the product has a fixed investment strategy or offers a choice of strategies.

<u>General</u>

Clause 8.1 requires the following statement to be disclosed for the "overall fund, the product issuer or the provider of an annuity":

> 'The ongoing management charges charged by a [*insert* 'trustee', 'life insurer', 'provider of an annuity' *or other appropriate description*] over a year can be expressed as a percentage of its assets.
>
> In the last [*insert* 'year', '2 years', '3 years', '4 years' or '5 years' *as appropriate*], the ongoing management charges, expressed as a percentage of the fund's assets, were:'

The statement is then completed according to whether the product offers only one investment strategy or a number of strategies.

Single Investment Strategy Products

In this case, the provider provides: [28]

(i) the actual ongoing management charge percentage for the required periods: and

(ii) the actual ongoing management charge percentage relating to the management of investments for the required periods; and

(iii) the actual ongoing management charge percentage not relating to the management of investments for the required periods.

The "required periods" are the latest year of income at the time the PDS is published and the 4 preceding years of income (but not a year of income ending on or before 30 June 2001).[29]

Following disclosure of this numerical information, the PDS must contain the following prescribed statement:

> 'The approximate effect of the ongoing management charges (based on the charges for the year to [*insert most recent year*] on your benefits can be shown by multiplying this percentage by the amount in your account. The following example shows the approximate amount of the ongoing management charges for an account balance of $10,000 in relation to the overall [*insert* 'fund', 'life insurer', 'provider of an annuity' *or other appropriate description*]. The actual effect of ongoing management charges will depend on the [*insert* 'fund's', 'life insurer's' *or other appropriate description*] charging arrangements and your individual circumstances. In particular, the amount in your account [*if more than one identified strategy* – and your chosen investment strategy] may have a significant effect on the amount of charges borne.'[30]

This statement is then "followed by an example deriving the converted amount for the overall fund, product issuer or provider of an annuity".[31] The "converted amount" is

[28] Corporations Regulations 2001, Schedule 10B, cl. 8.2(a).
[29] Corporations Regulations 2001, Schedule 10B, cl. 8.6.
[30] Corporations Regulations 2001, Schedule 10B, cl. 8.4(a).
[31] Ibid.

defined in cl. 8.3 as "$10 000 multiplied by the ongoing management charge percentage".[32]

A statement is then required which identifies the charges included in the OMC, in total and separated for investment and non-investment management expenditure, and which have been disclosed under cl. 8.1.[33] Then, the PDS must contain:

> (c) a statement that the person should read the charges section of the document; and
>
> (d) a statement that past charges should not be taken to be an indication of future charges; and
>
> (e) the statement:
>
> > 'The ongoing management charge for a [*insert* 'fund', 'life insurer', 'provider of an annuity' *or other appropriate description*] is required by law to be calculated and disclosed. Its purpose is to give a broad indication of the level of costs incurred by a particular fund or provider of an annuity as a percentage of the value of assets. Costs include all fees, charges and expenses except for [*insert* 'switching costs,[34] 'entry and exit charges' *or other appropriate description*]. The level of costs incurred by an individual product holder will depend on individual circumstances and as a percentage of value of the fund assets of the individual may be more or less than the ongoing management charge. The ongoing management charge should not be taken to be representative of the actual fees, charges and expenses that will be borne by an individual. Full details of fees, charges and expenses applicable to individual circumstances are set out in [*section X*] of this document.'.

<u>Multiple Investment Strategy Products</u>

Where the product has alternative identifiable investment strategies, the PDS must contain the same preliminary statement as required for a single strategy product but must also include the additional requirements in cl. 8.2. This requires, in much the same way as for a single strategy product, providing for each identified investment strategy: the same actual OMC percentage information for the required periods in respect of overall OMC, investment-management OMC and non-investment-

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[32] This definition is expressed to be applicable to cl. 8.2 (which is applicable to products having multiple investment strategies). Consistency would indicate that the "converted amount" ought be the same for single strategy and multiple strategy products. The fact that the foregoing prescribed statement refers to that same sum of $10,000 seems to confirm that consistent approach.

[33] Corporations Regulations 2001, Schedule 10B, cl. 8.4(b).

management OMC, together with in each case, the "converted amount" for each percentage, or a statement:

(i) of the highest and lowest actual ongoing management charge percentage for the required periods in respect of all investment strategies and the converted amount for each percentage; and

(ii) of the highest and lowest actual ongoing management charge percentages relating to the management of investments for the required periods in respect of all investment strategies; and

(iii) of the highest and lowest actual ongoing management charge percentages not relating to the management of investments for the required periods in respect of all investment strategies; and

(iv) that information on the specific ongoing management charge calculations for a particular investment strategy are available on request, and details of how to request that information.

The prescribed statements and example required by cl. 8.4 are required as for single strategy products.[35]

Essentially, disclosure of OMC for superannuation and annuities varies depending on whether the product has one investment strategy or multiple strategies. The following table illustrates the distinction:

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[34] The second single-quotation mark appears to have been omitted.
[35] See nn 30-34, above, and text thereto.

OMC Disclosure

Schedule 10B – Corporations Regulations

Single Strategy

cl. 8.1

- Preamble statement
- Overall OMC%, investment-mgmt OMC% and non-investment-mgmt OMC%

cl. 8.4

- Explanation of effect of OMC
- Example based on $10,000 for overall fund/product
- Statement of charges included in each of overall OMC, investment-management OMC and non-investment-management OMC
- Prescribed statements
  - Warning to read charges section
  - Notice that past charges do not necessarily indicate future charges
- Description of OMC and signpost

Multiple Strategy

cl. 8.1

- Preamble statement

cl. 8.2

- "For each identified investment strategy": OMC% and converted amount, for each of overall OMC, investment-mgmt OMC and non-investment-mgmt OMC

OR

- "In respect of all investment strategies": a statement of the highest and lowest OMC% and converted amount, for each of overall OMC, investment-mgmt OMC and non-investment-mgmt OMC, and a notice that OMC calculations specific to particular strategies is available on request

cl. 8.4

- Explanation of effect of OMC
- Example based on $10,000 for overall fund/product
- Statement of charges included in each of overall OMC, investment-mgmt OMC and non-investment-mgmt OMC
- Prescribed statements
  - Warning to read charges section
  - Notice that past charges do not necessarily indicate future charges
- Description of OMC and signpost

Where a prospective investor requests further information in the case of a product having multiple investment strategies, r 7.9.12 states that where a product issuer has provided a PDS that complies with cl. 8.2(b), a request for further information must be met by provision of the information that would have to be disclosed under cl. 8.1 in respect of single strategy products. That disclosure would then provide an accurate indication of OMC percentages, rather than merely the highest and lowest OMC percentages.[36] Although the heading to r 7.9.12 implies that the regulation is confined to standard employer-sponsors and successor superannuation funds, the content of the regulation itself suggests no such limitation.

The numerical OMC information must not be more than 15 months out of date.[37]

Schedule 10C: Capital Guaranteed Funds, RSAs and Some Annuities[38]

Item 7 of Schedule 10C is similar to the corresponding item in Schedule 10B; there are two main differences:

- Clause 7.1 – charges: the applicable charges are slightly different, given the nature of the products covered by this schedule. They are: "any contribution charge, direct account charge or exit charge of a capital guaranteed fund".
- Clause 7.4: this is unique to Schedule 10C:

> If fees and charges are deducted before interest is credited to the fund — a statement to the effect that interest is paid net of expenses.

There is no requirement in Schedule 10C to disclose prescribed statements along the lines of item 8 of Schedule 10B.

[36] Corporations Regulations 2001, r 7.9.12 modifying s 1017A of the Act for the purposes of s 1020G(1)(c) of the Act.
[37] Corporations Regulations 2001, Schedule 10B, cl. 8.7.
[38] The signpost to the heading to Schedule 10C erroneously refers to r 7.912; it should refer to r 7.9.11.

Part 5

International Review of Laws Governing Disclosure of Fees and Charges

INTRODUCTION

In this part of the report a detailed review is provided of the regulatory framework for the disclosure of fees and charges in managed investments in four countries:

- the United Kingdom;
- New Zealand;
- Canada; and
- the USA.

UNITED KINGDOM

The legislation relating to product disclosure in the United Kingdom is less detailed in comparison to its Australian counterpart. Considerable discretion for implementation of disclosure standards is left to the Financial Services Authority ("**FSA**"). The FSA disclosure standards are published in the FSA's Handbook ("**the Handbook**"). The Handbook is complex and technical and is divided into Handbook Modules, Sourcebooks, Legal Instruments and Consultation Papers, *inter alia*. The Reader's Guide to the Handbook explains the status of the Handbook as follows:

> Section 153 of the [Financial Services and Markets Act 2000] requires the FSA to exercise its rule-making powers in writing. The Act describes the document by which the rules are made as a 'rule-making instrument' and imposes a number of requirements, including a requirement to publish it. The FSA will publish all instruments by which provisions in the Handbook are made or amended in full on its website. These fulfil the statutory and other legal requirements for publication, and will be the definitive source for determining what the text was at any particular time for legal purposes… [39]

[39] Financial Services Authority, *Handbook: Reader's Guide*, 1.

PRODUCTS COVERED

The regime governed by the FSA covers a broad array of products, from cash deposit and savings accounts to life insurance, pensions and trust-governed investments, with numerous variations in between. In order to facilitate comparisons across jurisdictions, this review is confined to *packaged products* and *collective investment schemes*.

Packaged Products

The Glossary to the Handbook defines packaged products to include:[40]

- Units in *regulated collective investment schemes*, which means:[41]
  - An *investment company with variable capital* ("**ICVC**"), which is a body incorporated under the Open-Ended Investment Company Regulations 2001;[42] or
  - An *authorised unit trust scheme*, which is a collective investment scheme under which property is held on trust for participants;[43]
- Interests in *investment trust savings schemes* ("**ITSS**"), which are dealing services dedicated to the securities of particular investment trusts (and the securities themselves);[44] and
- *Stakeholder pension schemes* ("**SPS**"), which are a form of private superannuation enabling regular contributions to be accumulated and invested and preserved until retirement, at which point the pension is used to purchase an annuity.[45]

Collective Investment Schemes

Collective investment schemes, which are defined by s 235 of the Financial Services and Markets Act 2000, are summarily defined by the Glossary as follows:

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[40] FSA, *Handbook: Glossary* (22 November 2001) ("**FSA Glossary**"), 103-4. The definition also includes life policies but this international review does not encompass insurance products.

[41] Ibid, 123. The definition also includes recognised schemes, which is simply a territoriality provision.

[42] Ibid, 72.

[43] Ibid, 13 (*authorised unit trust scheme*: a unit trust scheme which is authorised by the FSA); 152 (*unit trust scheme*); 23 (*collective investment scheme*); 105 (*participant*).

[44] Ibid, 75 (*investment trust savings scheme*); 74 (*investment trust*: a listed UK or EEA company which has the Inland Revenue Commission's approval under the Income and Corporation Taxes Act 1988); 36 (*dealing*: buying, selling, subscribing for or underwriting investments or offering or agreeing to do so, whether as principal or agent), 72 (*investment*: any investment, including any asset, right or interest).

[45] FSA, *Factsheet: Stakeholder Pensions and Decision Trees* (November 2001), 7.

(a) any arrangements with respect to property of any description, including money, the purpose or effect of which is to enable persons taking part in the arrangements (whether by becoming owners of the property or any part of it or otherwise) to participate in or receive profits or income arising from the acquisition, holding, management or disposal of the property or sums paid out of such profits or income; and

(b) which are not excluded by the Financial Services and Markets Act (Collective Investment Schemes) Order 2001.[46]

Application

The Conduct of Business Module[47] to the Handbook ("**COB**") is subsumed within the Business Standards "block" of the Handbook. The Collective Investment Schemes Module[48] ("**CIS**") is subsumed within the Specialist Sourcebooks "block".

COB applies to every firm, except for ICVCs,[49] mostly "in relation to *regulated activities*, conducted by *firms*, which fall within the definition of *designated investment business*".[50] The Glossary defines the italicised terms. A firm is a person who is authorised to carry on regulated activities, with which there is quite some degree of overlap with designated investment business. Regulated activities and designated investment business are defined by Part II of the Financial Services and Market Act 2000 (Regulated Activities) Order 2001. Regulated activities include dealing in investments as agent, arranging deals in investments, managing investments, establishing or operating a collective investment scheme, acting as trustee of an authorised unit trust ("**AUT**"), establishing or operating an SPS, and advising on investments.[51] These activities are regulated activities if they are undertaken by way of business and relate to *specified investments*[52] (except in the case of collective investment schemes, AUTs and SPSs, in which case the activities relate to property of any kind). Designated investment business means carrying on by way of business most of the regulated activities.[53] The packaged products and collective investment schemes covered by this review fall within the advisory and agency aspects of regulated activities and designated investment business.

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[46] FSA Glossary, 23.
[47] Financial Services Authority, *Handbook: Conduct of Business*, (21 June 2001) ("**COB**").
[48] Financial Services Authority, *Handbook: Collective Investment Schemes* (21 June 2001) ("**CIS**").
[49] COB, ¶¶1.1.1R and 1.2.1R(3). References denoted by an "R" are to Rule paragraphs, while references denoted by a "G" are to Guide paragraphs.
[50] Ibid, ¶1.3.2G(2).
[51] FSA Glossary, 122-3.
[52] Ibid, 141-2 (*specified investment*: includes a deposit, share, debenture, unit, SPS, option and future).

Whereas COB applies generally to packaged products and some types of collective investment (generally, regulated collective investment schemes, but not ICVCs), CIS applies specifically to ICVCs, directors and depositaries thereof, and managers and trustees of AUTs,[54] and additionally provides further regulation in respect of collective investments generally; thus there is some overlap between the COB and CIS modules.

PRODUCT DISCLOSURE[55]

Key Features

COB section 6.1 applies to the sale, recommendation and/or arrangement thereof of packaged products[56] to private customers.[57] Product providers[58] are required to give key features[59] in respect of each product offered.[60] The FSA's rationale echoes Australian policy sentiments on product comparability:

> …there is a special need to ensure that *private customers* are supplied with information which will highlight particular *packaged product* features. This also needs to be achieved in a way which will optimise the *private customer's* ability to make a comparative analysis of different *packaged products*.[61]

In order to achieve that optimisation of comparability, the FSA requires prescribed and marketing material to be presented to the same standards:

> A firm must ensure that any key features or information document it produces is in writing, whether in printed hard copy or in electronic format, and:
>
> (1) is produced and presented to at least the same quality and standard as the associated sales or marketing material being used by the firm to promote the packaged product…to customers…[62]

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[53] Ibid, 39-40.
[54] CIS, ¶1.1.1G.
[55] COB, Chapter 6.
[56] And individual savings accounts ("**ISAs**"), which are omitted from this review. According to the FSAwebsite (http://www.fsa.gov.uk/register/glossary/main.asp):

> This is like a wrapper you can put around various savings and investments. Income and growth from the savings and investments inside the ISA are currently tax-free. What you can put into it depends on the type of ISA. For example, a cash ISA can hold a bank, building society or National savings account; an equity ISA (also called a 'stocks and shares ISA') can hold gilts, corporate bonds, shares, unit trusts and so on. An insurance ISA can hold an investment-type life insurance policy.

[57] As well as trustees of an occupational pension scheme and the trustee or operator of an SPS: COB, ¶6.1.1R.
[58] FSA Glossary, 116 (*product provider*: defined to include the operator of a regulated collective investment scheme or an ITSS).
[59] Ibid, 76: (*key features*: defined to include information about a scheme or SPS which is required to be produced in the format specified in COB 6.1 to COB 6.5).
[60] COB, ¶6.1.4R.
[61] Ibid, ¶6.1.3G.
[62] Ibid, ¶6.1.5R.

The FSA described the role and prominence of key features as follows:

> The main component of the product disclosure regime is the Key Features Document (KFD). Firms are currently required to provide consumers with a KFD both pre- and post-sale for all 'packaged products'….The KFD is generally produced by the product provider.
>
> All KFDs must include information about the aims, risks, commitments and charges for the product. They include detailed tables of the projected return on the investment based on assumed growth rates prescribed by the FSA, with the aim of showing how charges can affect the return on the product throughout its life. For life and pension products only these tables are based on customer-specific information such as age and sex, and are referred to as a 'personal illustration'.[63]

COB Chapter 6 provides detailed guidance in respect of the format of key features, with special provisions in relation to particular products, including those previously stated to be packaged products and *schemes*.[64]

Key features are required to be provided for the following packaged products:

- Schemes (regulated collective investment schemes, AUTs, ITSSs): COB ¶6.2.22R.
- Stakeholder Pension Schemes: COB ¶6.4.15R, but not where the SPS is sold on the personal recommendation of, or arranged to be sold by, another firm (COB ¶6.4.18R).

Content of Key Features

COB section 6.5 explains that key features differ for schemes and SPSs.[65]

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[63] FSA, *Informing Consumers: A Review of Product Information at the Point of Sale* (Discussion Paper, November 2000), at ¶¶15-16.

[64] For clarity it should be pointed out that a *scheme* is not an SPS and is not necessarily an ITSS. In CIS (and other parts of the Handbook, excluding COB), a scheme is "a collective investment scheme"; in COB, a scheme is a regulated collective investment scheme and/or an investment trust where the relevant shares are acquired through an ITSS. It is by virtue of that definition that both COB and CIS apply to determining the contents of key features in respect of packaged products. Another way to understand the overlap is to regard the definition of *scheme* for CIS ("a collective investment scheme") as being broader than the COB definition, which makes sense given that COB does not apply to ICVCs but does apply to AUTs.

[65] COB, ¶6.5.2R(1).

Schemes

The key features for schemes require the information set out at the table given in ¶6.5.11, which signposts provisions within ¶¶6.5.12 – 6.5.40. Relevantly, the key features are as follows:

- Non-prescriptive: ¶6.5.3R provides that firms may adapt the prescribed content and format requirements if necessary to reflect the terms and nature of a particular product. ¶6.5.4G(1) goes further: "where the rules in COB 6.5 do not require the use of prescribed text, firms may give the relevant information using their own words and style".
- An example: a personalised projection must be given,[66] generally based upon the actual amount the private customer is proposing to invest.[67] COB section 6.6 explains how projections are to be calculated, and includes consideration of charges and expenses.
- Tables: ¶¶6.5.30 – 6.5.31R require the following table to be provided within the key features, with the wording within the brackets replaced as directed by the instructions within those brackets:[68]

[66] Ibid, ¶6.5.15R.
[67] Ibid, ¶6.5.19R(3).
[68] Ibid, ¶6.5.32R.

How will charges and expenses affect my investment?

[Give an indication of the nature and amount or rate of the charges and expenses which the *private customer* will or may bear, including any relevant proportion of *scheme* charges deducted directly from the fund or not directly attributed to the account of the *private customer*. In describing the nature of charges state how the charges will be made, in particular whether they will be taken from capital or income. Include a statement that dealing costs are not included.]

[Give a statement that there is a buying price and a selling price (if that is the case) and that the difference between them is called the 'spread', and an indication of where up–to–date information may be obtained on these prices.]

Their effect on an *investment* of £_____ assuming growth of [insert the intermediate rate appropriate to the type of *scheme* set out in *COB* 6.6.49R)] a year, is set out below

[Where (except as described in *COB* 6.5.15R(2)) a *projection* is not a *requirement*, include a statement that the figures are not guaranteed and serve only to demonstrate the effect of charges and expenses on an investment.]

At end of year	Investment to Date	Effect of deductions to date	What you might get back [at the appropriate intermediate rate]
	£	£	£
1			
3			
5			
10			

The figures in the table are to be calculated in accordance with the projection rules contained in COB section 6.6.[69]

[69] Ibid.

The "Effect of deductions to date" column provides the cumulative sum of charges and expenses (as defined by ¶6.6.23) and the figures must be calculated in accordance with ¶6.5.35 which provides the calculation method for the effect of charges to date.[70] The "What you might get back" column takes account of charges and expenses and shows what the value might be if the scheme were cashed in.[71]

The "effect of charges to date" is derived as follows:

> For each year, figures must be given for the effect of deductions assuming the fund grows in accordance with a relevant rate of return (as defined in COB 6.6.33). These calculations must reflect all deductions (charges and expenses as defined in COB 6.6.23) expected to be levied against the fund and against the private customer's investment.[72]

The charges and expenses consideration in ¶6.6.23 provides:

> (1) For a scheme…charges and expenses are all explicit charges and expenses the customer will or may bear:
>
> (a) including:
>
> (i) all other deductions and expenses which will or may bear upon the fund (including charges in respect of any collective investment scheme…in which any funds of the contract in question are invested but excluding dealing costs of the underlying portfolio);
>
> (ii) all deductions from the…contribution payable which do not accrue to the benefit of the customer by way of contribution to the value of the benefit;
>
> (b) having regard to:
>
> …
>
> (ii) any tax relief which will be available to the…scheme in respect of so much of the…scheme's gross expenses as can be properly attributed to the contract.

[70] Ibid, ¶6.5.32R(4).
[71] Ibid, ¶6.5.32R(5).
[72] Ibid, ¶6.5.35R. Additional principles are given which expand upon this Rule.

Para 6.6.24G explains: "For the calculation of the effect of deductions in projections, charges are all explicit charges adjusted for tax…and expenses are all other deductions." The Glossary defines a *charge* as "any fee or charge made to a client in connection with designated investment business…including a mark-up or mark-down".[73] However, for the purposes of ¶6.6.23R, expenses are assessed and apportioned as follows:

- AUTs, OEICs and recognised collective investment schemes: ¶6.6.65G provides the overriding guidance. Importantly, in terms of presentation, ¶6.6.65G(3) states that "[w]here expenses are charged directly against the assets of the fund, it will normally be appropriate to express such expenses as an annual percentage charge against the fund…". In respect of the types of expenses to be considered, ¶6.6.67G provides as follows:

  (1) The following are those expenses and costs of investment that firms should take into account when making their calculations. The list is not comprehensive. These are in addition to explicit charges.

  (2) Examples of expenses are:

  (a) registration fees;

  (b) safe custody fees;

  (c) trustees' fees;

  (d) handling charges;

  (e) audit fees;

  (f) regulatory fees and subscriptions;

  (g) costs of investment management, but excluding dealing costs of the underlying portfolio, and costs associated with routine management and servicing of existing property investments;

  (h) bid/offer spread in the pricing of units.[74]

- ITSSs: in contrast to AUTs et al, the overriding guidance here (¶6.6.70G) states:

  (1) Charges and expenses as described in COB 6.6.23 should be taken to include all explicit charges and, in addition, all other deductions and expenses which are not financed from explicit charges.

[73] FSA Glossary, 18.
[74] COB, ¶6.6.67G.

(2) The method is to identify all expenses that will be borne by the customer, and these will include not only the cost of acquiring a holding but also the cost of disposing of the investment.

(3) Where expenses are charged directly against the assets of the investment trust, it will normally be appropriate to express the expenses as an annual percentage charge against the trust, which is then added to such charges….

The (non-exhaustive) types of expenses to be considered are given in ¶6.6.72G(2):

(a) deductions levied against the assets of the investment trust company;

(b) management expenses levied against the assets of the investment trust company; these expenses include management fees plus any management costs financed from commission received, directors' fees, pension contributions, non-recurring expenses, all other professional and regulators' fees and subscriptions, rents paid, depreciations, custody fees, audit fees and all other pre-tax expenses (except for interest paid); management expenses include marketing costs, if any;

(c) expenses borne by the customer in acquiring or disposing of investment trust shares; these include adviser's commission (if any), stockbroker dealing commission on purchases and sales, stamp duty and withdrawal charges;

(d) investment spread in the pricing of the investment trust shares.

- Deductions summary: immediately beneath the table, the key features must say:

The last line in the table shows that over [n] years the effect of the total charges and expenses could amount to £x.

and either:

Putting it another way, if the growth rate were to be (x)%, which is in no way guaranteed, this would have the effect of reducing it to (y)% a year.

or

Putting it another way, this would have the same effect as bringing investment growth from (x)% a year down to (y)% a year.[75]

[75] Ibid, ¶6.5.33R.

COB also provides particular rules for the calculation of this "reduction in yield".[76]

- Commission and remuneration: like Australia, the UK does not place adviser earnings firmly in the "cost of product" sphere. However, COB does indicate that the cost of advice does impact upon the investment structure: omitting references to life policies, COB states that a firm is required, under the heading "How much will the advice cost?", to state that commission or remuneration is paid for out of deductions or charges (as appropriate).[77]

COB section 5.7 sets out rules and guidance in respect of communicating to clients the costs, "directly or indirectly, of financial services, so that [they are] better able to make informed choices".[78] A firm is required to disclose in writing to a customer the basis or amount of its charges as well as the nature or amount of any other income receivable by it.[79] COB states that "disclosure should include any product-related charges that are deducted from the private customer's investment",[80] noting further that disclosure of such product-related charges would be made in key features in respect of packaged products.[81] In any event, COB ¶5.7.5R requires, before effecting a packaged product transaction, a product provider or independent intermediary to disclose to the private customer any remuneration or commission receivable in respect of the transaction in "cash terms".[82] This disclosure is not required to be made if the customer is given example key features, provided that disclosure of remuneration or commission is made within five business days of effecting the transaction.[83]

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[76] Ibid, ¶¶6.6.54R – 6.6.57R ff.
[77] Ibid, ¶6.5.38R.
[78] Ibid, ¶5.7.2G.
[79] Ibid, ¶5.7.3R.
[80] Ibid, ¶5.7.4G.
[81] See also COB, ¶5.7.13G.
[82] COB, ¶5.7.5R(2).
[83] Ibid, ¶5.7.10R.

A specimen table, extracted from ¶6.6.79G, is reproduced below; note the inclusion of a deductions summary, and also the assumed annual return of 6%. COB stipulates rates of return for various products for the preparation of projections. It is conceded that it is difficult to ascertain how the figures in the specimen were derived; as a result, COB provides (at ¶6.6.77G) the detailed parameters for the resultant lengthy calculation (see **Appendix UK-1**).

At end of year	Investment to date £	Income to date £	Effect of deductions to date £	What you might get back £
1	6,000	148	470	5,740
3	6,000	451	715	5,940
5	6,000	766	998	6,150
10	6,000	1,600	1,890	6,720

The last line in the table shows that over 10 years the effect of total charges and expenses could amount to £1,890.
Putting it another way, this would have the same effect as bringing the illustrated investment growth from 6.0% a year down to 3.7% a year.

Stakeholder Pension Schemes

The key features for a SPS must broadly follow those for a scheme,[84] however there is an additional requirement to provide *decision trees*,[85] or at least the tree relevant to the particular investor.[86] COB does not expand greatly upon what a decision tree actually is, but it does say that there are three versions of the tree, one for each of employed, self-employed and unemployed persons.[87] The trees themselves say that they "provide information and help you to answer the question: 'Would a stakeholder pension be a good choice for me as part of my financial planning for retirement?'".

Subject to modifications to accommodate the firm's corporate image, its marketing material or any interactive mechanisms involved in the delivery of the trees,[88] firms are required to "reproduce the text, content and format" set out in the annex to COB.[89] A sample tree from the annex is reproduced here for reference:[90]

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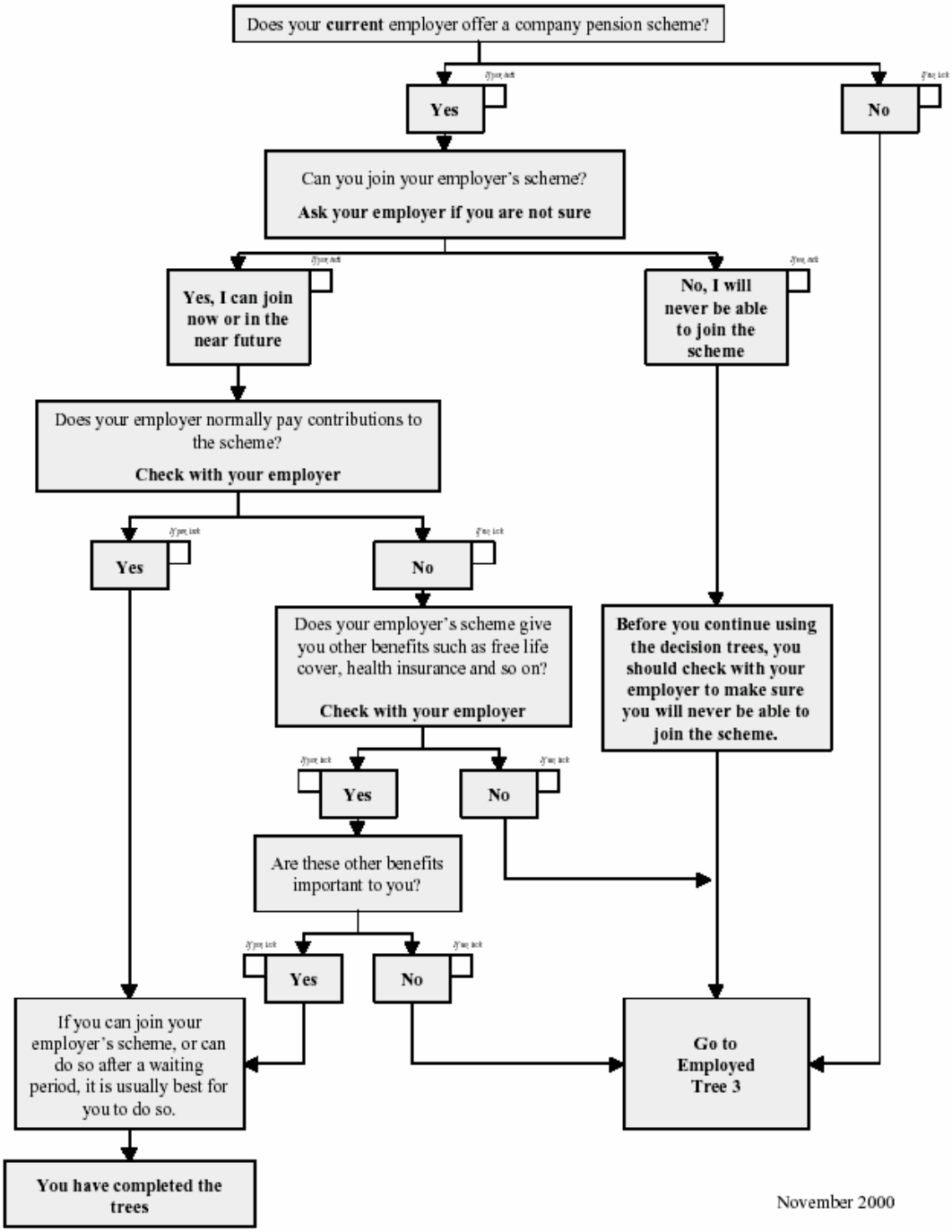
[84] Ibid, ¶6.5.2R(5)(a).
[85] Ibid, ¶6.5.2R(5)(b).
[86] Ibid, ¶6.5.6R.
[87] Ibid, ¶6.5.7G.
[88] Ibid, ¶6.5.9R.
[89] Ibid, ¶6.5.8R.
[90] Trees 1 and 4 have been omitted here for ease of reference.

Annex 1

The decision tree is intended to help you make your own choice about your pension arrangements. It does not give you financial or professional advice and you should not regard it as doing so. You should get help if you require advice.

Employed Tree 2 – No current pension



November 2000

Annex 1

The decision tree is intended to help you make your own choice about your pension arrangements. It does not give you financial or professional advice and you should not regard it as doing so. You should get help if you require advice.

Employed Tree 3 – How much should I save towards a pension?

THIS IS AN IMPORTANT DECISION

Most people save every month. It is better if you can keep up your monthly contributions.

The following table shows the **estimated monthly pension,** at today's prices, that you would get for different **regular monthly contributions**. The contribution shown is assumed to **increase each year in line with inflation**. The government will also add tax rebates to increase the actual amounts paid into your stakeholder pension (although all tax breaks are subject to change). The estimated pension figures include this tax rebate. When you retire, your pension will increase in line with inflation.

Remember: these estimates are not guaranteed - you could get more or less than the amounts shown.
A stakeholder pension would be on top of any State pensions you are entitled to.

The table gives you an idea of how much you need to pay now - as a regular monthly contribution - to receive the monthly pension you want when you retire. First look down the left-hand column to find the age closest to your age now. Then look across to find the monthly contribution you want to pay and the age at which you want to retire.

Your approximate age now	What you pay per month for the first year (tax rebates will be added to this amount)							
	£20		£50		£100		£200	
	Initial monthly pension if you retire at 65	Initial monthly pension if you retire at 60	Initial monthly pension if you retire at 65	Initial monthly pension if you retire at 60	Initial monthly pension if you retire at 65	Initial monthly pension if you retire at 60	Initial monthly pension if you retire at 65	Initial monthly pension if you retire at 60
20	£154	£108	£386	£272	£772	£544	£1,544	£1,089
25	£124	£86	£310	£215	£620	£431	£1,240	£863
30	£98	£67	£245	£168	£491	£336	£983	£672
35	£76	£50	£191	£127	£382	£254	£765	£509
40	£57	£37	£144	£92	£289	£185	£579	£371
45	£42	£25	£105	£63	£211	£127	£422	£254
50	£28	£15	£72	£38	£144	£77	£289	£155
55	£17	£7	£44	£17	£88	£35	£176	£71
60	£8		£20		£40		£81	

Have you found the level of monthly pension that you need in the table and can you afford the monthly contribution?

If yes, tick

Yes, I've found the pension I need and can afford the monthly contribution

Consider starting a stakeholder pension.

If in doubt seek help from an expert adviser. See Employed Tree 4 for details.

You have completed the trees

If no, tick

No, I can't find the pension I need or I can't afford the contribution

For details of where to get further help, Go to Employed Tree 4

Nov 2000

An example: it has been seen that a projection is required to be provided in relation to the acquisition of a scheme interest – COB does not require a projection in relation to the acquisition of an SPS:

> Where the proposed transaction is for a stakeholder pension scheme, a specimen projection will have been included in the decision tree. There is no requirement in these rules for a personalised projection in the key features for a stakeholder pension scheme.[91]

COB section 6.6 makes explicit the exception in relation to trees:

> The rules in COB 6.6 do not apply to a firm when it provides a projection…contained in a decision tree as specified in COB 6.5.8.[92]

Given that it is possible to nevertheless provide a projection in relation to an SPS, COB section 6.6 defines the charges that are to be accounted for in an SPS projection:

> For stakeholder pension schemes, charges are all explicit charges and expenses for the underlying policy or contract, including any charges levied by the manager or trustees of the stakeholder pension scheme.[93]

Tables: likewise, COB does not require that the tables and deductions summaries for schemes be provided in relation to SPSs:

> COB 6.5.37 outlines a simplified illustration of charges for stakeholder pension schemes. There is no requirement for the tables of figures or the reduction in yield summary required for…schemes.[94]

Para 6.5.37R states that the following statement must appear beneath or within the information as to the SPS' description:

> "There is an annual charge of [y]% of the value of the funds you accumulate. If your fund is valued at £500 throughout the year, this means we deduct [£500 x y/100] that year. If your fund is valued at £7500 throughout the year, we will deduct [£7500 x y/100] that year."[95]

---

[91] COB, ¶6.5.17G. The guidance provides that where an investor requests a personalised projection in addition to the tree, the projection is to be given in accordance with the rules discussed earlier in relation to schemes.
[92] Ibid, ¶6.6.5R(5).
[93] Ibid, ¶6.6.24G.
[94] Ibid, ¶6.5.22G.
[95] Ibid, ¶6.5.37R(2).

Presently, the charge denoted as [y] is capped at 1%:

> Providers of stakeholder pensions usually charge for managing your money. There is an upper limit on this charge. The limit is 1% of the value of your fund each year. The charge is taken from your fund. So if your fund is worth £5,000, a 1% charge would be £50.[96]

The preamble within the decision tree repeats this statement. Unless investors read more-widely or get more-detailed advice, they could be forgiven for thinking that the 1% charge is the only charge they will face – the FSA's *Guide to Saving for Retirement* says as follows:

> Management charges are capped at 1% of the value of your pension fund each year. As well as 1%, the law allows pension providers to recover costs and charges they have to pay for certain other things.[97]

Commission and remuneration: disclosure of adviser commission and remuneration in key features for an SPS is the same as for a scheme.[98]

Collective Investment Schemes

As previously indicated,[99] CIS applies to ICVCs and AUTs, the latter of which are also subject to COB. AUTs therefore must meet the requirements to provide key features pursuant to COB plus any other requirements imposed by CIS, the most relevant being the obligation to provide a prospectus, as ICVCs and managers of AUTs cannot market or sell fund units until a prospectus has been provided to a prospective investor.[100]

The Prospectus

"A prospectus must contain the matters specified in CIS 3.5 (Information to be contained in the prospectus)".[101] CIS section 3.5 sets out, in tabular form, the statements required to be contained in the prospectus. The following summary shows how fees, charges, expenses and costs must be disclosed in the prospectus, cross-referenced to governing provisions elsewhere in CIS.

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[96] FSA, above n 45, 7.
[97] FSA, *Guide to Saving for Retirement – Starting to Save* (January 2002), 22.
[98] Ibid, ¶6.5.38R; see above n 77 and text thereto.
[99] Above nn 49-54 and text thereto.
[100] CIS, ¶3.2.2R.

- Payments to the authorised fund manager[102] – item 12: the prospectus must explain payments out of scheme property to the authorised fund manager, whether being for manager's remuneration or reimbursement for expenses. In relation to remuneration, each category thereof must separately disclose the maximum and current rates or amounts of such remuneration[103] and how it will be calculated;[104] reimbursable expenses need only be set out.[105]
- Other payments out of scheme property – item 13: this contemplates a number of different types of payment, the most relevant of which are:
  - Any remuneration paid out of scheme property to an *affected person* (but not the depositary or any third party): an "affected person" includes the manager and trustee of an AUT.[106] The prospectus would therefore disclose any "manager's periodic charge" (which is the only payment by way of remuneration that a manager may receive from scheme property)[107] and/or a trustee's remuneration or properly-incurred reimbursable expenses.[108] The former appears to require disclosure in the form of a percentage,[109] the latter either by actual amount, rate or method of determination.[110]
  - The types of any other charges or expenses that may be taken out of scheme property: this would appear to encompass the long list of miscellaneous costs described in CIS ¶8.5.5R(1), such as broker's commission,[111] property maintenance[112] and audit fees.[113] There does not appear to be any requirement that the amount or rate of these charges and expenses be disclosed.

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[101] Ibid, ¶3.2.1R(1).
[102] An *authorised fund manager* is either an authorised corporate director of an ICVC or a manager of anAUT: FSA Glossary, 12.
[103] CIS, ¶8.2.3R(2).
[104] Ibid, ¶8.2.3R(1).
[105] Ibid, ¶8.2.3R.
[106] FSA Glossary, 5.
[107] CIS, ¶8.5.1R(1).
[108] Ibid, ¶8.5.4R(1)(a).
[109] Ibid, ¶8.5.1R(4)(a).
[110] Ibid, ¶8.5.4R(1)(a)(i).
[111] Ibid, ¶8.5.5R(1)(a).
[112] Ibid, ¶8.5.5R(1)(d).
[113] Ibid, ¶8.5.5R(1)(g).

- Preliminary charges – item 21: in addition to the current rate or amount of these charges, the prospectus must also set out the maximum amount, expressed either as a fixed amount or percentage of the issue price.[114]
- Redemption charges – item 22: the prospectus must disclose the amount of any redemption charge or, if it is variable, the rate or method of arriving at it. CIS ¶8.2.7R(2) applies to ICVCs, while CIS ¶8.5.2R(2) applies to AUTs.
- Umbrella scheme exchange charges – item 24(1)(d): For brevity, an *umbrella scheme* is a scheme in which a number of funds share a core of common features, each fund however being a discrete and separate fund in its own right. Investors may transfer their monies between funds within the umbrella.[115] Such exchange charges are probably most akin to switching charges. CIS imposes a cap on exchange charges: they must not exceed the aggregate of the fee payable on switching and any excess over preliminary charges already paid.[116]

CONSUMER RESEARCH AND PRICE COMPETITION

Much the same can be said about the UK experience on consumer awareness as has been said about Australia: many investors either do not understand or do not read the information disclosed to them in key features documents ("**KFDs**"):

> [A] programme of research (published separately) shows that most consumers do not use KFDs for shopping around. Many consumers do not read KFDs, or only skim them; and those who do read KFDs often have difficulty understanding the material and in some cases misunderstand it.[117]

The recent UK Sandler Report has also noted that: "Surveys of investor knowledge consistently show that retail investors do not understand how disclosed charges affect net returns: Ron Sandler, *Medium and Long-Term Retail Savings in the UK: A Review*, Report Prepared for the UK Government, July 2002, para 7.24. The Sandler Report also states that:

> The difficulties consumers have in understanding charges are not simply due to lack of financial knowledge. Disclosure practices in the savings industry make it very hard to compare the price of financial services offered by different companies. (Ibid, para 7.25)

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[114] See also CIS ¶8.2.2R(2)(b).
[115] FSA Glossary, 151.
[116] CIS, ¶8.2.8R(1).
[117] FSA, above n 63, ¶5.

The intentions of the UK disclosure regime were far more utilitarian than simply increasing issuers' compliance burden:

> The specific objectives of the product disclosure regime when it was introduced were:
>
> - To facilitate comparisons between products, encouraging consumers to shop around and thereby promoting competition
> - To give consumers the information about a product and its charges needed to make informed decisions about whether or not to buy.[118]

The conclusion to be drawn from this UK research is that although consumers can be provided with abundant information, they cannot be forced to make use of it. Even where the information is explained in very simplistic terms, there may be an innate reluctance on the part of consumers to make an effort to utilise the information:

> The FSA's research suggests that the regime has been less successful in informing individual consumers' decision-making and that, in practice, KFDs themselves rarely form part of the process of shopping around.[119]

The research also found that the documents were not particularly successful in conveying the information to consumers, for two main reasons:

> - Consumer (un)willingness to read the material: The research found that most consumers provided with Key Features Documents either do not read them, or only skim them briefly.
> - Consumer understanding of the material: Where consumers do read their KFD, the research found that they have difficulty understanding the contents. The research found that less confident consumers are likely to stop reading if an unfamiliar term is encountered and that some consumers misinterpreted information contained in the KFD or personal illustration.[120]

This is not to suggest that, in this initial familiarisation phase of the product cycle, disclosure should be adjusted to the lowest common denominator:

> There is an argument that disclosure should be aimed at the least able and experienced consumers of financial products. …[W]e do not think that it would serve any group of consumers well to 'dumb down' the information at the expense of clarity or precision. Conversely we are not persuaded by the claims that

[118] Ibid, ¶19.
[119] Ibid, ¶28.
[120] Ibid, ¶29.

> the target market for some packaged products…is sufficiently better informed or more financially literate to warrant more complex or detailed material…[121]

Be that as it may, the mere fact of disclosure itself seems to encourage price-competition among product-issuers, and thereby achieve at least the first of the regime's objectives:

> Since 1995 the PIA has published an annual Disclosure Report which tracks trends in product charges. These have shown that the introduction of the regime and its emphasis on charges appears to have acted as a catalyst for driving down the cost of products and facilitating market entry of new firms competing on price.[122]

COMPARATIVE INFORMATION TABLES

The FSA's preliminary view at the end of 2000 was that Comparative Information Tables would help to achieve its objectives of encouraging competition and providing sufficient information to assist decision-making.[123] The FSA explains:

> Publication of authoritative Comparative Tables should improve the efficiency of the market for financial services. It should be of direct benefit to retail consumers who are able to make use of the information to shop around and get a better or more appropriate deal. And it should have a wider market benefit by illuminating the extent to which products of the same type offer better or worse value for money to the consumer.[124]

The Tables (which are delivered via the FSA's website)[125] provide comparative information, on the basis of some preliminary investment details provided by the investor, in respect of products available in the UK market. The Tables do not display information as to risk and return,[126] but do display charges and deductions.

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[121] Ibid, ¶103.
[122] Ibid, ¶26. The PIA (Personal Investment Authority) was a predecessor to the FSA.
[123] Ibid, ¶48.
[124] FSA, *Response to Consultation Paper 28: Comparative Information for Financial Services* (Response Paper, June 2000), ¶1.2.
[125] http://www.fsa.gov.uk/tables/index.jsp.
[126] FSA, above n 124, ¶¶6.31-6.34.

This is the welcome page to the Tables:

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FSA COMPARATIVE TABLES from the Financial Services Authority

Welcome to the Financial Services Authority's Comparative Tables.

If you're shopping around for financial services, we can help.

Who are we?
We, the FSA, are the independent watchdog set up by the government to regulate financial services and protect your rights.

What are Comparative Tables?
The tables compare similar products available from various providers. So, for example, if you're looking to buy an ISA, our tables will help you decide which ones to look at.

Currently we have tables for pensions, unit trust ISAs, investment bonds and endowments. Tables for mortgages and other products will be added in the future, so do come back.

What are they for?
The tables won't recommend which financial product you should buy, so never buy a product just based on what you see in the tables.

Use the tables to select, say, half a dozen products and then get more detailed information or specific quotes from the provider or an authorised financial adviser.

Some warnings!
If you don't understand how the kind of product you're looking for works, or if you're not sure whether it's suitable for you, then get advice before coming back to the tables.

The tables are updated every working day and are as accurate as we can make them. But this is a complex, fast-moving market and we cannot guarantee that the data is 100% correct. You should always check the details with the provider or an adviser before deciding to buy.

Each table covers the vast majority of products on the market, but participation is voluntary and some providers may prefer not to show their products in the tables.

The terms and conditions for using the Comparative Tables are not the same as those for the rest of our website. They are available through a link at the bottom of each page.

Where can I find out more?
If you would like more information on financial services and products our 'Consumer Help' website can help you. Consumer Help and links to other websites can be found under 'useful links' at the bottom of each page.

Choose a route to take you to the Comparative Tables

Guided route This will ask you some questions about you and the product you're looking for, before showing you a table.

Fast track If you know exactly what you're looking for, this will get you to the right table faster.

Rules for professionals and publishers
If you want to use the tables in a professional capacity, or you want to publish the information they contain, then special terms and conditions apply. Your use of the Comparative Tables is subject to those terms and conditions. They are available through a link at the bottom of each page.

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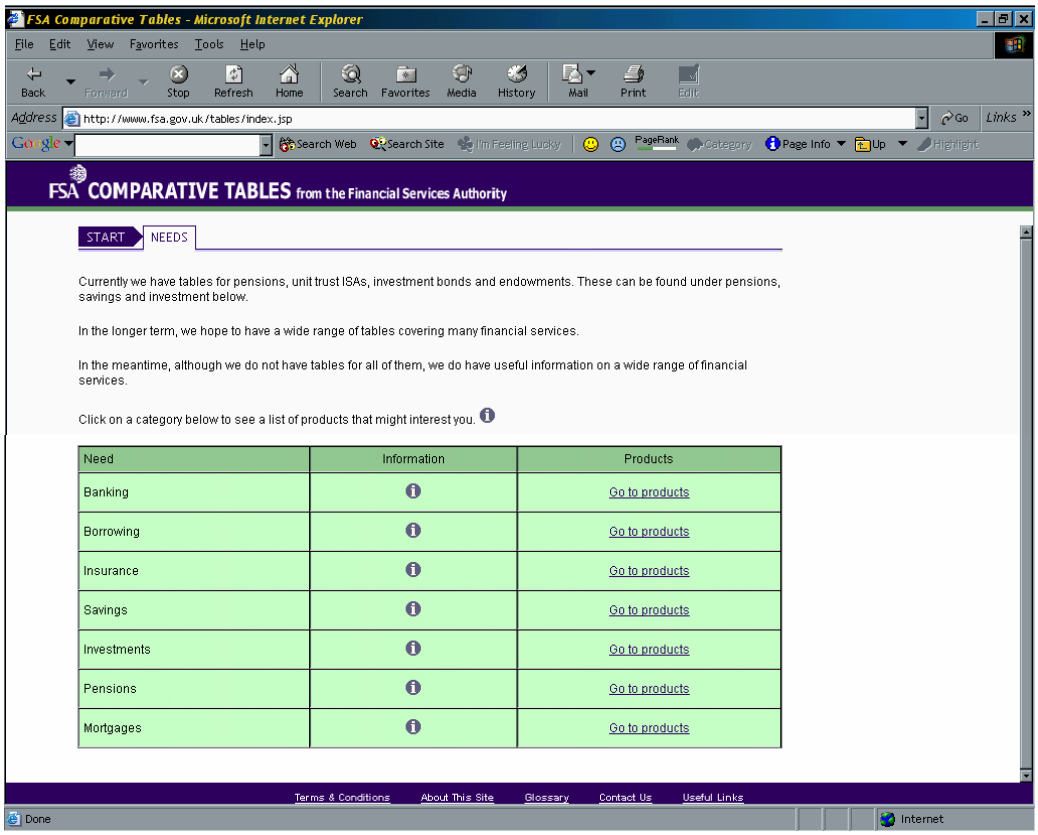
Done Internet

After scrolling through the preliminary information, the Tables require the user to select the appropriate category of product for computation:



The Tables then describe the information that is not included within them…

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Address http://www.fsa.gov.uk/tables/index.jsp

FSA COMPARATIVE TABLES from the Financial Services Authority

START NEEDS INVESTMENTS UNIT TRUST ISAS

What's not in the Comparative Tables?

The tables you are about to see give you some useful information to help you compare the price of different unit trust ISAs (including OEICs), together with some other relevant factors.

But they do not tell you everything you might want to know. This page highlights some other things you might want to bear in mind.

Choice of funds

The tables only include funds in the six largest of the fund sectors defined by the Association of Unit Trust and Investment Funds (AUTIF). There are other fund sectors, covering other funds that specialise in different countries, or different kinds of investment.

More about AUTIF fund sectors

Smaller and specialist providers

Smaller and specialist providers are not listed in the tables unless they ask to be. But they might still be able to offer you the sort of product you are looking for.

Non-participating providers

Some providers have chosen not to have their details listed in the tables, even though they are significant players in the market.

Non-participating providers

Discounts, special offers and 'fund supermarkets'

Sometimes, discounts or special offers are available from product providers, advisers, brokers or 'fund supermarkets'. The tables show special offers where possible, but we cannot show the full range of discounts that you might be able to get.

Past investment performance

The return you will receive depends on investment performance in the future, which is not known by anyone - not even the provider. Many people use the relative past investment performance of funds to help them choose where to invest, hoping that it will repeat. Our research suggests that this information is not very useful. More about past performance

Risk and return

Investment risk is a very personal thing. What you consider very risky may be an acceptable risk for someone else hoping to get a better return. As it's very difficult to quantify accurately, we have not been able to include anything about it in the tables.

More about risk and return

Investment strategy

The investment strategy of the fund manager may be important to you, but it is almost impossible to describe in a table.

More about investment strategy

Using an ISA to pay off your mortgage

You might be thinking of using an ISA to help pay off a mortgage, but there are also other ways of doing this.

More about repaying your mortgage

Your Personal Circumstances

We do not know your personal circumstances, whether you can afford these investments, whether you need them, or whether something else might be better for you.

Consider your own circumstances, get more detailed information from the product providers or an adviser, and seek professional advice if you need it. Do not rely on these tables alone.

Continue

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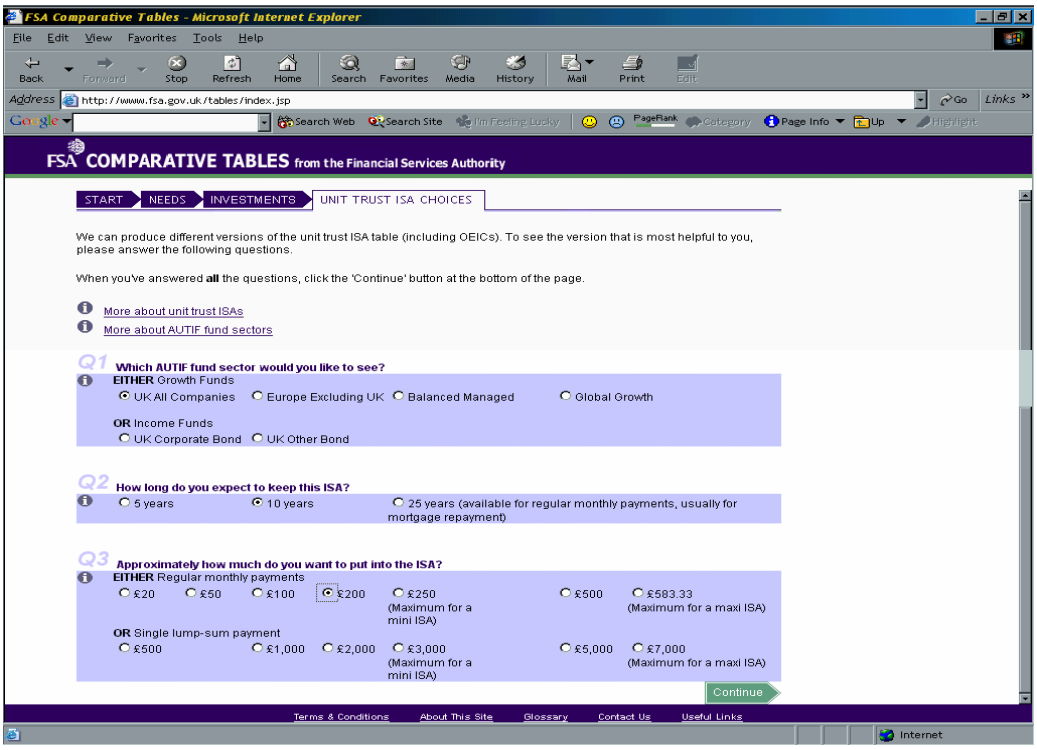
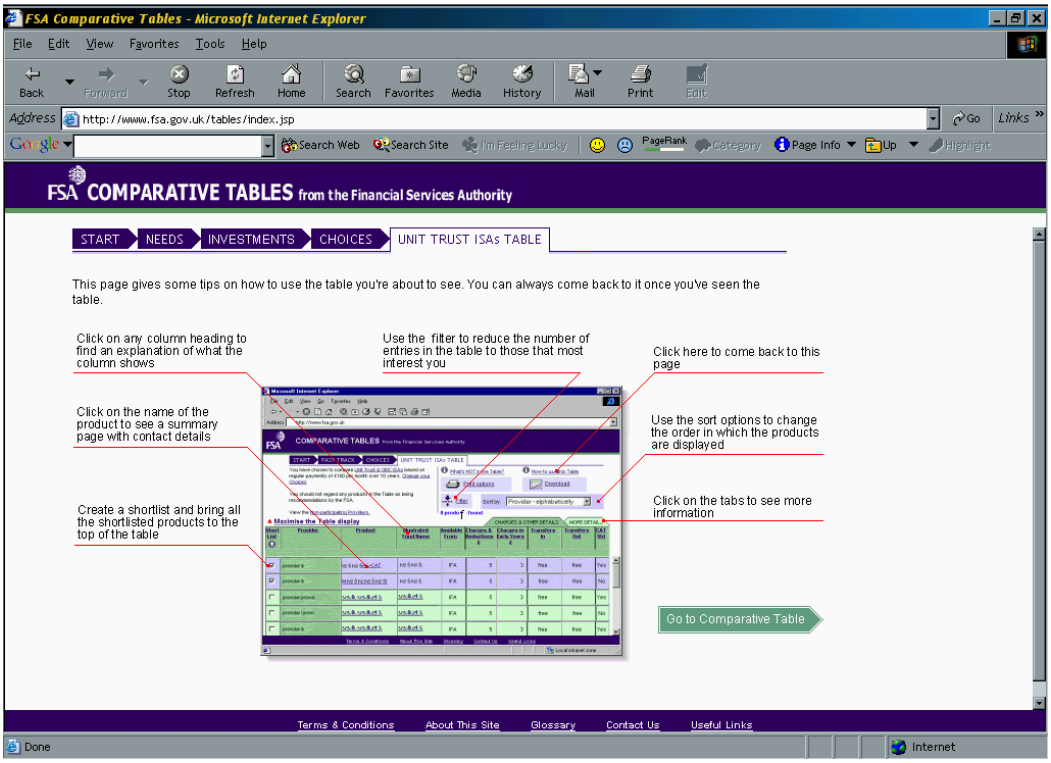
Internet

before proceeding to the input screen where investors enter the information which best fits their own circumstances:



An explanatory screen then highlights key components of the computed Table:



And the finished Table looks like this:

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FSA COMPARATIVE TABLES from the Financial Services Authority

START NEEDS INVESTMENTS CHOICES UNIT TRUST ISAs TABLE

You have chosen to compare unit trust and OEIC ISAs from the UK All Companies AUTIF fund sector based on regular payments of £200 per month over 10 years. Change your choices

You should not regard any of the products in the table as being recommendations by the FSA.
View the non-participating providers.

What's NOT in the table? How to use this table

Print options Download

Filter Sort by: Provider - alphabetically

241 products found.

Maximise the table display

CHARGES & OTHER DETAILS MORE DETAILS

Short List	Provider	Product name	Illustrated fund	Available from	Charges & deductions £	Charges in early years £	Transfers in	Transfers out	CAT std
These products are not FSA recommendations. Always confirm the product details with the provider or an adviser.									
☐	Abbey National	Investment ISA	Stockmarket Tracker Fund	Direct	666	44	Standard charges	Free	Yes
☐	Abbey National	Investment ISA	UK Growth Fund	Direct	3,690	553	Standard charges	Free	No
☐	Aberdeen	ISA	UK Growth Unit Trust	Direct, IFA	3,930	586	Discounted charges	Free	No
☐	Aberdeen	ISA	UK Blue Chip Unit Trust	Direct, IFA	3,820	564	Discounted charges	Free	No
☐	Aberdeen	ISA	UK Mid Cap Unit Trust	Direct, IFA	3,950	588	Discounted charges	Free	No
☐	ABN AMRO Fund Mgrs Ltd	Unit Trust ISA	UK Growth Fund	Direct, IFA	4,450	654	Standard charges	Free	No

The information in this table was last revised on: 09/04/2002

The filters you applied were:

Filter	Option Chosen
Fund type	Show all
Charges & deductions	Show all
Charges in early years	Show all
Maxi or mini	Show all
CAT standard	Show all

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The Tables explain the charge and deduction information as follows:[127]

> **Charges and deductions**
> The provider will charge you for the services they offer. This reduces how much you will get back.
>
> This column shows you the effect of these deductions over 5, 10 or 25 years (depending on your choice).
>
> Effectively, this is the 'price' of the ISA.
>
> Assuming that you pay the amount you have chosen for the period you have chosen, and assuming that the fund manager achieves a standard growth rate of 7% each year, then this column shows the effect of those charges and deductions on the value of your fund. The amount you would get back would be reduced by this amount.
>
> This figure just shows the effects of explicit charges and deductions. The actual amount you get back will also depend on how efficiently the fund is run and whether the fund achieves more or less than the 7% a year we have used in this example.
>
> These calculations also assume that the government extends the period of availability for ISAs to cover the full 5, 10 or 25 year period of the illustration.
>
> If you want to, you can sort this column from cheapest to most expensive, and then filter out the more expensive products.[128]

[127] Click on the appropriate column heading for an explanatory pop-up console window.
[128] ISAs are explained earlier; see above n 56.

The charges and deduction information illustrates the "effect" over time of the charges and deductions (5, 10 or 25 years) assuming a standard growth rate of 7%,

The Comparative Tables approach does rely upon consumers making the effort to find the Tables on-line and use them correctly. However, the FSA's view is that "[c]onsumer testing revealed that users expected this sort of approach from a neutral authoritative source like the FSA".[129]

CRITICISM OF THE UK APPROACH

Underlying Dealing Costs

It is not clear why, in the preparation of projections for KFDs, dealing costs of the underlying portfolio are not included in the deductions calculations for AUTs[130] but are included for ITSSs.[131] Not only does this import inter-product inconsistency, it is at odds with the guidance note for AUT charge and expense disclosure which states: "Charges and expenses…means 'all explicit charges and expenses, and includes all other deductions and expenses which will or may bear upon the fund'".[132] It is entirely possible that a product provider offering essentially-similar AUT and ITSS products would, for the same costings and accountings, be permitted to provide wholly-different projections in KFDs on the basis of this differential treatment of underlying dealing costs.

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[129] FSA, *Comparative Tables* (Bulletin Number 1, May 2001), ¶3.11.
[130] COB, ¶6.6.67G.
[131] Ibid, ¶6.6.72G(2)(b). See also COB, ¶6.6.23R, which applies to projection calculations for schemes generally, thus adding further to the confusion.
[132] Ibid, ¶6.6.65G(1).

The FSA "[acknowledges] the difficulties of including dealing costs and other hidden charges but, in the interests of transparency and greater efficiency would ideally like to extend the price measure to include them".[133] This comment was made in respect of the pricing information provided in the Comparative Tables, but it can also be applied more generally to KFDs and projections.

Projection Calculations

A specimen table was reproduced earlier,[134] and attention was drawn to the complex and technical calculation required to derive the table. The following criticisms should be noted:

- The specimen projection is difficult to understand: while investors focussing on the 'What you might get back' column should be able to readily identify the bottom-line figure, it is far more difficult attempting to resolve, by means of the table alone, how that figure is derived. This is despite the summary comments at the foot of the table.
- The calculation is difficult to understand: attempting to reverse-engineer the table via the provided calculation is even more problematic.
- It is accordingly difficult to determine, via the table alone, whether the product is internally efficient compared to other products: itemisation of fees and charges is not accommodated within this methodology.
- Discretion as to expression - £ or %: COB and CIS extend to providers significant latitude in terms of how deductions may be presented. The potential for confusion and obfuscation is not overly remote, considering that a virtually-identical product offered by two different providers would convey vastly different impressions as to their fees and charges were one product to be presented in percentages and the other in pounds.

Given the increasing importance of retirement saving, investors need to be aware of how products work, and that means understanding the impact of fees and charges from both a comparative and an efficiency perspective. The FSA projection model does not permit these comparisons to be made. (The same comments may be made, with appropriate modification, in respect of the decision trees for SPSs.)

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[133] FSA, above n 63, ¶98.
[134] Above, under the heading "Content of Key Features".

Appendix UK-1

FSA Handbook: Conduct of Business ¶6.6.77G
Parameters for the calculation of specimen projection table
for preparation of key features documents

The parameters

(1) Contract details: *unit trust* for a term of 10 years with a single *investment* of £6,000 (SP).

(2) Distributions: at the rate of 2.4% per annum, distributed as 1.2% of the offer value at the end of each half year.

(3) Charges:

(a) initial charge of 3% of *investment* (IC);

(b) fund management charge of 1/12 of 1.25% per month (FMC) on distribution *units*;

(c) attributable expenses of 1/12 of 0.25% per month (AE);

(d) investment spread of 3% (IS) making total bid/offer spread of 6%.

(4) Calculation:

(a) investment of £6,000 (SP) less (IC+IS) giving an initial bid value of £5,640

(b) interest of 6% pa or 0.4868% per month less (FMC + AE) = 1.004868 x (1- 0.015/12) – 1 = 0.3612% per month

(c) the value after 10 years as shown in ■ COB 6.6.79 is £6,720

(d) the internal rate of return necessary to generate £6,720 plus distributions over 120 months from an initial investment of £6,000 is 0.3030% per month or 3.7% per annum

(e) one method of creating the table is to use 20 periods of six months, each of which end with the payment of a distribution.

(f) after 6 months:

(i) the bid value of the fund before the distribution is 6000 x 0.94 x (1.003612)^6 = £5,763

(ii) the distribution is 0.012 x 5763/0.94 = £73

(iii) the fund carried forward is 5763 - 73 = £5,690

(iv) after the end of Year 1, that is, after the second 6 months

(v) the bid value of the fund before the distribution is 5690 x (1.003612)^6 = £5,814

(vi) the distribution is 0.012 x 5814/0.94 = £74

(vii) the fund carried forward is 5814 - 74 = £5,740

(viii) this bid value is disclosed as there is no exit penalty as 'what you might get back'.

(g) the 'effect of deductions' is calculated from the accumulation of the *investment* with no allowance for charges and expenses but with allowance for income:

(i) the accumulated fund after 1 year with no allowance for charges is [6000 x (1.004868)^6 - 73] x (1.004868)^6 - 74 = £6,210

(ii) the 'effect of deductions' is this figure less 'what you might get back', that is, £6,210 - £5,740 = £470

(h) this process is continued throughout the term of the table; after 10 years, the accumulated investment at 0.4868% per month with no allowance for charges and expenses but with allowance for the same distributions of income is £8,621; 'What you might get back' is £6,723 so 'effect of deductions' is the difference or £1,898;

(i) the deduction in *investment* return is determined by calculating the rate of interest which accumulates the *investment* with no allowance for charges and expenses but with allowance for income to £6,723; this is 0.3030% per month (0.4868% per month gives £8,621); the yearly rate is (1.00303)^12 - 1 or 3.7%.

NEW ZEALAND

Like Australia, the New Zealand approach to regulation of investment-linked financial products is manifested in the form of statutory and regulatory provisions. The Securities Act 1978 (as amended) ("**the Act**") regulates the offering of securities and the Securities Regulations 1983 (as amended) ("**the Regulations**") made thereunder provide for the content of disclosure documents in relation to the offering of securities.

Securities are defined by s 2D(1) of the Act to mean:

> any interest or right to participate in any capital, assets, earnings, royalties, or other property of any person, and includes –
>
> (a) An equity security; and
>
> (b) A debt security; and
>
> (c) A unit in a unit trust, and
>
> (d) An interest in a superannuation scheme; and
>
> (e) A life insurance policy; and
>
> (f) Any interest or right that is declared by regulations to be a security for the purposes of this Act…

The governing provision is s 33 of the Act which relates to restrictions on the offer of securities to the public:

> (1) No security shall be offered to the public for subscription, by or on behalf of an issuer; unless –
>
> (a) The offer is made in, or accompanied by, an authorised advertisement that is an investment statement that complies with this Act and regulations; or
>
> …
>
> (c) The offer is made in, or accompanied by a registered prospectus that complies with this Act and regulations.

Investment statements provide to prospective investors key information about securities in summary form in respect of offers for subscription thereof and also serve as a promotional document seeking to develop a prospective investor's interest in the investments.

Registered prospectuses are mandatory for the issue of publicly-offered securities: s 37(1) prohibits and makes void the allotment of publicly-offered securities unless, at the time of allotment, a prospectus had been registered in respect of the securities

sought to be offered. Where an allotment is sought to be made to a subscriber who did not receive an investment statement, s 37A(3) merely makes that allotment voidable on written notice from the subscriber to the issuer within a prescribed period. Effectively, the combined operation of ss 37(1) and 37A(3) means that product issuers will produce a prospectus for registration with the New Zealand Securities Commission but will distribute investment statements both to generate publicity for the product and to satisfy the requirement that investors be given key investment information at the outset.

DISCLOSURE DOCUMENTS

Registered Prospectuses

Clause 3 of the Regulations signposts the relevant provisions therein which make provision for the contents of prospectuses. While s 33(1) requires a prospectus to be registered in respect of the offering of every class of security within s 2D(1), this section of the international review is confined to the following securities and their respective requirements:

- Participatory Securities – reg 3(3): Third Schedule to the Regulations.
- Unit Trusts – reg 3(4): Schedule 3A to the Regulations.
- Superannuation Schemes – reg 3(6): Schedule 3C to the Regulations.

The detailed requirements in respect of each product type will be covered later in this section. In general, the prospectus requirements in respect of each product type are similar although there are some key differences. It should be noted at this point that registered prospectuses are not as comprehensive as investment statements in respect of the disclosure of fees and charges. As the requirements in respect of investment statements are uniform regardless of product type, it is useful to describe and comment upon investment statements before examining the discrete differences displayed in prospectuses relating to various product types.

Investment Statements

The definition, purpose and form and content of investment statements are provided by ss 38C-E of the Act. Section 38C provides that an investment statement is a written document that:

> (a) Contains or refers to one or more offers of securities to the public for subscription; and
> (b) States that it is an investment statement for the purposes of this Act.

Section 38D provides that the purpose of such statements is to:

> (a) Provide certain key information that is likely to assist a prudent but non-expert person to decide whether or not to subscribe for securities; and
> (b) Bring to the attention of such a person the fact that other important information about the securities is available to that person in other documents.

Section 38E states that the investment statement must be in writing, dated and refer to the registered prospectus in respect of the securities being offered by the investment statement.[135] Section 38E also requires the statement to contain all the information required by the Regulations. In that regard, Schedule 3D to the Regulations stipulates the matters required to be included in investment statements. Key information is presented to consumers in the form of headings phrased as rhetorical questions directed to significant matters which consumers should be asking themselves in relation to the investment (indeed, in relation to any investment). The questions are:

> What sort of investment is this?
> Who is involved in providing it for me?
> How much do I pay?
> What are the charges?
> What returns will I get?
> What are my risks?
> Can the investment be altered?
> How do I cash in my investment?
> Who do I contact with enquiries about my investment?
> Is there anyone to whom I can complain if I have problems with the investment?
> What other information can I obtain about this investment?[136]

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[135] This is because the investment statement serves as a form of advertisement authorised by s 38 of the Act.

[136] Securities Regulations 1983, Schedule 3D (amended 1997).

In respect of the question "What are the charges?", the statement must disclose the following:

7. Types of charges

(1) A statement as to which of the following types of charges are or may be payable to the issuer or promoter, or an associated person of the issuer or promoter, or (if there is a scheme) the scheme, by a subscriber (whether directly or indirectly, including by deduction):

(a) Entry charges:

(b) Trustee, administration, or management charges:

(c) Expenses or overhead charges:

(d) Charges or expenses relating to goods or services that the subscriber is required to obtain:

(e) Early termination charges:

(f) Switching or sale charges (including the difference between any buying and selling prices for the securities):

(g) Alteration charges:

(h) Other charges.

(2) A statement as to which of the types of charges specified in subclause (1) are or may be payable by the issuer or, if there is a scheme, from the scheme to a promoter or administration manager or investment manager or an associated person of the issuer or the promoter or the administration manager or the investment manager, being charges that will or may affect the amount of the returns to subscribers.

(3) A brief description of any practices of the issuer or any associated person in relation to charges that will or may affect the amount of the returns to subscribers.

(4) A brief description of the rights of the issuer or any other person to alter any of the charges applicable to the securities.

Note the potential for overlap in items (1)(b) and (c): this potential is due to the breadth of application of "expenses or overhead charges" which, on another analysis, might be subsumed within "administration" or "management" charges. Note also that the regime requires disclosure of which of the charges paid by investors will be paid by the issuer or scheme to promoters, administrators or managers, where such charges will impact upon the return to investors. Subclause (3), in relation to practices in respect of charges which may affect returns, could be taken to include rebate and waiver practices inuring to the benefit of the investor.

The charges information must also provide information as to quantum:

8. Amount of charges

(1) If a charge, or the minimum or maximum amount of a charge, referred to in clause 7(1) can, at the date of the investment statement, be expressed as a dollar amount (or as a percentage of another

> dollar amount), a statement of the dollar amount (or of the percentage and a description of the other dollar amount).
>
> (2) If a charge, or the minimum or maximum amount of a charge, referred to in clause 7(1) cannot, at the date of the investment statement, be expressed as a dollar amount (or as a percentage of another dollar amount), a statement describing how the charge will be calculated and what procedure is available to the subscriber to ascertain the amount at the time of, and following, the subscription.

Clause 8 requires, broadly, that issuers describe the "cost" of an issue to investors, and if that "cost" cannot be quantified (presumably in the case of a new issue where, for example, there is no historical financial information upon which to base the requisite charge), then at least investors will receive information as to how that quantification will occur and how they can go about obtaining that information upon or following their investment. However, there appears to be discretion within that broad provision as follows:

- No stipulation as to precision: the issuer may provide the amount of the charge, or its minimum or maximum. There is no guidance as to when precise amounts are required and when a range of amounts would be appropriate.
- Choice between dollar or percentage expression: the provision draws no qualitative distinction between the two forms of expression. It would be open to issuers to quantify a readily-ascertainable fee by convoluted reference to a percentage of some other amount, such other amount only required to be given by way of "description": presumably this is a reference to another variable (for example, average fund balance) which is presently unascertainable and therefore amenable only to mere qualitative description.

PRODUCTS COVERED AND PROSPECTUS REQUIREMENTS

Participatory Securities – Third Schedule

Section 2 of the Act and cl. 2 of the Regulations define *participatory securities* as any security other than an equity security, a debt security, a unit in a unit trust, an interest in a superannuation scheme or a life insurance policy. According to one treatise:

> This negative definition hardly does justice to the wide-ranging investment schemes, interests in which are classified as participatory securities. The schemes that may be the subject of participatory securities are various: forestry ventures, racing syndicates, film syndicates, retirement villages, to name a few.

> Some schemes for certain types of participatory security, such as contributory mortgages and group investment funds, have their own legislation that merits their being given special attention.[137]

A prospectus for participatory securities is required to disclose the following fee, charge and expense information:

- Management expenses: cl. 6 of the Third Schedule requires a prospectus to contain a financial statement in summary form (and in tabular form if practicable). Clause 6(3) in particular requires these statements to include amounts in respect of management expenses:

  > (a) In respect of each of the 5 consecutive accounting periods preceding the date of the statement of financial position contained or referred to in the registered prospectus, and…for the period from the end of the last accounting period to the date of the interim statement of financial position.

  The amount of the manager's remuneration is also required to be disclosed in the prospectus by cl. 32(d) as part of the statements of financial performance for the most recently completed accounting period.
- Promoters' interests: cl. 14(2) requires disclosure of the particulars of the amount of remuneration a promoter is entitled to receive for services in respect of the participatory scheme.
- Issue expenses: cl. 17 requires the following disclosure:

  > Particulars of any issue expenses, including –
  > (a) Their amount or estimated amount, and
  > (b) In respect of any commission payable, –
  > (i) The rate of commission; and
  > (ii) The persons or classes of persons to whom the commission is payable.

<u>Group Investment Funds</u>

According to the *Laws of New Zealand*, an interest in a group investment fund is a participatory security as it fits none of the other definitions of security in s 2 of the

[137] *Laws of New Zealand*, ¶105 "Shares and Securities: Nature of Participatory Securities".

Act.[138] The *Laws of New Zealand* describes group investment funds in the following way: [139]

> A group investment fund is a fund that may only be set up by a trustee company or the Public Trust Office….The purposes of the fund is to provide for pooling and investment of trust funds under the control of the trustee organisation. Funds lodged with a trustee organisation by a person who appoints the trustee organisation to act as its agent or attorney may be invested in a group investment fund administered by that organisation.[140]

Unit Trusts – Schedule 3A

The *Laws of New Zealand* provides the following short summary of unit trusts and their position within the Securities Act regime:

> Unit trusts may be classified as "open-ended" or "closed-ended". A closed-ended unit trust is one in which the number of units is fixed so that to all intents and purposes it operates as a company with a prescribed number of shares on issue. A unit trust of this kind may be listed on the Stock Exchange, and the units traded at the price set by the market. On the other hand, units in an open-ended unit trust fluctuate in accordance with the constant inflow and outflow of funds and the valuations of the assets, and since they contain a right for the unit holder to require the manager to buy back the holder's units at a pre-determined price, they are not traded on the open market. Open-ended unit trusts are known as mutual funds.[141]

A prospectus for units in a unit trust is required to disclose the following fee, charge and expense information:

- Investment, management and other expenses: cl. 6 of Schedule 3A requires a prospectus to contain a financial statement in summary form (and in tabular form if practicable). Clause 6(3) in particular requires these statements to include amounts in respect of investment, management and other expenses in respect of both the reporting period relating to the most recent financial statements complying with and registered under the Financial Reporting Act 1993 and the four consecutive preceding periods.
- Interested persons: cl. 11 requires disclosure of the particulars of remuneration or reimbursement of expenses of the unit trustee, manager, administration

[138] Ibid, ¶666 "Shares and Securities: Group Investment Funds under the Securities Act 1978".
[139] Ibid, ¶667 "Shares and Securities: Nature of a Group Investment Fund".
[140] Citations omitted.

manager, investment manager, custodian or promoter. If the remuneration or reimbursement is from the unit trust, the prospectus must also disclose whether or not this is limited and, if so, to what extent.

- Issue expenses: cl. 14 requires the following disclosure:

> Particulars of any issue expenses, including –
>
> (a) Their amount or estimated amount, and
>
> (b) In respect of any commission payable, –
>
> (i) The rate of commission; and
>
> (ii) The persons or classes of persons to whom the commission is payable.

Superannuation Schemes – Schedule 3C

Leaving aside "small employer superannuation schemes" (the total assets of which must not exceed $5 million),[142] and which are exempted from the requirement to register a prospectus but which must provide an investment statement to prospective members in order to avoid invalidation of an issue,[143] superannuation schemes must comply with the following prospectus requirements in respect of fee and charge disclosure:

- Investment, management and other expenses: cl. 5 of Schedule 3C requires a prospectus to contain a financial statement in summary form (and in tabular form if practicable). Clause 5(3) in particular requires these statements to include amounts in respect of investment, management and other expenses in respect of both the reporting period relating to the most recent financial statements complying with and registered under the Financial Reporting Act 1993 and the four consecutive preceding periods. The accounting for management expenses is required to include any amounts related to "general administration and trustees' remuneration".
- Interested persons: cl. 8 requires disclosure of the particulars of remuneration or reimbursement of expenses of the superannuation trustee, administration manager, investment manager, custodian or promoter. If the remuneration or reimbursement is from the superannuation scheme, the prospectus must also disclose whether or not this is limited and, if so, to what extent.

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[141] *Laws of New Zealand*, ¶50 "Shares and Securities: Closed and Open-ended Unit Trusts".
[142] Securities Regulations 1983, cl. 2C.

In addition to these disclosures in the prospectus, the Superannuation Schemes Act 1989 requires each prospective member of a superannuation scheme to be advised in writing of "the charges or fees (if any) that the members may have to pay in addition to contributions"[144] and be given a copy of the most recent annual report of the trustees.[145] To clarify the position between the two Acts governing disclosure in respect of superannuation, the Government of New Zealand amended the Superannuation Schemes Act in 1996 to obviate the need to require disclosure under that Act where a prospective investor is provided with an investment statement.[146] In sum, then, superannuation funds of any size must make disclosure under s 16 of the Superannuation Schemes Act unless they make disclosure within an investment statement. Larger funds (that is, funds which are not "small employer" funds) are also required to register a prospectus and comply with the prospectus regime.

COMMISSIONS

In addition to the disclosure required by the Regulations,[147] s 4(1) of the Investment Advisers (Disclosure) Act 1996 requires investment advisers to disclose:

> (e) Whether or not the adviser or an associated person has, or will or may have, a direct or indirect pecuniary or other interest in giving investment advice to the investor (being an interest that is reasonably likely to influence the adviser in giving the advice) and, if so, the nature of that interest:
>
> (f) Without limiting paragraph (e) of this subsection, if the adviser or an associated person has received, or will or may receive, -
>
> (i) Directly or indirectly, from a person (other than the investor); and
>
> (ii) In connection with the giving of the investment advice or a transaction resulting from the giving of the advice, -
>
> remuneration that is reasonably likely to influence the adviser in giving the advice, the nature and (to the extent practicable) the amount or rate of the remuneration, and the name of the person from whom the remuneration has been, or will or may be received.

The requirement to so disclose is only in relation to such of the above information that has not already been disclosed (whether in writing, to an investor's electronic address,

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[143] Securities Act 1978, s 5(2E).
[144] Superannuation Schemes Act 1989, s 16(1)(a)(ii).
[145] Ibid, s 16(1)(b).
[146] Ibid, s 16(2).

or by way of broadcast),[148] and then only within five working days of a request by the investor of the adviser.[149]

INVESTMENT STATEMENT EXTRACTS

Following are some extracts from actual investment statements. The reproduction of the extracts is not intended either as an endorsement or a criticism of the investment statements, the products or their issuers or persons associated with either the products or the issuers or the preparation and/or publication of the investment statements. The extracts are presented to illustrate disclosure of fees and charges under the New Zealand regime.

The first extract is from the *AXA New Zealand Investment Funds & Professionally Managed Trusts* investment statement dated 20 December 2000. The relevant extracts are pages 6 and 7 which disclose the fee and charge information applying generally to all the products contained in the investment statement.

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[147] Securities Regulations 1983, Third Schedule, cl. 17; Schedule 3A, cl. 14; Schedule 3D, cl. 7(2).
[148] Investment Advisers (Disclosure) Act 1996, s 5.
[149] Ibid, s 4.

What Are The Charges?

	Entry Fee	Exit Fee(1)	Annual Management Fee p.a.	Trustee Fee p.a.
New Zealand Investment Funds				
AXA Cash Management Fund	Nil	Nil	0.9125%	0.0765%
AXA Mortgage Backed Fund	2.0%	1.5%	1.25%	0.0765%
Professionally Managed Trusts (2)				
AXA Mortgage Income Trust	1.5%	1.5%	1.5%	0.10%
AXA Balanced Growth Trust	5.0%	Nil	1.5%	0.10%
AXA New Zealand Selected Equities Trust	5.0%	Nil	1.5%	0.10%
AXA Global Equities Trust	5.0%	Nil	1.75%	0.10%

Note *(1) Of amount withdrawn within the first twelve months of investment.*
(2) The Trustee's fee shall reduce to 0.075 % p.a. in respect of a Professionally Managed Trust in the instance detailed below.

The Manager, in conjunction with the relevant Trustee, reserves the right to vary any of the fees referred to in the above table. Investors will receive three months' notice of any alteration affecting their existing investment.

Entry Fees

In most cases an entry fee is payable to gain entry into the Funds. This fee is paid in part or in full to your financial adviser as commission.

With one exception, entry fees are deducted from your initial investment and any additions (including regular contributions). The exception is the AXA Mortgage Income Trust where the entry fee is deducted from your first quarter's distribution (and that of subsequent quarter's if necessary).

No entry fee is charged for investments in the AXA Cash Management Fund.

Exit Fees

The withdrawal of your funds may give rise to the payment of an exit fee. This fee applies only to certain Funds in the following circumstances -

AXA Mortgage Backed Fund
AXA Mortgage Income Trust

Investors who elect to withdraw part or all of their investment within the first twelve months will be charged a fee of 1.5% calculated on the amount withdrawn.

Annual Management Fee

The annual management fees specified above are payable to the Manager for the on-going administration of your investment. The costs of investment management are paid by the Manager out of these fees. In respect of the Funds, the Manager may contract out certain services to, or have arrangements with, related companies. The Manager pays for such services from the annual management fees charged in relation to the relevant Funds.

Annual management charges are calculated daily as a percentage of, in the case of the New Zealand Investment Funds the current capital value of the units in the Fund and in the case of the Professionally Managed Trusts the total gross investments of the Fund, and are deducted from the Fund.

Trustee's Fee

The Trustee's fee in respect of the New Zealand Investment Funds is calculated daily as a percentage of that Fund's current capital value.

The Trustee's fee in respect of the Professionally Managed Trusts is calculated daily as a percentage of the total gross investments of all the Professionally Managed Trusts. The Trustee's fee will reduce to 0.075% p.a. on each dollar by which the total gross investments of all the Professionally Managed Trusts exceeds $100 million. This fee is apportioned between the Professionally Managed Trusts in proportion to their respective total gross investments, and the relevant amounts are deducted from those Funds.

Switching Fees

You are able to switch your investment to other Funds in this Investment Statement providing they are on offer at the time you elect to make the switch. Switches will be treated as a withdrawal and an application.

You are entitled to make two free switches per year. Thereafter, a switching fee of 0.5% is payable on the amount switched, up to a maximum of $500 per switch.

There are circumstances in which a switch may attract an entry or exit fee, as specified below -

- In the case of the AXA Mortgage Backed Fund and AXA Mortgage Income Trust, in addition to the switching fee, the exit fee of 1.5% will apply to amounts switched within the first twelve months of investment.
- At all times AXA Cash Management Fund investors, instead of the switching fee, are required to pay the respective entry fee of the Fund(s) switched to, calculated on the amount switched.

The Manager may, at its discretion, waive or rebate any of the above charges for any particular investor (including the respective Trustee's Fee where its consent has been obtained).

Goods and Services Tax may be charged on any of the above fees if applicable.

Other Charges

The Manager and the relevant Trustee are entitled to deduct from or be reimbursed out of, a Fund for any costs, disbursements, charges or expenses in accordance with the trust deed governing the Fund. These may include expenses directly attributable to the administration and operation of the relevant Fund, such as audit, registry and legal fees, the cost of holding investor meetings and other expenses properly and reasonably incurred by the Manager or the Trustee for that Fund in carrying out their respective duties.

The Manager may levy, at the same or at differing levels, investor(s) balances to meet expenses of the relevant Fund including administration expenses, costs of making investment adjustments and payment of fees due to the Manager and the Trustee for that Fund.

The Manager may charge investors an administration fee, as determined by the Manager in respect of each contribution being part of a Regular Savings Programme. As at the date of this Investment Statement the Manager does not charge this fee, but reserves the right to do so at any time.

State Street Fees

Fees are paid to State Street Australia Limited ("State Street") for providing settlement services in respect of the AXA Global Equities Trust. These fees are paid from that Fund. These fees are currently in line with the bulk rate made available to NMFM's parent company and will vary in the same manner as those fees vary. The Trustee and State Street may also agree to vary the fees at any time. Investors will receive three month's notice of any increase. These fees currently comprise (all dollar references in (a) - (c) below are in Australian Dollars):

(a) an account fee of $3,500 per annum;

(b) a master custody services fee based on the aggregate value of the assets in respect of which State Street provides services, and which are managed by NMFM or its parent company. The fee is determined by taking the aggregate of 0.06% per annum of the first $1 billion of the value of such assets and 0.04% per annum on any value of such assets over $1 billion. The fee payable to State Street in respect of the AXA Global Equities Trust is a portion of that aggregate amount, based on the proportion that the value of the AXA Global Equities Trust's assets bears to the value of such total assets; and

(c) between $15 and $100 in respect of each transfer settled by State Street of assets in or out of the Fund and $15 for each notice of corporate action forwarded by State Street.

State Street will also be reimbursed from the Fund for any trade related expenses in relation to the services it provides to the Trustee in respect of the AXA Global Equities Trust.

The next extracts are from the *Tower Managed Funds New Zealand Investing* investment statement dated 14 January 2002. The extracts have been edited for ease of presentation.

Firstly, the specific disclosure in respect of the "New Zealand Equity Trust" product:

Unit Trust – Growth Fund

INVEST 7+ YEARS

New Zealand Equity Trust

This Fund invests in a high quality portfolio of listed New Zealand company shares. It is managed by TOWER Asset Management Limited. The objective of this Fund is to achieve investment growth by selecting New Zealand companies with strong earnings potential over the medium to long term. It is actively managed with an aim to outperform the NZSE40 Index over time.

The MER for this Fund for the year ended 31 March 2001 was 1.28% net of tax.

Value of $10,000
invested since inception (30/11/85)

The chart above assumes reinvestment of all distributions. The growth is net of fees and tax, but no entry fee has been taken into account. Investors are reminded that past performance is not a guarantee or indicator of future returns.

Next, the disclosure in respect of fees and charges as applying to all the products in the investment statement generally, including a fee table:

What are the charges?

The following fees for each fund are set out in the table on the following page.

Entry fee

Each fund, except FirstRate, has an entry fee which is deducted from your initial and each subsequent investment. This fee is agreed between you and your financial adviser and is paid to him or her as commission. There is no entry fee for FirstRate. However, you may be charged transaction fees (more details below).

Exit fee

There are no exit fees on any of the funds, except for TOWER MortgagePlus. Investments withdrawn from this Fund within one year of deposit will be subject to a fee of 1% that reduces incrementally to zero over the 12-month period. This fee will be paid to the Fund. The fee can be waived by the Trustee in special circumstances. There is a 30-day notice period for withdrawing funds from MortgagePlus (ie. on your request, funds will be paid to your account 30 days later). The Trustee may reduce this notice period at its absolute discretion. The minimum investment timeframe in TOWER PropertyPlus is two years and the investment is automatically renewed for a further two years unless a withdrawal notice is received within one month of the notice of maturity being issued. However, monies may be withdrawn on three months' notice but only where reasonable causes can be demonstrated. The Trustee has the right to charge a penalty for this, but it is not currently charged. If charged this fee will be paid to the Fund.

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Management fee

This fee is paid to TOWER Managed Funds. From this fee, the Manager pays the costs of investment management, service brokerage to your financial adviser and any custody costs. This fee is deducted from the gross asset value of each Unit Trust and from the distributable income of the GIFs.

Trustee fee

The fee for trustee services is deducted from the gross asset value of each Unit Trust and from the distributable income of the GIFs.

Transaction fee (FirstRate only)

FirstRate is a cash management account, not a current account. Multiple transactions (including withdrawals, or payment by means other than cheque or Direct Debit) are therefore discouraged. You may make up to three transactions per quarter free of charge, then a $5 per transaction fee may apply. The transaction fees are paid to TOWER Managed Funds.

The transaction fee will also apply to FirstRate foreign currency transactions and switching. This is in addition to the foreign currency transaction fee which may apply to any withdrawal, investment, or switch to or from a Foreign Currency Account. This foreign currency transaction fee covers any bank charge, which will be a maximum of NZ$25. The charge will be deducted from your account.

Switching fee

No fee is charged on the first two switches between any of our funds in any 12-month period. If investors switch more than twice in a 12-month period, a fee of 1% of the value switched may be applied for each subsequent switch. The exit fee for TOWER MortgagePlus and any transaction fees payable on FirstRate still apply. Switching funds is subject to maintaining minimum account balances in each fund. The switching fee is paid to TOWER Managed Funds.

Other fees and expenses

The manager may also charge expenses incurred in managing the funds, such as audit, registry, administration and legal fees to the fund/s. These additional charges are deducted from each fund before the declaration of the fund's unit prices or rates of return. These additional charges and fees are incorporated in the Management Expense Ratio (MER) for each fund, which is the total amount of fees and expenses charged to a fund, expressed as a percentage of the average fund size net of tax. By investing in a fund, investors accept and authorise these deductions and fees to occur and understand that these fees can be altered. The amount of fees and expenses charged for the previous financial year is disclosed in the financial statements of the funds.

Investors must receive three months' notice before any fees can be increased for any of the funds in this Investment Statement (for FirstRate, the Trustee's fee may be increased on giving one month's notice). In most circumstances any increase will need to be agreed to between the Trustee and TOWER Managed Funds Investments.

The fees for each fund are shown in the table below.

All fees are stated on a GST exclusive basis. Under current law some fees are wholly or partially exempt from GST. If GST is payable on any of the fees, then the GST component would be payable in addition to the fee stated. From January 2002 GST (at 12.5%) will be charged on 10% of management fees. GST may be payable in the future on trustee and other fees, or at a greater rate on management fees.

LIST OF FEES

	Entry Fee	Exit Fee	Management Fee (gross)	Trustee Fee
TOWER FirstRate Account	Nil (1)	Nil (1)	Up to 1.15%	0.05% (2)
TOWER MortgagePlus	Up to 1.50%	Up to 1% for 1 year (3)	0.975%	0.05% (2)
TOWER BondPlus	Up to 1.50%	Nil	1.25%	Up to 0.07%
TOWER Multi Sector	Up to 5.50%	Nil	1.75%	Up to 0.07%
TOWER PropertyPlus	Up to 5.00%	Nil	1.00%	0.05% (2)
TOWER NZ Equity	Up to 5.50%	Nil	1.50%	Up to 0.07%
TORTIS-New Zealand	Up to 5.50%	Nil	0.75%	Up to 0.07%

(1) Transaction fees may apply. See under 'What are the charges?' for details.
(2) Or a minimum of $7,500 p.a., payable out of the distributable income of the fund. For these funds, the Trustee Fee is paid out of the Management Fee.
(3) Investments withdrawn within one year of deposit will be subject to a withdrawal fee of 1% that incrementally reduces to zero over the 12-month period.

The final extract is from the *Bank of New Zealand Managed Funds* investment statement dated 21 December 2001.

Firstly, the extract in respect of the "BNZ International Equity Trust" product:

BNZ International Equity Trust

Designed to provide an exposure to an actively managed portfolio of selected international shares

Who is the investment manager?

Franklin Templeton Investments was selected to sub-manage this Trust following extensive research and analysis of the world's leading international equity managers. They have been one of the pioneers of a global, value style of share investing, and have an enviable track record of consistent performance.

What is the investment manager's approach?

The investment manager invests the Trust's assets in a portfolio of companies from around the world that, based on thorough research, are viewed as being under-valued.

The investment manager uses a world wide network of experienced research resources to identify the best investment opportunities. Information is examined on a company by company basis in a range of countries and industries. Companies are selected if they are expected to produce the strongest returns over time. Under normal circumstances, the Trust's currency exposure will be unhedged.

Over the recommended minimum investment period, this investment approach provides the potential for strong capital gains.

What are the risks associated with this approach?

Investing in unhedged international shares carries a medium/high degree of risk that the value of your investment may fall, particularly in the short term. In exchange for seeking a strong, long term return from an exposure to international shares, there is likely to be a medium/high degree of fluctuation in the value of your investment.

How long should I be invested for?

Because of the medium/high risk of short term fluctuations in the value of your investment, this Trust is suitable for you if you are looking to invest for seven years or more.

What are the fees and costs?

Entry fee: 5.0% is deducted from the value of each contribution made.

Management fee: 1.50% p.a. of the Trust's average daily gross asset value plus GST (please refer to page 11).

Trustee fee: 0.08% p.a. of the Trust's average daily gross asset value.

Switching fee: Nil, as contributions have already had the highest Bank of New Zealand Managed Fund's entry fee deducted.

Important Fund Information as at 30 November 2001

Fund Size

$168.85 million

Top 20 Company Holdings

(may vary from time to time)

Holding	Country	Exposure
Mylan Laboratories	USA	2.02%
Cheung Kong Holdings	Hong Kong	1.88%
Unilever NV cva	Netherlands	1.73%
Abbott Labs Com	USA	1.72%
Hewlett Packard Ltd	USA	1.66%
Merck KGAA	Germany	1.37%
Mattel Inc	USA	1.35%
Samsung Electronics	Korea	1.31%
Eni Spa	Italy	1.28%
Torchmark Corp	USA	1.24%
SBC Communications	USA	1.24%
Swiss Reinsurance	Switzerland	1.22%
Pharmacia Corp	USA	1.18%
Adidas-Salomon AG	Germany	1.15%
Akzo Nobel NV	Netherlands	1.15%
Newell Rubbermaid	USA	1.13%
Nomura Securities Co	Japan	1.13%
Worldcom Inc	USA	1.12%
Cable & Wireless	UK	1.11%
Jabil Circuit Inc	USA	1.10%
Other		64.66%
Sub Total		**91.75%**
Cash		8.25%
Total		**100.00%**

Net Investment Returns

(after management fees and tax)

Last 1 Year	-5.04%
Last 3 Years	8.77% p.a.
Last 5 Years	12.25% p.a.
Last 10 Years	8.59% p.a.
Since Inception (Sept 1987)	7.88% p.a.

Growth of $10,000

Invested since inception of the Trust in Sept 1987

For an explanation of how the 'Net Investment Returns' and 'Growth of $10,000' graph are calculated, please refer to Question 9 on page 14.

Fund Summary

Assets invested in:	International shares
Potential Return Variability:	Medium/High
Potential Returns:	Strong capital growth
Recommended Minimum Investment Period:	7 years

The Management Expense Ratio ("MER")

Year Ended	MER
March 1999	1.183%
March 2000	1.164%
March 2001	1.158%

For an explanation of what the MER measures and how it is calculated, please refer to Question 6 on page 12.

The following fee and charge information is provided in respect of the products in the investment statement generally. The extracts have been edited for presentation:

5. What are the charges?

The charges vary between Trusts. They are as follows:

- **BNZ New Zealand Cash Management Trust**

Entry Fee	Nil.
Management Fee	0.75% p.a. of the Trust's average daily gross asset value plus GST.
Trustee Fee	0.08% p.a. of the Trust's average daily gross asset value.
Switching Fee	The switching fee will be equivalent to the entry fee for the Trust to which the switch is made.

- **BNZ New Zealand Strategic Bond Trust**

Entry Fee	3.0% of the amount of each contribution made.
Management Fee	1.25% p.a. of the Trust's average daily gross asset value plus GST.
Trustee Fee	0.08% p.a. of the Trust's average daily gross asset value.
Switching Fee	A switching fee will only apply where the switch is into a Trust with a higher entry fee, in which case the fee will be the difference between the entry fees.

- **BNZ International Bond Trust**

Entry Fee	3.0% of the amount of each contribution made.
Management Fee	1.25% p.a. of the Trust's average daily gross asset value plus GST.
Trustee Fee	0.08% p.a. of the Trust's average daily gross asset value.
Switching Fee	A switching fee will only apply where the switch is into a Trust with a higher entry fee, in which case the fee will be the difference between the entry fees.

- **BNZ New Zealand Equity Index Trust**

Entry Fee	5.0% of the amount of each contribution made.
Management Fee	0.95% p.a. of the Trust's average daily gross asset value plus GST.
Trustee Fee	0.07% p.a. of the Trust's average daily gross asset value.
Switching Fee	Nil, as contributions have already had the highest Bank of New Zealand Managed Fund's entry fee deducted.

- **BNZ New Zealand Equities Discovery Trust**

Entry Fee	5.0% of the amount of each contribution made.
Management Fee	1.50% p.a. of the Trust's average daily gross asset value plus GST.
Trustee Fee	0.08% p.a. of the Trust's average daily gross asset value.
Switching Fee	Nil, as contributions have already had the highest Bank of New Zealand Managed Fund's entry fee deducted.

- **BNZ International Equity Trust**

Entry Fee	5.0% of the amount of each contribution made.
Management Fee	1.50% p.a. of the Trust's average daily gross asset value plus GST.
Trustee Fee	0.08% p.a. of the Trust's average daily gross asset value.
Switching Fee	Nil, as contributions have already had the highest Bank of New Zealand Managed Fund's entry fee deducted.

Commencing on 1 January 2002 in addition to the management fee, the Manager shall be paid Goods and Services Tax (GST) on 10% of the amount of the management fee payable to the Manager.

Any fees paid to investment managers (i.e., the sub-managers) for the Trusts are paid by the Manager out of its management fee for the relevant Trust.

Other expenses that can be deducted from the Trusts are legal, custodial, auditing, acquisition, registry and other associated costs. The impact of all fees and expenses on the Trusts can be seen in the Management Expense Ratio ("MER" please refer to Question 6 on page 12). The historic MER's for each Trust are listed on the individual Trust pages.

The Trust Deeds governing the Trusts allow the Manager and/or Trustee to vary the current fees from time to time.

In the event that a Trust is terminated, the Trustee is entitled to be paid a fee of 0.5% (or another agreed amount) of the gross asset value of the Trust at the date of termination.

The following information appears later in the investment statement by way of explanation:

> **6. What is the Management Expense Ratio?**
>
> The Management Expense Ratio (MER) measures the total amount that has been charged to each Trust to meet ongoing expenses and is calculated at the end of each Trust's financial year. The MER adds together the annual management fee as well as other associated costs such as audit fees, custodial fees and legal expenses and subtracts the tax deductability of these expenses. The MER is expressed as a percentage of each Trust's average monthly fund size and represents the actual historic costs to investors.

COMMENTARY

The intention of the New Zealand disclosure philosophy is "to enable investors to make their own decisions, not to insulate them from economic risk".[150] The philosophy is partly informed by "the lack of comprehensibility, comparability and information which investors needed in order to make investment decisions",[151] concerns which were raised in 1991-2 by the Government's Task Force on Private Provision for Retirement.

In respect of investment statements, which are the prevalent mode of disclosure, issuers appear to have a discretion as to whether to disclose fees in percentage terms or dollar terms; indeed, if amounts cannot be expressed in either percentage or dollar terms, the issuer is then able to comply by describing how the amount may be calculated.[152] In contrast, disclosure of requisite fees in a prospectus is to be by amount, not percentage, which is possible because the prospectus rules, as have been seen, require inclusion of certain expense information derived from historical financial statements.

Investment statements, however, require disclosure of a greater range and type of fee and charge. Moreover, the investment statement arguably requires disclosure of any

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[150] Peter Fitzsimmons, "Overseas Notes: New Zealand – Investment Statements: Simplified Disclosure Documents for Public Offerings" (1999) 17 *Company & Securities Law Journal* 132.
[151] Ibid.

fee rebate or waiver arrangements and also requires notification of any capacity to alter the charges.[153] The various prospectuses do not require this heightened level of disclosure, although certain amounts which are by way of remuneration or reimbursement to particular persons must be disclosed to investors; presumably this is to assist in the disclosure of commission-like arrangements, especially for superannuation for which there is no specific requirement for the prospectus to disclose any amounts in respect of issue expenses or commission.[154]

The prospectus requires, as a general rule, disclosure of five years' worth of management expenses and, in the case of unit trusts and superannuation, also investment and "other expenses". Presumably the New Zealand Parliament intended "other expenses" to capture a wide range of expenses which were not discretely itemised in the Regulations. The investment statement does not require this historical reporting.

Neither the prospectus nor the investment statement require an illustration or projection (personalised or standardised) to be presented, nor are returns required to be expressed net of fees. Moreover, neither mode of disclosure mandates measures such as OMC or MER (although management expenses must be disclosed). As borne out by the examples, market convention may encourage disclosure of such ratios.

The standard of comprehensibility of investment statements is the "prudent but non-expert investor";[155] in that regard, consumer testing of investment statements has indicated that over 90% of investors felt they could understand the document, while a similar percentage found the document useful.[156] It would appear that the investment statement has, if not achieved its aim, at least gone quite some way towards it, thus making more-accessible the range of investment products to ordinary New Zealand investors who are perhaps put-off by lengthy, technical prospectuses.

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[152] Securities Regulations 1983, Schedule 3D, cl. 8(2).
[153] Securities Regulations 1983, Schedule 3D, cl. 7(4)
[154] Although promoter's remuneration or expenses will need to be disclosed.
[155] Fitzsimmons, above n 150.
[156] Ibid, citing M Wydeveld, "Investors' Opinions on Offer Documents", *New Zealand Securities Commission* (15 January 1999).

CANADA

The Canadian securities market is characterised by jurisdictional differences between the Federal, Provincial and Territorial governments. In respect of some types of financial products (eg: pensions), although there is some regulatory overlap between the Federal and Provincial governments, there are important differences: the Federal government maintains prudential oversight while the Provinces typically maintain operational oversight. The Canadian Constitution provides for this "sharing" of regulation through s 91(2), which grants the Federal government a general power over "trade and commerce", and s 92, which sets out the exclusive powers of the Provinces, in particular s 92(11) which enables Provincial power over "the incorporation of companies with provincial objects".[157]

"Every Canadian province and territory has passed legislation with respect to the regulation of securities. Much of this legislation is similar…".[158]

> The Securities Acts of British Columbia, Alberta, Saskatchewan, Ontario, Nova Scotia and Newfoundland are virtually identical in their regulation of the securities market by the "closed system". Under the closed system, disclosure via a prospectus circulated by the issuing company is not required until such time as the securities are traded outside the closed system.[159]

Despite the stated similarity of securities legislation between the jurisdictions, the differences are such that it is difficult to generalise about securities regulation in Canada.

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[157] Paul Latimer, "Securities Regulation – Canadian Lessons for Australian Regulation" (2001) 13 *Australian Journal of Corporate Law* 206, 208.

[158] Don Tse, "Establishing a Federal Securities Commission" (1994) 58 *Saskatchewan Law Review* 427, 431.

[159] Ibid. Footnote 20 thereto elaborates as follows:

> Trades inside the closed system are generally those where all parties involved are considered not to require the protection of the securities commissions. This lack of a need for protection is measured by various means such as the profession of the parties, the size of the transaction or the relationship of the parties to the issuer.

In that respect, then, the Canadian closed system is similar to the Australian prospectus exemption provisions contained in Corporations Act 2001, s 708, which states that a prospectus is not generally required for issues that are defined as "small scale" or are to "sophisticated investors".

> In Canada, where much of the…regulatory structure is located at the provincial and territorial level and many companies operate in several jurisdictions, the opportunities for regulatory duplication and disharmony are extensive.[160]

As a result of pragmatic concerns deriving from jurisdictional differences, the securities regulators of each Province and Territory have formed an umbrella body known as the Canadian Securities Administrators ("**CSA**") to act as a forum "to coordinate and harmonize regulation of the Canadian capital markets".[161]

> The CSA brings provincial and territorial securities regulators together to share ideas and work at designing policies and regulations that are consistent across the country and ensure the smooth operation of Canada's securities industry. By collaborating on rules, regulations and other programs, the CSA helps avoid duplication of work and streamlines the regulatory process for companies seeking to raise investment capital and others working in the investment industry.

Although there are stated difficulties leading to disharmony and inconsistency in regulation, the CSA's role and effectiveness as a promulgator of consistent regulatory application means that, to a large extent, some generalisation may safely be adopted for this part of the international review. In that regard, the legal and regulatory environment of the Province of Ontario is taken to be representative of Canada.[162] Any special circumstances derogating from that representative characterisation will be covered as they arise.

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[160] Ontario Securities Commission, *A Framework for Market Regulation in Canada: A Concept Paper Prepared for the Canadian Securities Administrators* (February 1999): http://www.osc.gov.on.ca/en/Regulation/Rulemaking/Notices/conceptpro/concept_199902.html, under the sub-heading "Institutional Regulation".

[161] http://www.csa-acvm.ca/html_CSA/about.html, under the sub-heading "What is the CSA?".

[162] A thorough and comprehensive review of the Canadian securities industry would ideally cover each Province and Territory, as well as any Federal provisions. However, it is sufficient for the purposes of this part of the international review to confine the analysis to the Province of Ontario, which is the most important province in the corporate and financial markets. Any generalisations made by virtue of this reliance upon the position in Ontario are qualified to the extent necessary as being largely (but perhaps not entirely) representative of other Provinces or Territories or Canada as a whole. The selection of Ontario as the representative jurisdiction is not unprecedented: the CSA and Canadian Council of Insurance Regulators ("**CCIR**") also chose Ontario as being representative in a 1999 study: Working Group of the CSA and CCIR, *A Comparative Study of Individual Variable Insurance Contracts (Segregated Funds) and Mutual Funds* (7 May 1999), http://www.osc.gov.on.ca/en/About/Publications/segfunds_19990507.html:

> The regulation of mutual funds contained in provincial securities legislation is…largely consistent. For the purposes of [this study] the regulation of mutual funds contained in the Securities Act of Ontario and the regulation made thereunder has been taken as representative. (Citation omitted; at text to note 5 and immediately following.)

COVERAGE

This discussion of Canadian financial products is in two parts. In the first part, brief reference is made to retirement savings products such as superannuation and self-funded retirement plans. In the second part, a more-detailed review is conducted of the regulatory regime governing securities issues, indicating some types of products that are excluded from the regime before turning to mutual funds, which are the focus of this part of the international review.

Canada Pension Plan

The Canada Pension Plan ("**CPP**") is akin to superannuation as it is understood in Australia: a mandatory earnings-related savings scheme funded by contributions drawn from employees' salaries, providing disability and survivor benefits as well as a retirement pension.[163] The CPP is operated by the Canada Pension Plan Investment Board ("**CPPIB**") which is an independent statutory agency established for the sole purpose of investing CPP contributions in accordance with accepted actuarial and prudential guidelines to provide for inter-generational funding of Canadian retirees.[164] The level of contributions collected by the CPP have changed since the programme was introduced:

> When it was introduced, the Canada Pension Plan was designed as a "pay-as-you-go" plan with a reserve fund equivalent to two years of benefits. Under this approach, benefits paid to each generation of current retirees are financed from the contributions of the following generation of contributors. This design is in contrast to a "full-funding" approach in which each generation pre-funds its own benefits.
>
> In 1998, after extensive public consultation, the federal and provincial governments reformed the Canada Pension Plan significantly, and introduced "steady-state financing", which represents a balance between full funding and exclusively "pay-as-you-go" funding. Under "steady-state" financing, the Canada Pension Plan combined employer-employee contribution rate was increased incrementally from 5.6% in 1996, to 9.9% in 2003 and remains constant at 9.9% after 2003.[165]

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[163] See, generally, the website of the Human Resources Development Canada: http://www.hrdc-drhc.gc.ca/isp/cpp/genera_e.shtml.

[164] Canada Pension Plan Investment Board, *Investment Statement*, at 4-5. This document is available from the CPPIB's website at http://www.cppib.ca/, by clicking on the link "Investment Statement".

The CPP does not provide a prospectus or similar initial disclosure document as might be expected with private investments. This is not entirely surprising given that the CPP is mandated by statute and there are very few exceptions to its coverage. As the CPPIB is charged with the responsibility of growing contributors' funds, the CPP is akin to a very large public managed fund, and in that respect, "investors" in the fund are given some indication of the CPPIB's expenses incurred in managing the CPP:

> Total expenses for current fiscal year [ending March 2001] are about 12 cents for every $100 of average assets under management. Investment expenses are less than 3 cents per $100 of assets – substantially below the management expense ratio of mutual funds.[166]

Private Retirement Planning

The CPP may not be sufficient to meet the retirement needs of many Canadians. The alternative is self-funded retirement. The Canadian government assists self-funded retirees through a general scheme of tax effective concessions for federally-regulated private pension plans.[167] There are a large number of alternative private retirement facilities,[168] however it appears that the Registered Retirement Savings Plan ("**RRSP**") is the most popular form of self-funded retirement investment:

> RRSPs are the most popular method of personal savings for retirement, especially if you do not participate in an employer pension plan. RRSPs are individual, personally managed savings plans. Like employer pensions, savings in an RRSP receive tax assistance – contributions are tax deductible and investment income is not taxed as it is earned. The tax is paid when funds are withdrawn from these plans.
>
> RRSP funds may be invested in a range of financial products and investment vehicles, including savings accounts, Canada Savings Bonds, term deposits, guaranteed investment certificates, and mutual funds. You can set up an RRSP through most financial institutions – banks, credit unions, trust companies, mutual fund companies, insurance companies, and investment dealers or brokerage firms. You may set up a regular RRSP or a self-directed one. A self-directed RRSP may hold a wider range of investment vehicles (such as individual stocks) and allows you to directly manage your investments.[169]

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[165] Ibid.
[166] http://www.cppib.ca/, under the link "FAQ", at question 32.
[167] Human Resources Development Canada, *Canada's Retirement Income System: What's In It For You?* (March 2001), at 2 and 13.
[168] See, for example, the products covered in Office of the Superintendent of Financial Institutions, *Pension Guide for Members of Federally Regulated Private Pension Plans* (October 2000).
[169] Human Resources Development Canada, above n 167, 19.

In sum, Canadian retirement is essentially publicly-funded with scope for private involvement through tax-concessionary retirement products. Those concessionary products, like RRSPs, are no more than tax-effective investment vehicles.[170]

DISCLOSURE GENERALLY

Definition of Security

"Security" is broadly defined by the Securities Act RSO 1990 ("**the Act**")[171] to include:

> (f) any agreement under which the interest of the purchaser is valued for purposes of conversion or surrender by reference to the value of a proportionate interest in a specified portfolio of assets, except a contract issued by an insurance company licensed under the *Insurance Act* which provides for payment at maturity of an amount not less than three quarters of the premiums paid by the purchaser for a benefit payable at maturity,
>
> (g) any agreement providing that money received will be repaid or treated as a subscription to shares, stock, units or interests at the option of the recipient or of any person or company,
>
> …
>
> (i) any profit-sharing agreement or certificate,
>
> (n) any investment contract.

These are just a few of the many items included within the statutory definition of "security". The foregoing selections are those that are most like the sort of investments one might expect an investment-linked financial product to offer.

Registration for Trading

Generally, no person or company is permitted to trade in securities unless registered to do so by the Ontario Securities Commission ("**OSC**").[172] "Trade" or "trading" is defined broadly to include the following:

> (a) any sale or disposition of a security for valuable consideration, whether the terms of payment be on margin, instalment or otherwise, but does not include a purchase of a

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[170] http://www.globefund.com/centre/GettingStarted08.html, under the heading "What is an RRSP?".
[171] Securities Act, RSO 1990, c. S-5, s 1(1). RSO means Revised Statutes of Ontario. The legislation is current and consolidated to 5 December 2001.
[172] Securities Act, s 25(1).

security or, except as provided in clause (d), a transfer, pledge or encumbrance of securities for the purpose of giving collateral for a debt made in good faith,

(b) any participation as a trader in any transaction in a security through the facilities of any stock exchange or quotation and trade reporting system,

(c) any receipt by a registrant of an order to buy or sell a security,

(d) any transfer, pledge or encumbrancing of securities of an issuer from the holdings of any person or company or combination of persons or companies described in clause (c) of the definition of "distribution" for the purpose of giving collateral for a debt made in good faith, and

(e) any act, advertisement, solicitation, conduct or negotiation directly or indirectly in furtherance of any of the foregoing.[173]

Section 35 of the Act exempts certain types of trades from any requirements to be registered. Any trades that are not exempted therefore require registration in respect of trading. The importance of registration in respect of trading is borne out later in this part, as it will be seen that conducting trading in non-exempted trades is not permitted unless a prospectus and preliminary prospectus have been filed with the OSC. The trades which are exempted from registration include private mutual funds and prospecting syndicates. It is perhaps useful to discuss briefly these exempted situations (trading in which is not required to be conducted pursuant to a prospectus) before moving on to examine mutual funds in greater detail.

Private Mutual Funds

Trades in the securities of private mutual funds are exempted from registration by s 35(2)(3) of the Act. A private mutual fund is a mutual fund that is:

(a) operated as an investment club, where,

  (i) its shares or units are held by not more than fifty persons and its indebtedness has never been offered to the public,

  (ii) it does not pay or give any remuneration for investment advice or in respect of trades in securities, except normal brokerage fees, and

  (iii) all of its members are required to make contributions in proportion to the shares or units each holds for the purpose of financing its operations, or

(b) administered by a trust corporation registered under the *Loan and Trust Corporations Act* and consists of a common trust fund as defined in section 1 of that Act.[174]

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[173] Ibid, s 1(1).
[174] Ibid.

Prospecting Syndicates

Trades in securities of prospecting syndicates are exempted from registration by s 35(2)(12)-(13) of the Act:

> s 35(2) 12. Securities issued by a prospecting syndicate that has filed a prospecting syndicate agreement under Part XIV for which the Director has issued a receipt, where the securities are sold by the prospector or one of the prospectors who staked claims that belong to or are the subject of a declaration of trust in favour of the prospecting syndicate, and the prospector delivers a copy of the prospecting syndicate agreement to the person or company purchasing the security before accepting payment therefor.
>
> s 35(2) 13. Securities issued by a prospecting syndicate that has filed a prospecting syndicate agreement under Part XIV for which the Director has issued a receipt, if the securities are not offered for sale to the public and are sold to not more than fifty persons or companies.[175]

Section 51(4) expressly prohibits registered dealers from trading in securities of registered prospecting syndicates, either as agent or principal.

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[175] The Part XIV provisions in respect of prospecting syndicates state that, upon the filing with the OSC of a prospecting syndicate agreement and the issuance by the OSC of a receipt, the liability of the members of the syndicate is limited to the extent provided by the terms of the agreement (Securities Act, s 51(1)), where:

(a) the sole purpose of the syndicate is the financing of prospecting expeditions, preliminary mining development, or the acquisition of mining properties, or any combination thereof;

(b) the agreement clearly sets out,

…

(iii) the maximum amount, not exceeding 25 per cent of the sale price, that may be charged or taken by a person or company as commission upon the sale of units in the syndicate,

…

(viii) that the administrative expenditures of the syndicate, including, in addition to any other items, salaries, office expenses, advertising and commissions paid by the syndicate with respect to the sale of its units, shall be limited to one-third of the total amount received by the treasury of the syndicate from the sale of its units,

(ix) that a statement of the receipts and disbursements of the syndicate shall be furnished to the Director and to each member annually,

…

(c) the agreement limits the capital of the syndicate to a sum not exceeding $250,000.

DISCLOSURE BY PROSPECTUS

General Requirements

The Act provides that:

> No person or company shall trade in a security on his, her or its own account or on behalf of any other person or company where such trade would be a distribution of such security, unless a preliminary prospectus and a prospectus have been filed and receipts therefor obtained from the Director.[176]

The requirement to be issued with a receipt for the filing of the prospectus or preliminary prospectus gives effect to a "waiting period": this is defined as the interval, of no less than ten days, between the Director issuing a receipt for the preliminary prospectus and issuing a receipt for the prospectus.[177] During the waiting period, an issuer may distribute advertisements and the like promoting the security provided that the promotional material contains details about how a preliminary prospectus may be obtained, may distribute the preliminary prospectus, and may solicit expressions of interest from prospective purchasers provided they are forwarded a copy of the preliminary prospectus.[178] Although the Act does not explicitly state that no trading in securities shall take place during the waiting period, that would appear to be the effect of s 65 taken together with s 53(1). Once the Director provides the second receipt (in respect of the prospectus), the issuer may commence trading in the securities.

In respect of preliminary prospectuses, s 54(1) of the Act provides that such prospectuses "shall substantially comply with the requirements of Ontario securities law respecting the form and content of a prospectus, except that the report or reports of the auditor or accountant required by the regulations need not be included". In respect of prospectuses other than preliminary prospectuses, the Act provides that they "shall provide full, true and plain disclosure of all material facts relating to the securities

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[176] Ibid, s 53(1). The Director is the Executive Director of the Ontario Securities Commission or a deputy or delegate thereof: s 1(1).
[177] Ibid, s 65(1).
[178] Ibid, s 65(2).

issued or proposed to be distributed and shall comply with the requirements of Ontario securities law".[179]

In the case of an investor who purchases securities without a prospectus, an issuer is obliged to send or deliver to a purchaser a copy of the latest prospectus no later than two days after entering into a sale and purchase agreement resulting from an order or subscription in relation to the securities the subject of the prospectus.[180]

National Instruments

Reference was made earlier to the different jurisdictions in respect of securities regulation across Canada, and the role of the CSA as a collaborative forum for the Provincial regulators. One of the functions of the CSA is the promulgation of National Instruments governing various aspects of securities law and regulation. These Instruments are numerically classified for ease of identification and provide both general guidance in respect of persons, securities or conduct to whom an Instrument applies, as well as specific instruction in respect of rules and regulations governing particular practices and requirements for prescribed forms. The numbering classification system for the Instruments also accommodates Local Instruments promulgated by particular Provincial regulators. Generally, all Instruments are accompanied by a Companion Policy which sets out the reasoning behind the Instrument's requirements, as well as providing additional guidance.[181]

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[179] Ibid, s 56(1). It should be noted that "Ontario securities law" is defined to mean the Act and "the regulations" (s 1(1)), which in turn is defined to mean the regulations made under the Act and, unless the context otherwise indicates, "the rules". "The rules" are defined as rules made under s 143 of the Act and orders, rulings and policies listed in the Schedule to the Act. Thus, prospectuses and preliminary prospectuses must comply with the Act, the regulations, any applicable rules and any orders, rulings and policies.

[180] Ibid, s 71(1).

[181] The Instrument-promulgation regime is premised upon the issuance of Notices which contain the contents of the Proposed Instrument, Forms and Companion Policy. The Notice system provides open consultation upon the contents of the Proposed Instrument, Forms and Policy. Effectively, the proposed material is open to public submission for a short time before the Provincial regulator considers the submissions (if any), issues further Notices in respect of any proposed changes arising out of the consultation process, and, if no other consultative action is required, the regulator then issues a Final Notice advising of the completion of the consultation phase, together with the Final Text of the Instrument, Forms and Policy. See http://www.osc.gov.on.ca/en/Regulation/Rulemaking/Notices/staffnotices/rulemakingOntario_19951020.html, which describes the rule making process in Ontario.

It is essentially up to each Province to decide whether it adopts a National Instrument as a rule within the Province. Once adopted, Instruments and ancillary regulatory apparatus have the force of law within the Province by virtue of s 1(1) of the Act which provides for a broad definition of "Ontario securities law",[182] and ss 143(2)-(3), the latter of which specifically provides that, subject to ministerial approval, the OSC may, concurrently with making a rule, make a regulation that amends or revokes an existing regulation, if necessary to effectively implement the rule. Section 143(1) of the Act provides that the OSC may make rules in respect of 56 various heads of rule-making power covering many aspects of securities regulation. Sections 143.1-143.13 provide the legal mechanism for the adoption of Instruments as Rules, and mandates the publication of proposals for consultation.

Thus, the Provincial regulators have at their disposal a flexible, openly-consultative, discretely-focused rule-making power which is premised upon achieving inter-Provincial regulatory consistency. Although there do not appear to be any overarching requirements that Provincial regulators must be consistent in their regulatory arrangements, a brief examination of some of the Provincial regulators' websites reveals that many of the National Instruments have been adopted by the Provinces, with local modifying Instruments reflective of discrete Provincial concerns.

MUTUAL FUND DISCLOSURE

National Instruments Affecting Mutual Funds

The starting point for regulation of mutual funds by Instrument is *National Instrument 81-102 Mutual Funds* ("**NI 81-102**") and the Companion Policy thereto, NI 81-102CP.[183] NI 81-102 is of general application and regulates prudential, governance and conduct aspects of mutual funds. Specifically, the Instrument applies to:

> (a) a mutual fund that offers or has offered securities under a prospectus or simplified prospectus for so long as the mutual fund remains a reporting issuer; and
> (b) a person or company in respect of activities pertaining to a mutual fund referred to in paragraph (a) or pertaining to the filing of a prospectus to which subsection 3.1(1) applies.[184]

[182] See, above, n 179.
[183] *National Instrument 81-102 Mutual Funds* (2 May 2001, as amended) ("**NI 81-102**").
[184] Ibid, ¶1.2.

The prospectus requirements for mutual funds are found in *National Instrument 81-101 Mutual Fund Prospectus Disclosure* ("**NI 81-101**").[185] NI 81-101 applies only to mutual fund prospectuses. Prospectuses more generally are governed by *National Instrument 41-101 Prospectus Disclosure Requirements* ("**NI 41-101**"). For clarity, *Rule 41-502 Prospectus Requirements for Mutual Funds* (a local rule applying to Ontario) provides that "NI 41-101 does not apply to a simplified prospectus prepared under NI 81-101".[186] In the Companion Policy to the Rule, the OSC:

> notes that the prospectus of a mutual fund that is not permitted to use the simplified prospectus disclosure system of NI 81-101…will be required to comply with Rule 41-501, as that rule applies to Ontario prospectuses generally. An exchange-traded mutual fund would be an example of this type of fund.[187]

Definition of Mutual Fund

According to the CSA:

> A mutual fund is a pool of money that is managed on behalf of investors by a professional money manager. The manager uses the money to buy stocks, bonds or other securities according to specific investment objectives that have been established for the fund. … Mutual funds are '**open-ended**' investment funds, meaning that new investors can contribute money to the fund at any time, and existing investors can return their units or shares to the fund for redemption at any time.[188]

The statutory definition within the Act is as follows:

> "Mutual fund" includes an issuer of securities that entitle the holder to receive on demand, or within a specified period after demand, an amount computed by reference to the value of a proportionate interest in the whole or in a part of the net assets, including a separate fund or trust account, of the issuer of the securities.[189]

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[185] *National Instrument 81-101 Mutual Fund Prospectus Disclosure* (1 February 2000) ("**NI 81-101**"). Amendments to the Instrument have been made since its release but none are presently relevant.
[186] *Rule 41-502 Prospectus Requirements for Mutual Funds* (5 April 2001) ("**Rule 41-502**"), ¶3.3.
[187] Rule 41-502CP, ¶2.7(4).
[188] http://www.csa-acvm.ca/html_CSA/invinfo/mutual_funds.html, under the heading "What is a mutual fund?" (emphasis in original).
[189] Securities Act, s 1(1).

An "issuer" is "a person or company who has outstanding, issues or proposes to issue, a security".[190] A mutual fund is really just an issuer of securities (for which the Act provides many examples) that enables a subscriber to redeem part of the fund's net assets proportionate to the subscriber's interests in the fund. It can be seen that a mutual fund could offer for subscription interests within any of the category of securities defined by the Act.

Simplified Prospectuses

Under NI 81-101, a simplified prospectus ("**SP**") serves as a standard prospectus for the purposes of the securities legislation.[191] The Companion Policy explains the approach behind the simplified prospectus:

> (1) The Instrument contemplates that all investors in a mutual fund will receive a simplified prospectus, which is to be a clear concise document that is designed to provide the typical investor with the necessary information to permit the making of an informed investment decision. The Instrument requires the delivery only of a simplified prospectus to an investor in connection with a purchase, unless the investor also requests delivery of the annual information form, financial statements or both.
>
> (2) The approach of the Instrument is to give investors a choice of the amount of information that they wish to consider before making a decision about investing in the mutual fund. Investors will have the option of purchasing the mutual fund's securities after reviewing the information in the simplified prospectus only or after requesting and reviewing the annual information form, financial statements, or both, incorporated by reference into the simplified prospectus.
>
> (3) The Instrument and Form 81-101F1 (the "SP Form") provide detailed requirements as to the contents and format of a simplified prospectus. These requirements
>
> (a) are designed to ensure that simplified prospectuses are clear, concise, understandable and well-organized, and contain the most important information that an investor would consider in making an investment decision, in order to encourage investors to read and consider the contents of the simplified prospectus;
>
> (b) standardize, to some degree, the order in which information is presented in a simplified prospectus, in order to ensure that investors may easily compare disclosure about one mutual fund with disclosure about other mutual funds in the same or a different simplified prospectus; and

[190] Ibid.

(c) prohibit the addition of information in the simplified prospectus not specifically required by the SP Form, in order to prevent a simplified prospectus from expanding to a size that discourages an investor from reading it, and that obscures the most important information about a mutual fund that should be considered by an investor.[192]

A simplified prospectus is a two-part document:

- Part A: provides introductory information about the mutual fund, general information about mutual funds and information applicable to the mutual funds managed by the mutual fund organisation.
- Part B: contains specific information about the mutual fund.[193]

Most of the requirements in respect of mutual fund prospectuses fall within Part A. For clarity, reference will be made to both Parts of the SP as required in the following analysis.

Disclosure of Various Fees, Charges and Expenses

- Part A, Item 6 – Purchases, switches and redemptions: the Form requires the SP to describe all available purchase options and state any fees and expenses applicable to those purchase options. If any of the purchase options result in variations to dealer compensation, then that fact should be stated. This item is to be cross-referenced to Items 8 and 9.[194]
- Part A, Item 8 – Fees and expenses: the following special features may be noted:

  - Information is presented in summarised tabular form with a prescribed statement.[195] The table distinguishes between the fees and expenses payable by the fund, and the fees and expenses payable directly by the investor. The main components of the fund's operating expenses must

[191] NI 81-101, ¶2.4.
[192] NI 81-101CP, ¶2.2.
[193] NI 81-101CP, ¶4.1(2).
[194] NI 81-101F1, Part A, Item 6(4).

be disclosed,[196] and the fund must also state all fees and expenses payable by it, even if it is expected that the manager will waive or absorb some or all of those fees.[197]

- The table does not state whether fund-payable fees and expenses must be disclosed in dollars or percentages, but it does state that investor-payable sales charges must be disclosed as a percentage, tax plan and "other" fees must be disclosed in dollars, while switch fees and redemption fees may be disclosed in either dollars or percentages.
- Waiver and rebate arrangements are disclosed.[198]
- Under a separate heading ("Impact of Sales Charges"), the SP must include a further table illustrating, at stated time intervals, the amount of fees applicable to the various purchase options availed by the fund.[199] This further table is to be calculated according to stated assumptions, namely that the investor pays the maximum disclosed sales commission[200] and, in the case of a deferred sales charge option where the redemption charge is calculated on the net asset value at the time of redemption, that the annual rate of return of the fund is five percent.[201]

It is convenient to extract (in whole) this Item from the Form, together with the ancillary instructions:

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[195] NI 81-101F1, Part A, Item 8.1(2).
[196] NI 81-101F1, Part A, Item 8.1, instr. (3).
[197] NI 81-101F1, Part A, Item 8.1, instr. (4).
[198] NI 81-101F1, Part A, Item 8.1(5). If the information required by Part A, Item 8.1 is not contained in the requisite table, Part B, Item 5(f) requires that same information to be disclosed in Part B in tabular form under the heading "Fund Details".
[199] NI 81-101F1, Part A, Item 8.2(1). See also Item 6(4).
[200] NI 81-101F1, Part A, Item 8.2(2)(a).
[201] NI 81-101F1, Part A, Item 8.2(2)(b).

Item 8: Fees and Expenses

8.1 General Disclosure

(1) Set out information about the fees and expenses payable by the mutual fund and by investors in the mutual fund under the heading "Fees and Expenses".

(2) The information required by this Item shall first be a summary of the fees, charges and expenses of the mutual fund and investors presented in the form of the following table, appropriately completed, and introduced using substantially the following words:

"This table lists the fees and expenses that you may have to pay if you invest in the [insert the name of the mutual fund]. You may have to pay some of these fees and expenses directly. The Fund may have to pay some of these fees and expenses, which will therefore reduce the value of your investment in the Fund."

(3) Include the fees for any optional services provided by the mutual fund organization, as described by Item 7 of Part A of this Form, in the table.

(4) If management fees are payable directly by investors, add a line item in the table to disclose the maximum percentage that could be paid by investors.

(5) If the manager permits negotiation of a management fee rebate, provide disclosure of these arrangements. If these arrangements are not available for each mutual fund described in the document, make this disclosure in the description of fees and expenses required for each fund by Item 5 of Part B of this Form and include a cross-reference to that information in the table required by this Item.

Fees and Expenses Payable by the Fund	
Management Fees	*[See Instruction (1)]* *[disclosure re management fee rebate program]*
Operating Expenses	*[See Instructions (2) and (3)]* *Fund[s] pay[s] all operating expenses, including _____*
Fees and Expenses Payable Directly by You	
Sales Charges	*[specify percentage, as a percentage of _____]*
Switch Fees	*[specify percentage, as a percentage of _____ , or specify amount]*
Redemption Fees	*[specify percentage, as a percentage of _____ , or specify amount]*
Registered Tax Plan Fees *[include this disclosure and specify the type of fees if the registered tax plan is sponsored by the mutual fund and is described in the simplified prospectus]*	*[specify amount]*
Other Fees and Expenses *[specify type]*	*[specify amount]*

INSTRUCTIONS:

(1) If the table pertains to more than one mutual fund and not all of the mutual funds pay the same management fees, under "Management Fees" in the table, either

(a) state that the management fees are unique to each mutual fund, include management fee disclosure for each mutual fund as a separate line item in the table required by Item 5 of Part B of this Form for that mutual fund, and include a cross-reference to that table; or

(b) list the amount of the management fee, including any performance or incentive fee, for each mutual fund separately.

(2) If the table pertains to more than one mutual fund and not all of the mutual funds have the same obligations to pay operating expenses, either

(a) state that the operating expenses payable by the mutual funds are unique to each mutual fund, include the description of the operating expenses payable by each mutual fund as a separate line item in the table required by Item 5 of Part B of this Form for that mutual fund, and include a cross-reference to that table; or

(b) provide the disclosure concerning the operating expenses for each mutual fund contemplated by this Item separately.

(3) Under "Operating Expenses", state whether the mutual fund pays all of its operating expenses and list the main components of those expenses. If the mutual fund pays only certain operating expenses and is not responsible for payment of all such expenses, adjust the statement in the table to reflect the proper contractual responsibility of the mutual fund.

(4) Show all fees or expenses payable by the mutual fund, even if it is expected that the manager of the mutual fund or other member of the organization of the mutual fund will waive or absorb some or all of those fees and expenses.

(5) If the management fees of a mutual fund are payable directly by a securityholder and vary so that specific disclosure of the amount of the management fees cannot be disclosed in the simplified prospectus of the mutual fund, or cannot be derived from disclosure in the simplified prospectus, provide as much disclosure as is possible about the management fees to be paid by securityholders, including the highest possible rate or range of those management fees.

8.2 Illustrations of Different Purchase Options

(1) Under the sub-heading "Impact of Sales Charges" provide information, substantially in the form of the following table, concerning the amount of fees payable by an investor under the available purchase options and introduced using substantially the following words:

"The following table shows the amount of fees that you would have to pay under the different purchase options available to you if you made an investment of $1,000 in the Fund, if you held that investment for one, three, five or ten years and redeemed immediately before the end of that period."

	At Time of Purchase	1 Year	3 Years	5 Years	10 Years
Sales Charge Option	$!	---	---	---	---
Redemption Charge Option[1]	---	$!	$!	$!	$!
No Load Option	---	---	---	---	---
[Other purchase options]	$!	$!	$!	$!	$!

(1) *Redemption charges may apply only if you redeem your [units/shares] in a particular year. Redemption charges are shown under "Fees and Expenses" above.*

(2) In preparing the table contemplated by this Item, assume, in determining the fees paid under the sales charge option, that

(a) the maximum sales commission disclosed in the simplified prospectus is paid by the investor; and

(b) if the mutual fund has a deferred sales charge option in which the amount paid by an investor at the time of a redemption of securities is based upon the net asset value of those securities at that time, an annual return of five percent since time of purchase, and disclose that assumption in a footnote to the table.

- Part B, Item 13 – Financial highlights: the MER is required to be disclosed by this Item in tabular form as follows:

Item 13: Financial Highlights

13.1 Tables

(1) Provide selected financial information about the fund under the heading "Financial Highlights", in the form of the following tables, appropriately completed, and introduced using substantially the following words:

"The following tables show selected key financial information about the Fund and are intended to help you understand the Fund's financial performance for the past [insert number] years. This information is derived from the Fund's audited annual financial statements. Please see page [insert page number] for information about how you can obtain the Fund's audited financial statements."

…

Ratios and Supplemental Data

	[*insert year*]	[*insert year*]	[*insert year*]	[*insert year*]	[*insert year*]
Net assets (000's)(1)	$!	$!	$!	$!	$!
Number of [units/shares] outstanding(1)	!	!	!	!	!
Management expense ratio(2)	! %	! %	! %	! %	! %
Portfolio turnover rate(3)	! %	! %	! %	! %	! %

(1) *This information is provided as at [insert date of end of financial year] of the year shown.*

(2) *Management expense ratio is based on total expenses for the stated period and is expressed as an annualized percentage of daily average net assets during the period.*

(3) *The Fund's portfolio turnover rate indicates how actively the Fund's portfolio adviser manages its portfolio investments. A portfolio turnover rate of 100% is equivalent to the Fund buying and selling all of the securities in its portfolio once in the course of the year. The higher a fund's portfolio turnover rate in a year, the greater the trading costs payable by the fund in the year, and the greater the chance of an investor receiving taxable capital gains in the year. There is not necessarily a relationship between a high turnover rate and the performance of a fund.*

The Instruction requires calculation of the MER to be in accordance with Part 16 of NI 81-102[202] (see **Appendix CAN-1**).

Following this table, a prospectus must, under the heading "Fund Expenses Indirectly Borne by Investors", illustrate an example of mutual fund expenses borne by investors, representing an investor's cumulative proportional share of fund fees and expenses, in dollar terms, over stated time intervals.[203] Assumptions for this illustration are as follows:

(2) (a) an initial investment of $1,000;

[202] NI 81-101F1, Part B, Item 13.1, Instr. (2).
[203] NI 81-101F1, Part B, Item 13.2(1)-(2).

(b) a total annual return of the mutual fund of five percent in each year, calculated in accordance with section 15 of National Instrument 81-102;

(c) a management expense ratio of the mutual fund the same throughout the 10 year period as they were in the last completed financial year of the mutual fund…[204]

The illustration is also required to:

> Provide an introduction to the disclosure that explains that the disclosure is intended to help an investor compare the cost of investing in the mutual fund with the cost of investing in other mutual funds, shows the amount of fees and expenses paid by the mutual fund that are indirectly borne by an investor, and describes the assumptions used.[205]

Commissions and Commission Practices

- Part A, Item 9.1 – Dealer compensation generally: under the heading "Dealer Compensation", Part A of the SP must provide "disclosure of sales practices and equity interests required by sections 8.1 and 8.2 of NI 81-105".[206]

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[204] NI 81-101F1, Part B, Item 13.2(2) (as amended, effective 2 May 2001: OSC, *Notice of Rules and Policies Made Under the Securities Act: Amendments to NI 81-101F1* (16 February 2001), Part 2, ¶8).

[205] NI 81-101F1, Part B, Item 13.2(3).

[206] *National Instrument 81-105 Mutual Fund Sales Practices* ("**NI 81-105**") (1 May 1998). NI 81-105:

> regulates the sales and business practices followed both by managers and principal distributors of publicly offered mutual funds, and by registered dealers and their sales representatives in connection with the distribution of securities of publicly offered mutual funds. …[T]he National Instrument establishes only minimum standards of conduct for industry participants. (OSC, *Notice of Rule and Policy Under the Securities Act: NI 81-105* (1 May 1998), under the sub-headings "Substance and Purpose of National Instrument" and "Substance and Purpose of Companion Policy".)

NI 81-105 does not modify any of the disclosure requirements under NI 81-101 but rather provides detailed guidance as to the practices and conduct which are expected of industry participants. Provided there is disclosure in the SP to the extent required by the Instrument, NI 81-105 permits mutual funds to pay to dealers commissions (¶3.1(b)) and trailing commissions (¶3.2(1)(b)). The Instrument explicitly reinforces this:

> **PART 8 PROSPECTUS AND POINT OF SALE DISCLOSURE**
> **8.1 Disclosure of Sales Practices**
> (1) A mutual fund shall provide in its prospectus or simplified prospectus a complete description of
> (a) all compensation payable by members of the organization of the mutual fund to all principal distributors and participating dealers of the mutual fund; and
> (b) the sales practices followed by the members of the organization of the mutual fund for distribution of securities of the mutual fund.

The instructions to Item 9.1 require that such disclosure be "briefly state[d]…in a concise and explicit manner".[207] Examples are provided of the types of commissions that should be disclosed:

- Manager pays up-front sales commission to dealer: so state and include the range.
- Manager permits dealers to retain commissions paid by investors: so state and include the range.
- Manager pays trailing commissions: so state, provide the basis of calculation, and give the range of rates of such commissions.
- Fund pays dealer marketing expenses: so state.
- Fund holds educational conferences for dealers or pays dealer expenses incurred in holding such conferences: so state.

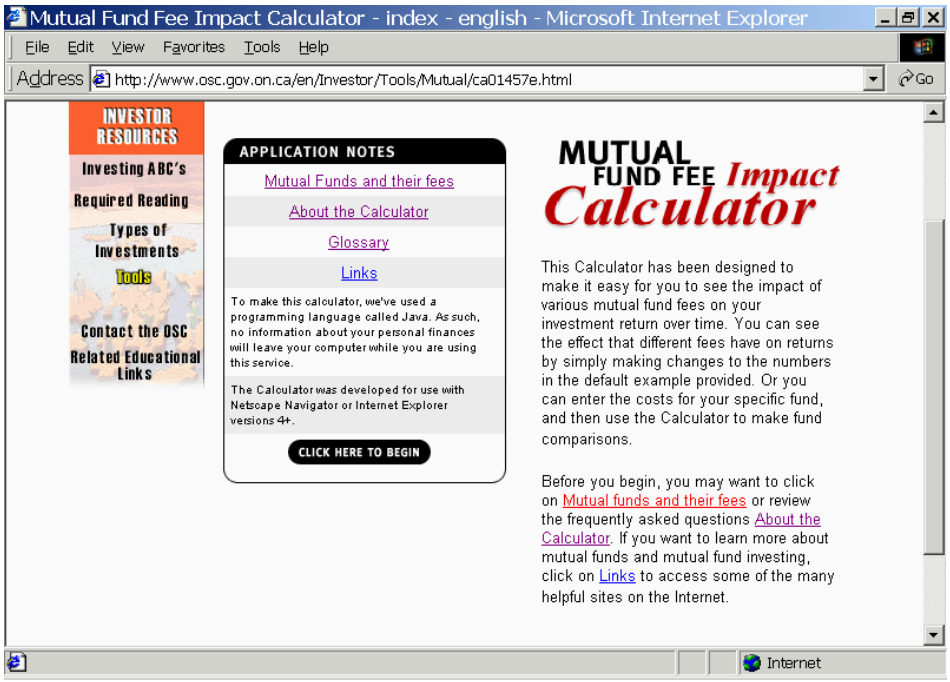
- Part A, Item 9.2 – Dealer compensation from management fees: this Item requires the fund to disclose the approximate percentage of aggregate management fees which was paid to dealers as compensation in relation to distribution or for marketing, promotional or educational expenses.

THE MUTUAL FUND FEES CALCULATOR

The OSC makes available on its website[208] an online calculator. The calculator is JavaScript-based, which means that the calculator runs as a standalone program within a web-browser, drawing upon user-specified data input via the calculator's real-time interface: as the user alters certain of the settings to reflect different fund characteristics or to attempt "What if…?" calculations, the calculator recalculates instantly, allowing users to evaluate the overall effect of the variables as they are input and/or changed. The intention is that users will input data from actual prospectuses so that the calculations performed will be of comparative use.

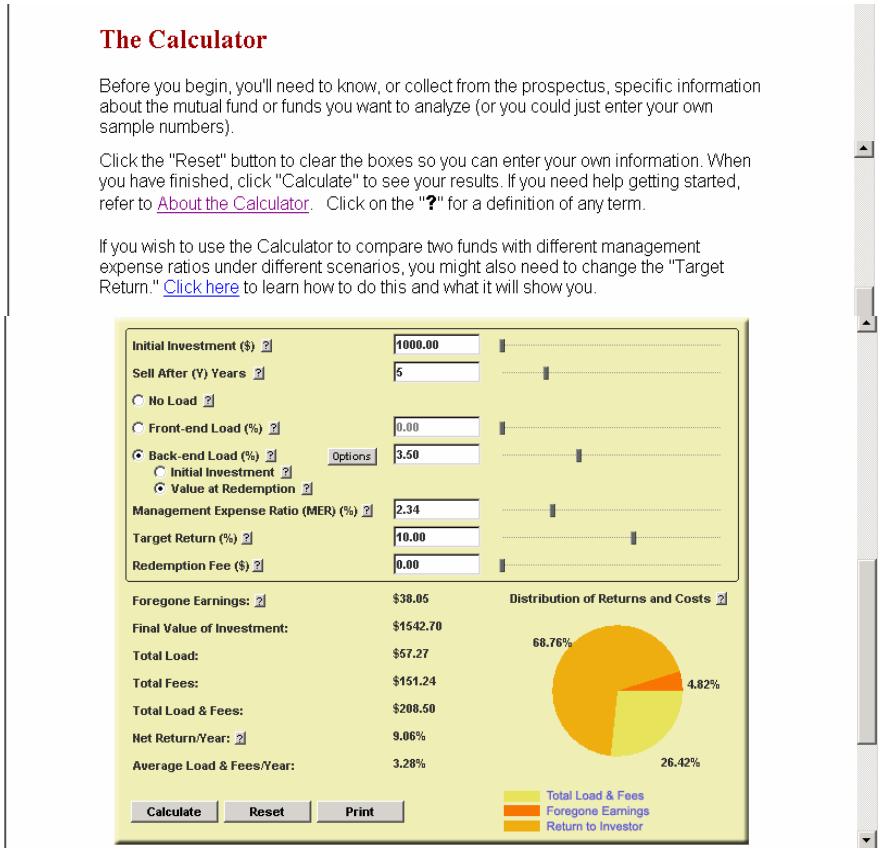
The introductory page to the calculator is as follows:

[207] NI 81-101F1, Part A, Item 9.1, instr. (1).
[208] http://www.osc.gov.on.ca/en/Investor/Tools/Mutual/ca01457e.html.



As can be seen, the preamble makes clear that the calculator is able to assist the investment-decision process in a number of ways.

The page containing the calculator is as follows:



The user can enter the data directly into the data fields or use the sliders. Changes effected through the sliders are calculated and represented, as they are changed, on the pie chart in the lower-right corner. The screendump above is unchanged from the OSC website and does not necessarily represent an actual fund or fund investment.

Information about the calculator and its parameters is presented in the form of "Frequently Asked Questions" which follows:

About the Calculator

Q: What does the Calculator do?
Q: What costs are included in the Calculator?
Q: What costs are not included in the Calculator?
Q: What other factors does the Calculator take into account?
Q: Can I compare one mutual fund's costs with another's?
Q: What are the minimum system requirements needed to run the Calculator?
Q: Can the Calculator download specific information about my mutual fund from other information sources?
Q: Where can I find specific information about my mutual fund to enter into the Calculator?
Q: How do I find definitions for terms I don't understand?
Q: Where can I learn more about mutual funds?
Q: Who do I contact if I need help or have questions?

Q: What does the Calculator do?
A: The Calculator enables you to compare how various mutual fund costs or fees affect your investment returns over time. The program provides a sample calculation to show the impact of selected costs on an investment of $1,000 and presents the results in an easy-to-understand pie chart.

Q: What costs are included in the Calculator?
A: The program allows you to enter a fund's:

- management expense ratio (MER)
- load: no load, front-end load, or back-end load
- redemption fee

Q: What costs are not included in the Calculator?
A: The program does not include any service fees a fund company or dealer may charge (for example, account opening fees or annual RRSP administration fees) that are related to an investor's account, not a specific fund.

Q: What other factors does the Calculator take into account?
A: The program is designed so that you can:

- choose an investment amount
- decide how long you will hold the investment
- enter the target return you hope your fund will achieve annually
- indicate whether a back-end load is calculated on the amount of the initial investment amount or on the value of the investment when you sell, or redeem, it.

Q: What are the minimum system requirements to run the Calculator?
A: The Calculator is designed for use with Netscape Navigator 4.0 or Internet Explorer 4.0 or higher. (Click here if you need to download Netscape Navigator (latest version) or Internet Explorer (latest version).) The browser that you use with the Calculator will need to have Java enabled.

Q: Can the Calculator download specific information about my mutual fund from other information sources?
A: No. You need to obtain the relevant information about your fund and enter it into the Calculator.

Q: Where can I find specific information about my mutual fund to enter into the Calculator?
A: You can learn all about the costs related to your mutual fund from its prospectus. Every mutual fund has a prospectus, which explains the fund's investment objectives, who manages the fund, the types of investments, the degree of risk, performance over different time periods, costs, and more. You can obtain a fund's prospectus from the fund company or your investment adviser, as well as the SEDAR web site. Most fund companies maintain web sites where you can also access fund information. And information about your fund (and how it compares with other similar funds) may also be found at some of the web sites listed in the Links section.

Q: How do I find definitions for terms I don't understand?
A: Just click on any underlined word or phrase.

Q: Where can I learn more about mutual funds?
A: Here are Links to online sources of information on investing in mutual funds.

Q: Who do I contact if I need help or have questions?
A: Just click here. Or you can e-mail us at inquiries@osc.gov.on.ca. And be sure to tell us what you think of this Calculator.

The auxiliary Glossary defines key terms applicable to the calculator (and to investing more generally):

Glossary

Back-end load

A load is a sales commission that may be charged when you buy or when you sell a fund. When you purchase a fund with a back-end load, you will pay a percentage fee to the fund when you sell, or redeem, the fund. This fee is also referred to as a deferred sales charge. The longer you hold a back-end load fund, the lower the fee will be. A typical load might start at 5.5% if you sell your fund after 1 year, declining to 0% if you sell after 8 years. However, many back-end load funds allow you to withdraw up to 10% of your investment per year without a charge.

A back-end load can be calculated either on the amount of the original investment or on the value of the investment at the time you sell the fund. The way your back-end load is calculated can have a significant impact on your investment return.

From time to time, a fund may pay dividends, which would be reinvested in the fund unless the investor requests the dividends in cash. These amounts can generally be redeemed without any charge.

Some fund dealers now offer an upfront bonus, or rebate, to investors who invest a minimum specified amount in a back-end load fund. This bonus is invested in the fund being purchased, which means that an investment of, for example, $2,500 with a bonus of 2.5% could immediately become an investment of $2,562.50.

Foregone earnings

This is the amount that you could have earned on your mutual fund investment if the money spent on fees had instead been invested.

The calculator derives foregone earnings as follows: Foregone Earnings = Gross Return - (Fees, Expenses and Loads) - (Return to Investor).

Front-end load

A load is a sales commission that may be charged by a mutual fund company or dealer when you buy or when you sell a fund. When you purchase a fund with a front-end load, you will pay a percentage fee that is immediately deducted from your initial investment amount and paid to the distributor. Front-end loads should be negotiated with your investment adviser or dealer. A front-end load can be as high as 9% but is more likely to be between 2% and 3%.

Initial investment

This is the dollar amount you wish to invest in your mutual fund.

Management expense ratio (MER)

A mutual fund's management expense ratio, or MER, is the management fees and expenses paid by the fund expressed as a percentage of the fund's assets. These are deducted from the fund's assets before the fund's rates of return are published in fund performance tables. All mutual funds charge such costs, and this fee is charged to your fund continuously regardless of how your fund performs. Over time, this can have a significant impact on your investment returns. You may not be concerned about an MER of 3% when your fund is earning 35% in a given year. But you will be concerned when your fund earns a much lower return, or loses money. A fund with a higher MER will have to achieve a higher return on the market to do as well as a similar fund with a lower MER.

You can use a fund's MER to compare the cost of investing in it as opposed to another fund. You can also determine if your fund's MER is higher or lower than the MERs of other funds with similar investment styles and objectives. A fund that invests in international markets is likely to have a higher MER than a fund that invests in Canada. And a fund that invests in equities is likely to have a higher MER than a fund that invests in bonds. MERs for all funds, and averages for the various fund types, are regularly published in some newspapers.

In some cases, you can purchase a fund on a front-end load basis or an equivalent fund on a back-end load basis. The difference between the two funds is the amount of the MER, which generally would be higher for the fund purchased with a back-end load.

On a technical note, this Calculator computes the MER on the average of the beginning investment (for example, $1,000) and of the end-of-year investment (for example, $1,000 + assumed 10% return over one year=$1,100) values. Therefore, the calculation would be based on the average of $1,000 and $1,100, which is $1,050. In real life, the MER is generally calculated daily.

Net return/year

This is the percentage return your mutual fund would actually earn upon sale after loads and fees are deducted. This amount may differ significantly from target return, depending on load and the amount of time you hold the fund.

No load

A load is a sales commission that may be charged when you buy or when you sell a fund. A no load fund does not carry any sales commission when you buy or when you sell the fund.

Pie Chart

The Pie Chart represents the "Gross Return" for the entire holding period before any payments (including payments to you) are made. It is different from "Target Return" which is the profit you hope to receive after fund management fees and expenses have been deducted.

- "Return to Investor" is the amount you pocket. This 'piece of the pie' is the final value of the investment to you, not counting your original principal.
- "Total Load and Fees" illustrates the amount actually paid to the fund company or dealer.
- "Foregone earnings" shows an additional amount you ***could*** have earned if deductions for loads, fees and expenses had been invested on your behalf, instead of being paid out.

  The following example shows the effect of a front-end load on foregone earnings. You've invested $10,000 in Fund XYZ which has a front-end load of 5%. Off-the-top, $500 of your investment is paid in sales charges – reducing your net investment to $9,500. Let's say you hold the investment for 1 year, during which time the Fund earns a "Gross Return" of 10%. In this case, "foregone earnings" as a result of the front-end load amount to $50 (0.10X 500). The $50 is the money you did not earn because $500 was deducted from your initial investment and not invested on your behalf. The payment of the MER by the fund also would result in foregone earnings.

Two points to remember – other investments may also charge fees, and fees and expenses are only one factor to consider when choosing to invest in a mutual fund. If you are concerned about the impact of foregone earnings on the value of your investment – one thing you can do is negotiate a lower sales charge.

Redemption Fee

Some fund dealers charge a fee (for example, $40) when you sell or transfer your mutual fund. This fee is deducted from your investment.

Sell after

This refers to the number of years you want to hold your mutual fund before you sell, or redeem, it.

Target Return

This is the percentage return you estimate your mutual fund will earn annually after the management fee and expenses have been deducted. You can estimate target return by referring to the fund's historical returns over various time periods. Of course, past performance is not necessarily an indication of how your fund will do in the future. Individual fund performance is reported by the mutual fund company, in newspapers, in books that compare mutual funds, and at many of the web sites in the Links section. "For more information, you may wish to see your financial adviser." At end,"Target Return differs from Gross Return. The latter is the return for the entire holding period before any payments (including payments made to you) are made." It is important to be realistic about the target return you enter. Even though your fund may have had a 50% return one year, that return is unlikely to be sustainable over the long term. On a compound annual basis, Canadian equity funds had average returns of 9.76% over the last 10 years.

Value at redemption

This is the dollar amount of your investment at the time you decide to sell, or redeem, your mutual fund. A back-end load calculated on the value of your investment when you sell, or redeem, it can significantly reduce your investment return. Refer to the example above under Back-end load.

EXTRACTS FROM ACTUAL PROSPECTUSES

Most public documents which are required to be filed by companies or securities-issuers in Canada are filed with SEDAR,[209] which is the CSA's national securities database. Prospectuses from two funds were randomly selected from SEDAR.

Firstly, the *CIBC Mutual Funds* SP (9 August 2000). CIBC present their SP in reverse order to that contemplated by NI 81-101: the specific fund information (Part B) comprises the bulk of the first 89 pages of the document, while the general information about the funds (Part A) comprises the remaining 28 pages.

Turning to that Part A information firstly, CIBC provide the following information in respect of fees, charges and commissions applicable to the funds in general:

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fees and expenses

The following table lists the fees and expenses that you may have to pay if you invest in the CIBC Mutual Funds. You may have to pay some of these fees and expenses directly. The Funds may have to pay some of these fees and expenses, which will therefore reduce the value of your investment in the Funds.

fees and expenses payable by the fund		
Management Fees	Each fund pays CIBC Securities Inc. an annual management fee to cover management expenses as disclosed on page 105. This fee is calculated daily and paid monthly. Each fund must pay GST on management fees. Management Fee Rebate: CIBC Securities Inc. may reduce the management fee it charges to certain funds for clients who invest certain minimum amounts, and pass this reduction of management fees to investors in additional units as a management fee distribution.	
Operating Expenses	Each fund is responsible for its own operating expenses which may include: • Interest, operating and administrative costs • Brokerage fees and commissions • Regulatory filing fees • Taxes, audit and legal fees and expenses • Trustee, safekeeping and custodial fees • Investor servicing costs and costs of unitholder reports, prospectus and other reports We will give you at least 60 days notice if there is a change in any contract or if a fund enters into a new contract, which would result in an increase in the management fee or operating expenses charged to the fund.	
fees and expenses payable directly by you		
Sales Charges Switch Fees Redemption Fees	None if you buy, switch or redeem through: • CIBC Securities Inc. • CIBC Investor Services Inc. • CIBC Financial Planning Inc. • CIBC branches	
Registered Tax Plan Fees	RRSP, RRIF and RESP Accounts. (Fees payable on registered accounts are deducted from your account, except in the case of RESP accounts for which fees may be deducted from the account or paid outside the plan):	
	Annual Administration Fee:	$12.00 (payable semi-annually) per account plus applicable sales tax
	Withdrawal Fee*:	$10.00 per account plus applicable sales tax
	Account Closing Fee*:	$40.00 per account plus applicable sales tax
	(If the CIBC U.S. Dollar Money Market Fund is the only holding then the above fees are all in U.S dollars.) *There is no Withdrawal Fee or Account Closing Fee if you transfer your account to: • CIBC Trust Corporation • CIBC World Markets Inc. • CIBC Investor Services inc. • CIBC Financial Planing Inc.	
Other Fees and Expenses	Annual Portfolio Rebalancing Service Fee:	up to $25.00 per account plus applicable sales tax
	Minimum Account Balance Fee:	up to $10.00 per account plus applicable sales tax
	Transaction Fee:	you may be charged a fee to cover losses if a purchase or sale is not completed.

[209] System for Electronic Document Analysis and Retrieval; http://www.sedar.com/.

management fee per year as a percentage (%) of net asset value

	Maximum Fee
CIBC Canadian T-Bill Fund	1.00%
CIBC Premium Canadian T-Bill Fund	0.50%
CIBC Money Market Fund	1.00%
CIBC U.S. Dollar Money Market Fund	1.00%
CIBC High Yield Cash Fund	1.00%
CIBC Canadian Short-Term Bond Index Fund	1.25%
CIBC Mortgage Fund	1.25%
CIBC Canadian Bond Index Fund	1.20%
CIBC Canadian Bond Fund	1.25%
CIBC Monthly Income Fund	1.25%
CIBC Global Bond Index Fund	1.20%
CIBC Global Bond Fund	1.50%
CIBC Balanced Fund	2.00%
CIBC Dividend Fund	1.70%
CIBC Canadian Index Fund	1.20%
CIBC Core Canadian Equity Fund	1.85%
Canadian Imperial Equity Fund	1.75%
CIBC Capital Appreciation Fund	2.00%
CIBC Canadian Small Companies Fund	2.00%
CIBC Canadian Emerging Companies Fund	2.20%
CIBC U.S. Equity Index Fund	2.00%
CIBC U.S. Index RRSP Fund	1.20%
CIBC U.S. Small Companies Fund	2.25%

	Maximum Fee
CIBC Global Equity Fund	2.00%
CIBC International Index Fund	2.00%
CIBC International Index RRSP Fund	2.00%
CIBC European Index Fund	1.20%
CIBC European Equity Fund	2.25%
CIBC Japanese Equity Fund	2.25%
CIBC Emerging Economies Fund	2.50%
CIBC Far East Prosperity Fund	2.50%
CIBC Latin American Fund	2.50%
CIBC International Small Companies Fund	2.50%
CIBC Financial Companies Fund	2.25%
CIBC Canadian Resources Fund	2.00%
CIBC Energy Fund	2.00%
CIBC Canadian Real Estate Fund	2.25%
CIBC Precious Metals Fund	2.00%
CIBC North American Demographics Fund	2.85%
CIBC Global Technology Fund	2.25%
CIBC Nasdaq Index RRSP Fund	1.20%
CIBC Nasdaq Index Fund	1.20%
CIBC European Index RRSP Fund	1.20%
CIBC Japanese Index RRSP Fund	1.20%
CIBC Asia Pacific Index Fund	1.20%
CIBC Emerging Markets Index Fund	1.20%

impact of sales charges

CIBC Mutual funds are no load. That means you pay no sales charges when you purchase, switch or redeem units through CIBC Securities Inc., CIBC Investor Services Inc., CIBC Financial Planning Inc., each of which is a wholly-owned subsidiary of CIBC, or through a CIBC branch. You may pay sales charges if you purchase, switch or redeem units through a registered dealer or broker.

dealer compensation from management fees

sales commissions

Registered dealers or brokers may charge sales commissions administered by their own back-office of up to 4% of the purchase price of CIBC Mutual Fund units at the time of investment. CIBC or CIBC Securities Inc. may pay some of their employees incentives based on sales of CIBC Mutual Funds such as cash or merchandise in addition to, or instead of, a salary.

service commissions

CIBC Securities Inc. may pay service commissions to registered dealers and brokers based on the value of CIBC Mutual Funds held by their clients of up to 1.50% per year. Before we pay service commissions, a client must own CIBC Mutual Fund units for 90 days. We may waive this requirement at our discretion.

dealer compensation from management fees

CIBC Mutual Funds are sold at no charge through CIBC Securities Inc., CIBC Investor Services Inc., CIBC Financial Planning Inc., and through CIBC branches. However, for the year ended October 31, 1999, CIBC Securities Inc. paid approximately 8.77% of total management fees to registered dealers and brokers as sales and service commissions for units of CIBC Mutual Funds sold by them.

sales practices

CIBC Securities Inc. or any fund may participate in co-operative marketing and educational activities and sponsor mutual fund conferences in accordance with approved industry practices.

For Part B, the CIBC prospectus presents individual fund information, as far as possible, on no more than two pages so as to convey the maximum "at a glance" information. Extracted is the Part B fee information in respect of the "CIBC Global Technology Fund":

financial highlights

The Fund's Distributions and Net Asset Value per Unit:

	1999	1998	1997	1996	1995
Distributions:					
from net income	$ 0.00	$ 0.00	$ 0.08	$ 0.00	$ 0.02
from realized gain	$ 3.89	$ 0.00	$ 1.03	$ 0.60	$ 0.01
return of capital	$ 0.00	$ 0.00	$ 0.14	$ 0.00	$ 0.00
Total Annual Distributions	$ 3.89	$ 0.00	$ 1.25	$ 0.60	$ 0.03
Net Asset Value	$ 44.00	$ 18.94	$ 12.95	$ 12.17	$ 10.31

Ratios and Supplemental Data:

	1999	1998	1997	1996	1995
Net Assets (000's)	$ 389,190	$ 119,797	$ 74,576	$ 37,077	$ 7,205
Number of Units outstanding	8,845,647	6,324,791	5,760,175	3,046,234	698,778
Management Expense Ratio	2.76%	2.77%	2.63%	2.46%	0.95%
Portfolio Turnover Rate	136.62%	210.75%	316.18%	429.38%	n/a

fund expenses indirectly borne by investors

Expenses payable over	One Year	Three Years	Five Years	Ten Years
	$ 28.30	$ 89.20	$ 156.35	$ 355.91

The foregoing Part B information is just one of almost 50 funds contained in the prospectus. In order to assist readers understand the Part B information in respect of a particular fund, CIBC provides the following guidance information which draws attention to and explains important aspects of the Part B information:

Ratios and Supplemental Data:

Management expense ratio is based on total expenses for the stated period and is expressed as an annualized percentage of daily average net assets during the period.

Example:

	1999	1998	1997	1996	1995
Net Assets (000's)	$ 176,690	$ 144,731	$ 151,589	$ 117,677	$ 104,729
Number of Units outstanding	18,000,806	14,100,649	14,690,615	11,198,789	10,334,901
Management Expense Ratio	0.96%	1.01%	1.38%	1.39%	1.34%
Portfolio Turnover Rate	82.08%	141.56%	98.90%	205.48%	166.90%

fund expenses indirectly borne by investors

This section provides you with information intended to help you compare the cost of investing in the Fund with the cost of investing in other mutual funds. It shows you the cumulative amount of fees and expenses that an investor indirectly pays when investing in the Fund assuming:

- you invested $1,000 in the Fund over the periods shown
- the Fund returned 5% each year
- the Fund paid the same MER in all periods as it did in the last completed financial year.

The *Fees and Expenses* section, page 104, provides more information on the cost of investing in the Funds.

The immediately foregoing information has been edited for convenience of presentation.

Extracts were also taken from the *National Bank Mutual Funds: Units of the Investor Series* SP (28 March 2002), which offers the following funds:

National Bank Mutual Funds

Units of the *Investor Series*

Simplified Prospectus

March 28, 2002

Money Market Fund (1-2)
Treasury Bill Plus Fund
U.S. Money Market Fund
Corporate Cash Management Fund
Treasury Management Fund
Mortgage Fund (1-2-3)
Bond Fund (1-2-3)
Dividend Fund (1-2-3)
Global RSP Bond Fund (1-2-3)
High Yield Bond Fund (1-4)
Retirement Balanced Fund (4)
Secure Diversified Fund
Conservative Diversified Fund
Moderate Diversified Fund
Aggressive Diversified Fund
Intrepid Diversified Fund
Canadian Equity Fund (1-2-3-4)
Canadian Opportunities Fund (1-2-3-4)
Canadian Index Fund (2-3)
Canadian Index Plus Fund (2-3)
Small Capitalization Fund (1-2-3)
Global Equity Fund (1-2-3)
Global Equity RSP Fund (1-2-3)
International RSP Index Fund (2-3)
American RSP Index Fund (2-3)
American Index Plus Fund (2-3)
European Equity Fund (1-2-3)
European Small Capitalization Fund (1-2-3)
Asia-Pacific Fund (1-2-3)
Emerging Markets Fund (1-2-3)
Quebec Growth Fund (1-2-3)
Natural Resources Fund (1-2-3)
Future Economy Fund (1-2-3)
Future Economy RSP Fund (1-2-3)
Global Technologies Fund (1-2-3)
Global Technologies RSP Fund (1-2-3)
National Bank/Fidelity Canadian Asset Allocation Fund
National Bank/Fidelity Global Asset Allocation Fund
National Bank/Fidelity True North Fund
National Bank/Fidelity International Portfolio Fund
National Bank/Fidelity Growth America Fund
National Bank/Fidelity Focus Financial Services Fund
Protected Canadian Bond Fund
Protected Retirement Balanced Fund
Protected Growth Balanced Fund
Protected Canadian Equity Fund
Protected Global RSP Fund

(1) Units of the ***Advisor Series*** also offered.
(2) Units of the ***F Series*** also offered.
(3) Units of the ***Institutional Series*** also offered.
(4) Units of the ***O Series*** also offered.

The prospectus explains the types of units and series offered as follows (edited for convenience):

About units of a series

We offer five series of units called the ***Investor, Advisor***, ***F, Institutional*** and ***O*** Series units.

All National Bank Mutual Funds are offered in units of the ***Investor Series***. However, all the funds do not offer the four other series of units. In particular, the Treasury Bill Plus Fund and the U.S. Money Market Fund only offer units in the ***Investor Series***. See ***Fund details*** with respect to each fund to find out which series is offered by each fund.

Investor Series	These units are offered to all investors as a no-load fund, which means that you do not pay any fees when you buy, switch or redeem your units through any branch of the National Bank of Canada, National Bank Securities Inc., National Bank Financial Services (Investments) Inc. or National Bank Discount Brokerage Inc. You may have to pay fees if you buy, transfer or redeem your units through another dealer.
Advisor Series	These units are offered to certain investors in either of the following ways: – with initial sales charge. In this case, you pay an initial sales charge which you negotiate with your dealer when you purchase fund units. – with deferred sales charge. In this case, you may be required to pay deferred sales charge if you ask for your units to be redeemed within 6 years of purchase. Your choice will have an impact on the fees you pay and the compensation your dealer receives. Please see ***Fees and Expenses*** and ***Dealer Compensation***.
F Series	These units are only offered to investors with a commission account with dealers who have entered into an agreement with us. These investors pay their dealer annual compensation based on asset value instead of commissions on each trade. They are also offered to certain other groups of investors for which we do not incur a significant investment fee. The ***F Series*** units have lower management fees than units of the other series because our costs are lower. In fact, these units were created for investors taking part in programs which were already charging service charges for services they were receiving and which did not require us to incur investment expenses in the form of trailer fees paid to dealers. We can reduce our management fees since our investment fees are lower and investors who buy these units have already entered into an agreement to pay fees directly to their dealer. Your dealer is responsible for deciding whether you are eligible to subscribe for and continue to hold ***F Series*** units. If you or your dealer are not eligible to hold them, we can switch them for ***Advisor Series*** units of the same fund upon 30 days' notice or redeem them.
O Series	Series O units are only available to selected investors that have been approved by us and have entered into an O Series account with us. These investors are normally financial services companies. The criteria for approval may include the size of the investment, the expected level of account activity and the investor's total investment with us. No management fees are charged to the Fund with respect to the Series O units, but investors will be charged a negotiated administrative fee. We don't pay any commissions or services fees to dealers who sell Series O units. There are no sales charges payable by investors who purchase Series O.
Institutional Series	These units are only offered to select investors we have approved who have entered into an agreement with respect to an Institutional Series unit account with us. These investors are normally financial services companies and other companies which make the minimum required investment determined by us from time to time. We do not pay a commission to dealers who sell Institutional Series units and investors do not pay any fees when they buy, switch or redeem their units through any branch of the National Bank of Canada, National Bank Securities Inc., National Bank Financial Services (Investments) Inc. or National Bank Discount Brokerage Inc. You may have to pay fees if you buy, transfer or redeem your units through another dealer.

The National Bank SP is arranged in the more-conventional order presupposed by NI 81-101. The Part A information in respect of National Bank funds is as follows:

Fees and expenses

The table below refers to the fees and expenses that you may have to pay if you invest in the National Bank Mutual Funds. You may have to pay some of them directly. The funds have to pay some of these fees and expenses, which will therefore reduce the value of your investment in the funds. Management fees are a percentage of the net asset value of the funds. The fees may be increased upon 60 days' notice to all unitholders.

Fees and expenses payable directly by the funds

Management fees	Each fund pays annual management fees to National Bank Securities Inc. in consideration of its management services. The fees are calculated and accrue daily and are paid monthly. Different management fees apply to each fund and series. Management fees represent a percentage of your investment and vary depending on the fund or series. Since we do not pay any investment or services fees or trailer fees for units in the *Institutional Series*, the *O Series* and *F Series* units, these series are subject to lower management fees than the Investor and *Advisor Series*. Please see *Fund details* for the maximum management fee for each fund
Operating expenses	Each fund has different operating expenses. They include, among other things, audit, legal and custodian fees, registration fees and expenses related to communicating with National Bank Mutual Funds unitholders. The funds which offer more than one series of units distribute the common operating fees among the series on a pro rata basis. The fees which are specific to a series are allocated to it.

Fees and expenses payable directly by you

Sales charges and switch fees	***Investor, Institutional and O Series*** For Investor and Institutional Series units, you do not pay any fees when you buy, switch or redeem your units through any branch of the National Bank of Canada, National Bank Securities Inc., National Bank Financial Services (Investments) Inc. or National Bank Discount Brokerage Inc. You may have to pay fees if you buy, transfer or redeem your units through another dealer. ***F Series*** For F Series units, you pay your dealer annual compensation based on asset value instead of commissions or fees on each purchase, switch or redeem.
	Advisor Series For Advisor Series units with initial sales charge option, you negotiate the fee with your dealer. These fees may not be greater than 5% of the purchase price for all the funds. We deduct the fee from the amount you are investing and pay it to your dealer as a brokerage fee. If you switch your Advisor Series units for Advisor Series units of another National Bank Mutual Funds, you may have to pay your dealer to transfer fees of up to 2% of the value of the units you switch. You negotiate these fees with your dealer. You will have to pay a deferred sales charge to buy Advisor Series units under the deferred sales charge option, if you request the redemption of your units within a specified time. The fee is based on the initial cost of your units and the amount of time you hold them. We will deduct the fee from the value of the units you are redeeming. The following table shows the deferred subscription fees:

	Units sold during the following periods after you bought them	Deferred sales charge if bought with the deferred sales charge option[1]
	during the 1st year	6%
	during the 2nd year	5.5%
	during the 3rd year	5.0%
	during the 4th year	4.5%
	during the 5th year	3.0%
	during the 6th year	1.5%
	after the 6th year	0%
Short-term trading fee	If you redeem or transfer within 90 days of purchase units of any series of National Bank Mutual Funds, you may be charged a short-term trading fee of 1% of the value of the units This fee is designed to protect unitholders from other investors moving quickly in and out of the funds. Frequent trading can hurt a fund's performance by forcing the portfolio manager to keep more cash in the fund than would otherwise be needed or to sell investments at an inappropriate time. It may also increase the fund's transaction costs. Short-term trading fees are paid to the fund and are in addition to any initial sales charge, deferred sales charge, or transfer charge. The fee is deducted from the amount you redeem or transfer, or it is charged to your account, and is retained by the fund. The short-term trading fee doesn't apply to units: • you receive from reinvested distributions • sold as a result of the death of a unitholder.	
Systematic withdrawal plan	Nil	
Periodic saving plan	Nil	
Portfolio rebalancing services	Nil	
Fees for a plan registered for tax purposes – Annual account administrative fee	Nil	
– Account termination fee	$50[2]	
Other fees and expenses	Nil	

[1] *These fees are only charged if you request the redemption of more than 10% of the investment you made.*
[2] *These fees are subject to the Goods and Services Tax and to provincial sales tax, if applicable.*

Impact of sales charges

Investor, F, O and Institutional Series

In general, you pay no charges when you buy, switch or request a redemption of your units of one of these series.

Advisor Series

For Advisor Series unit with the initial sales charge option, you negotiate the fee with your dealer. These fees may not be greater than 5% of the purchase price for all the funds. We deduct the fee from the amount you are investing and pay it to your dealer as a brokerage fee.

The following table indicates the fees you would have to pay according to the different subscription possibilities offered to you if you invest $1,000 over 1, 3, 5, or 10 years and if you ask them to be redeemed before the end of that time.

		Redemption fee before the end of:[1]			
	Sales charge	1 year	3 years	5 years	10 years
Investor Series	–	–	–	–	–
Advisor Series					
Option with initial sales charge	$50	–	–	–	–
Option with deferred sales charge	–	$60	50 $	30 $	–
F Series	–	–	–	–	–
O Series	–	–	–	–	–
Institutional Series	–	–	–	–	–

[1] *These fees are only charged by the Advisor Series if you request the redemption of more than 10% of the investment you made.*

Dealer Compensation

Dealers who sell National Bank Mutual Funds (in branches of the National Bank of Canada) may receive an incentive to sell National Bank Mutual Funds. This incentive may be in addition to salary. They are paid in cash or merchandise valued at up to 0.15% of the sales of fund units. The incentive is awarded based on sales of all units, other than money market funds. The award is structured to avoid encouraging the sale of mutual funds in preference to other products of the National Bank of Canada.

Some people are paid a commission to sell National Bank Mutual Funds. They include representatives of National Bank Securities Inc. in Québec, Ontario and New Brunswick. National Bank Securities Inc. has also contracted with independent mutual fund sales representatives to sell the funds. These representatives may also be representatives of National Bank Financial Services (Investments) Inc., who may also be financial security advisors employed by National Bank Financial Services Inc., a financial services firm in Québec. These representatives and insurance agents work on commission and also receive up to 40% of the management fee on the funds they sell.

All these commissions and service fees are paid by National Bank Securities Inc. out of the management fees paid by the funds. There is no direct cost to you.

National Bank Securities Inc. sets management fees on the funds. It pays up to 100% of the management fees to National Bank of Canada and National Bank Trust Inc. Marketing, advertising and promotional fees are covered by National Bank Securities Inc. and National Bank of Canada.

Advisor Series

Your dealer normally receive a commission each time you buy units in the ***Advisor Series*** of a National Bank Mutual Fund. This commission is based on how you invest in the fund.

- Initial sales charge option

  You and your dealer agree on the percentage you will pay as a fee when you buy ***Advisor Series*** units. This percentage varies between 0% and 5%. See ***Fees and expenses*** for more information.

- Deferred sales charge option

When you buy units in the ***Advisor Series*** with the deferred sales charge option we pay your dealer a commission equal to 5% of the amount you invest. You do not pay any fee unless you redeem your units within six years of their purchase. See ***Fees and expenses*** and ***Impact of sales charges*** for more information.

Switch fee

When you switch your units in the ***Advisor Series*** of a National Bank Mutual Fund for units of the same series of another National Bank Mutual Fund, you may have to pay your dealer transfer fees of up to 2%. You negotiate these fees with your dealer.

Service fee

At the end of each quarter we pay an ongoing advisory fee to your dealer. We assume that the dealers will pay part of that fee to the advisors to compensate them for the services they provide their clients. These fees represent a percentage of the average daily value of the units of each fund held by a dealer's clients. The maximum service fee rates are as follows:

Maximum annual service fee rate for ***Investor Series*** units

Funds	Maximum annual service fee
Money Market Funds	up to 0.35%
Institutional Funds	up to 0.15%
Income Funds	up to 0.50%
Balanced and Diversified Funds	up to 1.00%
Canadian Growth Funds	up to 1.25%
International Growth Funds	up to 1.25%
Specialized Funds	up to 1.25%

Maximum annual service fee rate for ***Advisor Series*** units

Funds	Option with initial sales charge	Option with deferred sales charge
Money Market Fund	0.35%	0.25%
Income Fund	0.50%	0.25%
Canadian Growth Fund	1.25%	0.50%
International Growth Fund	1.25%	0.50%
Specialized Bond Fund	1.25%	0.50%

F, O and Institutional Series

Your dealer does not receive any compensation whatsoever with respect to ***F, O*** and ***Institutional Series*** units.

Dealer compensation from management fees

National Bank Securities Inc. used 8.12% of National Bank Mutual Funds management fees to pay commissions and other promotional activities in 2001.

Note that the last section on this page headed "Dealer compensation from management fees" is drawn from another page in the SP and is only placed here for convenience.

Part B fee information from the "National Bank Global Technologies Fund" has been extracted. In the main, the National Bank funds comprise four or more pages for their Part B information.

Financial highlights

In the following tables we show the fund's financial highlights since the fund has been in existence. We have calculated this information based on the fund's audited annual financial statements as at September 30 for each year shown with the exception of those for 1999 that were audited on December 31. If you wish to receive a copy of these financial statements, you will find our contact information on page 1.

Distributions and net asset value per unit

	1999[1]	2000[3]	2001[3]
Distributions:			
From net income	$0.00	$0.00	$0.00
From net realized capital gains	$0.00	$0.00	$0.00
Return of capital	$0.00	$0.00	$0.00
Total annual distributions	$0.00	$0.00	$0.00
Net asset value per unit at year-end[2]	$15.70	$14.36	$4.97

Ratios and supplemental data

	1999[1]	2000[3]	2001[3]
Net assets (in thousands)[2]	$8,506	$30,965	$12,182
Number of units outstanding[2]	541,685	2,156,182	2,449,576
Expense ratio[4]	2.78%	2.63%	2.72%
Portfolio turnover rate[5]	6.26%	36.79%	188.05%

[1] For the 161-day period ended December 31, 1999.
[2] The information is provided on December 31 for fiscal 1999 and on September 30 for fiscal years 2000 and 2001.
[3] Further to the change in the date of the National Bank Funds' fiscal year-end on March 29, 2000, the financial statements are now audited on September 30 of each year.
[4] See page 30 for an explanation of the expense ratio.
[5] See page 30 for an explanation of the portfolio turnover rate.

Fund expenses indirectly borne by investors

A mutual fund generally pays some expenses out of its assets. The table below shows the costs you pay indirectly for each $1,000 that you have invested in the fund. To make it easy for you to compare these costs to the costs of other funds, this table assumes:

- the total annual return of the fund is 5.00% a year, and
- the expense ratio of the fund was the same throughout the ten-year period as it was in the last financial year of the fund.

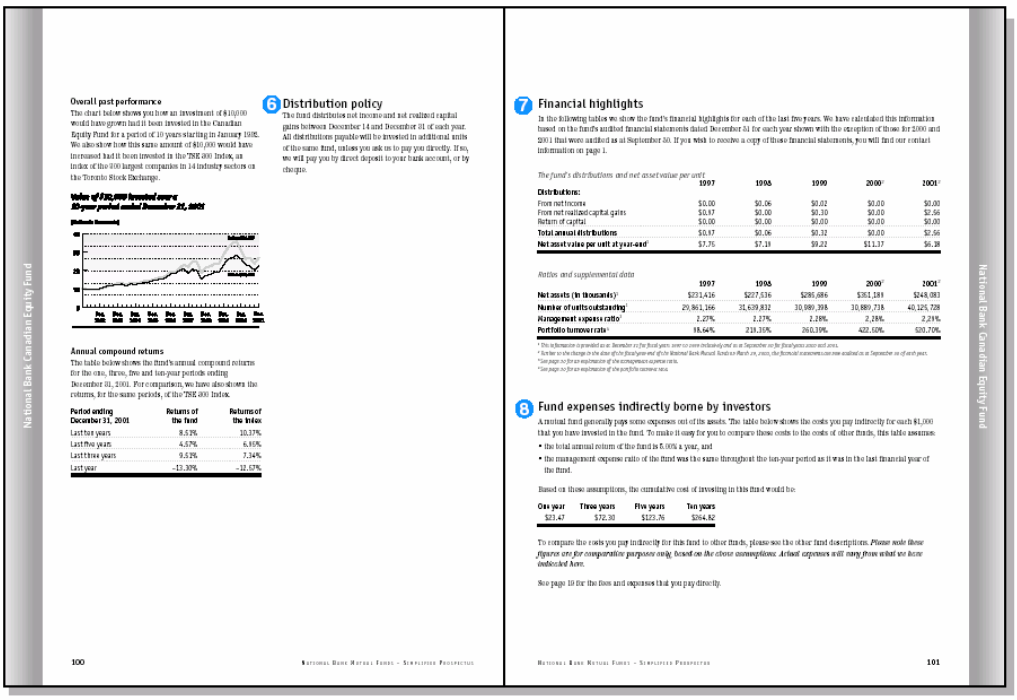
Based on these assumptions, the cumulative cost of investing in this fund would be:

One year	Three years	Five years	Ten years
$27.88	$85.50	$145.70	$308.25

To compare the costs you pay indirectly for this fund to other funds, please see the other fund descriptions. ***Please note these figures are for comparative purposes only, based on the above assumptions. Actual expenses will vary from what we have indicated here.***

See page 19 for the fees and expenses that you pay directly.

In order to assist readers understand the Part B information in respect of a particular fund, National Bank provides the following sample pages which draw attention to and explain important aspects of the Part B information. Points 7 and 8 on sample page 101 are expanded immediately below:



National Bank Canadian Equity Fund

Overall past performance

This chart below shows you how an investment of $10,000 would have grown had it been invested in the Canadian Equity Fund for a period of 10 years starting in January 1998. We also show how this same amount of $10,000 would have increased had it been invested in the TSE 300 Index, an index of the 300 largest companies in 14 industry sectors on the Toronto Stock Exchange.

Value of $10,000 invested over a 10-year period ended December 31, 2001

Annual compound returns

The table below shows the fund's annual compound returns for the one, three, five and ten-year periods ending December 31, 2001. For comparison, we have also shown the returns, for the same periods, of the TSE 300 Index.

Period ending December 31, 2001	Returns of the fund	Returns of the index
Last ten years	8.53%	10.17%
Last five years	4.57%	6.10%
Last three years	9.52%	7.34%
Last year	-13.30%	-11.57%

6 Distribution policy

The fund distributes net income and net realized capital gains between December 14 and December 31 of each year. All distributions payable will be invested in additional units of the same fund, unless you ask us to pay you directly. If so, we will pay you by direct deposit to your bank account, or by cheque.

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National Bank Mutual Funds – Simplified Prospectus

7 Financial highlights

In the following tables we show the fund's financial highlights for each of the last five years. We have calculated this information based on the fund's audited financial statements dated December 31 for each year shown with the exception of those for 2000 and 2001 that were audited as at September 30. If you wish to receive a copy of those financial statements, you will find our contact information on page 1.

The fund's distributions and net asset value per unit

	1997	1998	1999	2000[2]	2001[2]
Distributions:					
From net income	$0.00	$0.06	$0.02	$0.00	$0.00
From net realized capital gains	$0.97	$0.00	$0.30	$0.00	$2.56
Return of capital	$0.00	$0.00	$0.00	$0.00	$0.00
Total annual distributions	$0.97	$0.06	$0.32	$0.00	$2.56
Net asset value per unit at year-end[1]	$7.76	$7.18	$9.22	$11.17	$6.18

Ratios and supplemental data

	1997	1998	1999	2000[2]	2001[2]
Net assets (in thousands)[1]	$231,416	$227,536	$285,686	$361,189	$248,083
Number of units outstanding[1]	29,861,166	31,639,832	30,989,398	30,889,738	40,125,728
Management expense ratio[3]	2.27%	2.27%	2.28%	2.28%	2.24%
Portfolio turnover rate[4]	18.64%	218.35%	260.39%	422.50%	520.70%

[1] This information is provided as at December 31 of the fiscal years, over two years inclusively and as at September 30 for fiscal years over such years.
[2] Further to the change in the date of the fiscal year-end of the National Bank Mutual Funds in March 20, 2000, the financial statements are now audited as at September 30 of each year.
[3] See page 10 for an explanation of the management expense ratio.
[4] See page 10 for an explanation of the portfolio turnover rate.

8 Fund expenses indirectly borne by investors

A mutual fund generally pays some expenses out of its assets. The table below shows the costs you pay indirectly for each $1,000 that you have invested in this fund. To make it easy for you to compare these costs to the costs of other funds, this table assumes:

- the total annual return of the fund is 5.00% a year, and
- the management expense ratio of the fund was the same throughout the ten-year period as it was in the last financial year of the fund.

Based on these assumptions, the cumulative cost of investing in this fund would be:

One year	Three years	Five years	Ten years
$21.47	$72.30	$123.76	$264.82

To compare the costs you pay indirectly for this fund to other funds, please see the other fund descriptions. *Please note these figures are for comparative purposes only, based on the above assumptions. Actual expenses will vary from what we have indicated here.*

See page 10 for the fees and expenses that you pay directly.

National Bank Mutual Funds – Simplified Prospectus

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National Bank Canadian Equity Fund

7 Financial highlights

In this section, we have indicated financial highlights for each of the National Bank Mutual Funds with tables that show:

- the fund's distributions and net asset value per unit
- net assets and number of units outstanding
- management expense ratio
- portfolio turnover rate (where applicable).

Here's an explanation of key terms used in the *Financial highlights section*.

Managing expense ratio — reflects the total expenses of a fund, for the year, shown as a percentage of the average net assets of the fund. On February 1, 2000, the Canadian Securities Administrators changed the definition of management expense ratio. The main change consists of including the paid GST in the expenses for calculation purposes. The management expense ratios for all preceding periods were recalculated so that the data would be consistent. Consequently, the management expense ratios are higher than the figures shown in earlier prospectuses or other documents.

Portfolio turnover rate — indicates how frequently the portfolio manager buys and sells the investments of the portfolio. For example, a portfolio turnover rate of 100% would mean that the portfolio manager buys and sells all the securities in the portfolio once during the year.

As buying and selling increases, the fund's trading costs will also increase as will the chance of an investor receiving taxable capital gains in the year. There is not necessarily a relationship between a high turnover rate and the performance of a fund.

8 Fund expenses indirectly borne by investors

This section helps you compare the cost of investing in this fund with the costs of investing in other funds.

COMMENTARY ON THE EXTRACTS

Fee Impact Calculator

The introductory page to the calculator clearly describes the function and purpose of the calculator and provides links to other information cross-referenced within the calculator. This information is flagged from the outset so that users retain an awareness throughout their use of the calculator of this further information.

The calculator itself provides a helpful graphical representation of the impact of fees and charges upon investment returns by way of a pie-chart. The calculator also provides meaningful fee information in the form of actual dollar amounts in respect of fee data which was input in percentage terms. Thus, MER is converted into a set of real-world figures representing total commissions and fees and foregone earnings. The calculator enables ready comparisons to be made between two or more funds. However, comparisons can only be done by inputting the data in respect of the first fund, executing the calculation and recording or printing the result, and then repeating this process for any further funds. The investor must then make a comparative evaluation on the basis of the calculation results.

Prospectuses

The CIBC and National Bank prospectuses are quite similar in substance in respect of the requisite fee, charge and expense information. This may be due to the relatively prescriptive approach mandated by NI 81-101.

Where the two issuers differ is in format, style and presentation. NI 81-101 allows a fair degree of latitude to issuers in respect of these presentation issues, and it is in this aspect that prospectuses will begin to diverge. These presentation issues will also impact upon the explanatory and guidance material which is provided by way of assistance in understanding the substantive material within the prospectus. If the explanatory and guidance material is difficult to understand or poorly presented, then those weaknesses are likely to be apparent in the presentation of the substantive material as well.

The Canadian prospectus requirements are similar to the Australian superannuation requirements in that certain fee information is required to be presented over a five-year period. The difference is that for Canada, the five-year interval disclosure is in respect

of MER, and for Australia, the disclosure is in respect of OMC. The Australian requirements do not mandate MER for managed funds, whereas the Canadian requirements do. In general, the Canadian requirements for managed funds are more prescriptive than the Australian equivalent and require more detailed disclosure and itemisation of component fees and charges.

Appendix CAN-1

National Instrument 81-102, Part 16

Calculation of Management Expense Ratio

PART 16 CALCULATION OF MANAGEMENT EXPENSE RATIO

16.1 Calculation of Management Expense Ratio

(1) A mutual fund may disclose its management expense ratio only if the management expense ratio is calculated for a financial year of the mutual fund and if it is calculated by

(a) dividing

(i) the total expenses of the mutual fund for the financial year as shown on its income statement,

by

(ii) the average net asset value of the mutual fund for the financial year, obtained by

(A) adding together the net asset values of the mutual fund as at the close of business of the mutual fund on each day during the financial year on which the net asset value of the mutual fund has been calculated, and

(B) dividing the amount obtained under clause (A) by the number of days during the financial year on which the net asset value of the mutual fund has been calculated; and

(b) multiplying the result obtained under paragraph (a) by 100.

(2) If any fees and expenses otherwise payable by a mutual fund in a financial year were waived or otherwise absorbed by a member of the organization of the mutual fund, the mutual fund shall disclose in a note to the disclosure of its management expense ratio, details of

(a) what the management expense ratio would have been without any waivers or absorptions;

(b) the length of time that the waiver or absorption is expected to continue;

(c) whether the waiver or absorption can be terminated at any time by the member of the organization of the mutual fund; and

(d) any other arrangements concerning the waiver or absorption.

(3) All non-optional fees, charges and expenses paid directly by investors of a mutual fund in connection with the holding of securities of the mutual fund during the period to which the disclosed management expense ratio relates shall be included by the mutual fund in its calculation of the management expense ratio with an appropriate explanation in a note to the disclosure.

(4) If the aggregate amount of a non-optional fee, charge and expense payable directly by investors of a mutual fund in connection with the holding of securities of the mutual fund during the period to which the disclosed management expense ratio relates is not ascertainable, the mutual fund shall include the maximum amount of the non-optional investor fee that could have been paid by those investors in its calculation of the management expense ratio.

(5) Mutual fund expenses rebated by a manager or a mutual fund to a securityholder shall not be deducted from total expenses of the mutual fund in determining the management expense ratio of the mutual fund.

(6) A mutual fund that has separate classes or series of securities shall calculate a management expense ratio for each class or series, in the manner required by this section, modified as appropriate.

(7) In this section, the phrase "financial year" includes, for an issuer, a period other than the 12 months for which the issuer is required by securities legislation to prepare audited financial statements.

(8) The management expense ratio of a mutual fund for a financial year of less than 12 months shall be annualized.

The Instrument was amended (effective 2 May 2001):

1. Paragraph 1(a)(i) was amended as follows: [210]

(23) Section 16.1 of National Instrument 81-102 is amended by the deletion of subparagraph (1)(a)(i) and the substitution of the following:

"(i) the total expenses of the mutual fund, before income taxes, for the financial year, as shown on its income statement,".

2. A new paragraph 4 was inserted, and existing paragraphs 4-8 were renumbered 5-9 respectively:[211]

"(4) The requirements to provide note disclosure contained in subsections (2) and (3) do not apply if a mutual fund provides its management expense ratio to a service provider that will arrange for public dissemination of the management expense ratio, if the mutual fund indicates, as applicable, that management fees have been waived or that management fees were paid directly by investors during the period for which the management expense ratio was calculated.".

[210] OSC, *Notice of Rules and Policies Made Under the Securities Act: Amendments to NI 81-102* (16 February 2001), ¶23.

[211] Ibid, ¶24.

UNITED STATES OF AMERICA

Securities issues in the USA are governed by provisions of the Securities Act 1933 ("**1933 Act**"),[212] the Investment Company Act 1940 ("**1940 Act**"),[213] and any rules promulgated under those Acts. Primary responsibility for the federal regulation of securities issues is reposed in the Securities and Exchange Commission ("**SEC**"). The financial products falling within this jurisdiction that are the subject of this part of the international review are Employee Retirement Income Security Act ("**ERISA**") plans and mutual funds.

ERISA PLANS AND THE INTERNAL REVENUE CODE

Definition and Application

ERISA stands for Employee Retirement Income Security Act 1974.[214] ERISA imposes prudential and regulatory standards upon fiduciaries engaged in the management and administration of certain categories of employee retirement and benefit investments, such as health plans, annuities and retirement pensions. Generally, ERISA plans operate by way of investment of employee and employer contributions from salary in permitted investment vehicles, which include pooled equity trusts, mutual funds provided by external fund managers and conventional direct investment in property. The investment structure takes the form of a trust, with the trustee having "exclusive authority and discretion to manage and control the assets of the plan".[215] An incentive for the use of ERISA plans as a retirement investment vehicle is concessional income tax treatment under the Internal Revenue Code ("**IRC**").[216] ERISA plans complying with the IRC in this fashion are known as "401(k) plans".[217] The concession is in the form of a deferred tax arrangement, such that contributions to a 401(k) plan are effectively salary-sacrificed, and tax is computed once the 401(k) plan funds are

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[212] 15 USC 77a. USC means the United States Code, which is:

> a consolidation and codification by subject matter of the general and permanent laws of the United States.
>
> The Code does not include regulations issued by executive branch agencies, decisions of the Federal courts, treaties, or laws enacted by State or local governments. Regulations issued by executive branch agencies are available in the Code of Federal Regulations. Proposed and recently adopted regulations may be found in the Federal Register. (http://uscode.house.gov/about.htm.)

[213] 15 USC 80a-1.
[214] 29 USC 1001.
[215] 29 USC 1103(a).
[216] 26 USC 1.
[217] 26 USC 401(k).

withdrawn.[218] In this way, the investor is able to increase long-term earning potential by investing (and compounding) gross-of-tax contributions rather than net-of-tax contributions, with the tax liability being deferred rather than accrued.

ERISA Summary Plan Descriptions

Administrators of employee benefit plans[219] are required to furnish each participant in such plans with a "summary plan description".[220] The summary plan description is required to be provided to participants and beneficiaries under plans within 90 days after becoming a participant or first receiving a benefit.[221]

The format and content of summary plan descriptions prescribed by the Labor Secretary[222] requires that:

> Plans…shall include a summary of any provisions that may result in the imposition of a fee or charge on a participant or beneficiary, or on an individual account thereof, the payment of which is a condition to the receipt of benefits under the plan.[223]

A fee disclosure form for 401(k) plans has been jointly developed by the American Council of Life Insurance, the Investment Company Institute and the American Bankers Assocation.[224] The fee disclosure form is not legally mandated but has been developed by these industry bodies to improve transparency and information in the

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[218] Albert J. Golly Jr, "401(k) Plans and Their Role in an Investor's Portfolio" (April 1992) 14(4) *American Association of Individual Investors Journal*, http://www.aaii.com/promo/aie/role.shtml, and Maria Crawford Scott, "A Guide to the Advantages – and Disadvantages – of 401(k) Plans" (January 1995) 17(1) *American Association of Individual Investors Journal*, http://www.aaii.com/promo/aie/guide.shtml.

[219] An employee benefit plan is defined as either or both an employee welfare benefit plan and an employee pension benefit plan (29 USC 1002(3)). A welfare benefit plan provides for participants or their beneficiaries, through the purchase of insurance or otherwise, medical, surgical or hospital care and benefits in the event of sickness, disability, unemployment and the like (29 USC 1002(1)(A)); a pension benefit plan provides retirement income to employees or results in a deferral of income by employees for periods extending to the termination of employment or beyond (29 USC 1002(2)(A)).

[220] 29 USC 1021(a)(1). 29 USC 1022 provides for the information required to be contained in the summary plan description, but this section does not make provision for the disclosure of any fees or charges in respect of an employee benefit plan. That disclosure is provided for in 29 CFR 2520.102-3.

[221] 29 USC 1024(b)(1)(A).

[222] In accordance with 29 USC 1029(c).

[223] 29 CFR 2520.102-3(l). CFR means "Code of Federal Regulations" (see note 212 above for a more detailed explanation).

marketplace (see **Appendix USA-1**). The fee disclosure form does not displace the summary plan description.

Individual Retirement Accounts Under the IRC

Individual Retirement Accounts ("**IRAs**") are excluded from the definition of employee pension benefit plans and benefit plans more generally by 29 CFR 2510.3-2(d) and they therefore warrant separate discussion. An IRA is:

> A trust created or organized in the United States for the exclusive benefit of an individual or his beneficiaries, but only if the written governing instrument meets the following requirements:
> (1) …no contribution will be accepted unless it is in cash, and contributions will not be accepted for the taxable year in excess of $2,000 on behalf of any individual.
> (2) The trustee is a bank…or such other person who demonstrates to the satisfaction of the Secretary that the manner in which such other person will administer the trust will be consistent with the requirements of this section.
> (3) No part of the trust funds will be invested in life insurance contracts.
> (4) The interest of an individual in the balance in his account is nonforfeitable.
> (5) The assets of the trust will not be commingled with other property except in a common trust fund or common investment fund. …[225]

The trustee of an IRA is required[226] to provide to investors in such accounts a disclosure statement "at least seven days preceding the earlier of the date of establishment or purchase of the account".[227] In addition to providing a projection of growth of the value of the account,[228] the disclosure statement must also provide a description of:

> (1) Each type of charge, and the amount thereof, which may be made against a contribution, …

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[224] Investment Company Institute, *Financial Services Industries Develop 401(k) Fee Disclosure Form: New Form to Help Employers Identify, Compare Costs of 401(k) Plans* (15 July 1999), http://www.ici.org/issues/401k_fees_commun.html.
[225] 26 USC 408(a).
[226] 26 USC 408(i)(2)(B).
[227] 26 CFR 1.408-6(d)(4)(ii)(A)(1).
[228] Where a projection can reasonably be made (based on a $1,000 investment): 26 CFR 1.408-6(d)(4)(v) – 1.408-6(d)(4)(vii).

(3) Each charge…which may be applied to interest in determining the net amount of money available to the benefited individual and the method of computing each such charge[229]

Additionally, the disclosure statement must provide particulars of any sales commissions charged on contributions to the account, expressed in percentage terms.[230]

It is convenient now to turn to mutual funds as they represent a major investment vehicle for both retirement and non-retirement investors.

INVESTMENT COMPANIES AND MUTUAL FUNDS

Definition

Although the various States maintain their own separate companies and securities regulatory apparatus the SEC has exclusive jurisdiction under the 1933 Act in respect of investment companies, as follows:

Section 18 – Exemption from State Regulation of Securities Offerings

(a) **Scope of Exemption.** Except as otherwise provided in this section, no law, rule, regulation, or order, or other administrative action of any State or any political subdivision thereof—

(1) requiring, or with respect to, registration or qualification of securities, or registration or qualification of securities transactions, shall directly or indirectly apply to a security that—

(A) is a covered security; or

(B) will be a covered security upon completion of the transaction;

…

(b) **Covered Securities.** For the purposes of this section, the following are covered securities:

…

(2) **Exclusive federal registration of investment companies.** A security is a covered security if such security is a security issued by an investment company that is registered, or that has filed a registration statement, under the Investment Company Act of 1940.[231]

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[229] 26 CFR 1.408-6(d)(4)(vii)(A). This heightened level of disclosure is not necessary in all cases under these Regulations.

[230] 26 CFR 1.408-6(d)(4)(v)(D) and (d)(4)(vi)(C). The requirements in each case are slightly different and apply in slightly different circumstances.

Investment companies are defined by the 1940 Act as follows:

> **Section 3 – Definition of Investment Company**
>
> (a) Definitions.
>
> (1) When used in this title, "investment company" means any issuer which –
>
> (A) is or holds itself out as being engaged primarily, or proposes to engage primarily, in the business of investing, reinvesting or trading in securities;[232]

"Issuer" means "every person who issues or proposes to issue any security, or has outstanding any security which it has issued".[233] A "person" is "a natural person or a company",[234] and "company" means "a corporation, a partnership, an association, a joint-stock company, a trust, a fund, or any organized group of persons whether incorporated or not…".[235]

"Security" is defined very broadly as follows to mean:

> any note, stock, treasury stock, security future, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, any put, call, straddle, option, or privilege on any security (including a certificate of deposit) or on any group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency, or, in general, any interest or instrument commonly known as a "security"", or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.[236]

An investment company under the 1940 Act will be one of three types:

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[231] 15 USC 77r.
[232] 15 USC 80a-3.
[233] 15 USC 80a-2(a)(22).
[234] 15 USC 80a-2(a)(28).
[235] 15 USC 80a-2(a)(8).
[236] 15 USC 80a-2(a)(36).

(1) "Face-amount certificate company" means an investment company which is engaged or proposes to engage in the business of issuing face-amount certificates[237] of the installment type, or which has been engaged in such business and has any such certificate outstanding.
(2) "Unit investment trust" means an investment company which (A) is organized under a trust indenture, contract of custodianship or agency, or similar instrument, (B) does not have a board of directors, and (C) issues only redeemable securities, each of which represents an undivided interest in a unit of specified securities; but does not include a voting trust.
(3) "Management company" means any investment company other than a face-amount certificate company or a unit investment trust.[238]

Management companies are further classified into open-end and closed-end companies, defined as follows:

(1) "Open-end company" means a management company which is offering for sale or has outstanding any redeemable security of which it is the issuer.
(2) "Closed-end company" means any management company other than an open-end company.[239]

A "redeemable security" is:

> any security, other than short-term paper, under the terms of which the holder, upon its presentation to the issuer or to a person designated by the issuer, is entitled (whether absolutely or only out of surplus) to receive approximately his proportionate share of the issuer's current net assets, or the cash equivalent thereof.[240]

Mutual funds might therefore be described as federally-regulated investment companies being issuers of redeemable securities.[241]

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[237] "Face-amount certificate" means any certificate, investment contract, or other security which represents an obligation on the part of its issuer to pay a stated or determinable sum or sums at a fixed or determinable date or dates more than twenty-four months after the date of issuance, in consideration of the payment of periodic installments of a stated or determinable amount (which security shall be known as a face-amount certificate of the "installment type"); or any security which represents a similar obligation on the part of a face-amount certificate company, the consideration for which is the payment of a single lump sum (which security shall be known as a "fully paid" face-amount certificate): 15 USC 80a-2(a)(15).
[238] 15 USC 80a-4.
[239] 15 USC 80a-5(a).
[240] 15 USC 80a-2(a)(32).
[241] For the balance of this part of the review, references to investment companies (particularly where such references are in legislation) will be taken to be references to mutual funds. This is because the American legislation does not expressly provide for mutual funds but incorporates them in the manner as described.

Registration of Mutual Funds

The general position is that mutual funds must be registered under s 8 of the 1940 Act[242] in order to transact in securities, whether on the issuer-side or on the investor-side. An investment company becomes registered under the 1940 Act by filing with the SEC a registration statement "containing the following information and documents":

> (1) such copies of the registration statement filed by such company under this subchapter…as the Commission shall designate by rules and regulations; and
>
> (2) such additional information and documents (including a prospectus)[243] as the Commission shall prescribe by rules and regulations as necessary or appropriate in the public interest or for the protection of investors.[244]

The prescribed form for a registration statement under the 1940 Act is known as a Form N-1A ("**the Form**").[245] The SEC has developed Form N-1A to serve the purposes of a registration statement under both the 1933 and 1940 Acts, as well as prescribing the information required to be included in a prospectus for the issuing of securities to the public:

> Form N-1A is to be used by open-end management investment companies…to register under the Investment Company Act of 1940 and to offer their shares under the Securities Act of 1933. The Commission has designed Form N-1A to provide investors with information that will assist them in making a decision about investing in an investment company eligible to use the Form.

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[242] 15 USC 80a-8. 15 USC 80a-7 prohibits investment companies from transacting securities business by way of "interstate commerce" unless registered. 15 USC 80a-8 sets out the registration scheme which requires issuers to lodge the requisite form of registration statement with the SEC.

[243] For the purposes of the 1940 Act (save for one exception not presently relevant), "prospectus" means "a prospectus as defined in the Securities Act of 1933" (15 USC 80a-2(a)(31)), which in turn provides the following definition (15 USC 77b(a)(10)):

> The term "prospectus" means any prospectus, notice, circular, advertisement, letter, or communication, written or by radio or television, which offers any security for sale or confirms the sale of any security; except that (a) a communication sent or given after the effective date of the registration statement (other than a prospectus permitted under subsection (b) of section 77j of this title) shall not be deemed a prospectus if it is proved that prior to or at the same time with such communication a written prospectus meeting the requirements of subsection (a) of section 77j of this title at the time of such communication was sent or given to the person to whom the communication was made, and (b) a notice, circular, advertisement, letter, or communication in respect of a security shall not be deemed to be a prospectus if it states from whom a written prospectus meeting the requirements of section 77j of this title may be obtained and, in addition, does no more than identify the security, state the price thereof, state by whom orders will be executed, and contain such other information as the Commission, by rules or regulations deemed necessary or appropriate in the public interest and for the protection of investors, and subject to such terms and conditions as may be prescribed therein, may permit.

[244] 15 USC 80a-24(a).

[245] 17 CFR 274.11A. There are other forms in respect of other types of investment company.

The Commission also may use the information provided on Form N-1A in its regulatory, disclosure review, inspection, and policy making roles.[246]

Mutual Fund Registration and Prospectus Requirements

The General Instructions to Form N-1A provide an overview of the registration aspect of the Form:

C. Preparation of the Registration Statement

1. Administration of the Form N-1A requirements:

(a) The requirements of Form N-1A are intended to promote effective communication between the Fund and prospective investors. A Fund's prospectus should clearly disclose the fundamental characteristics and investment risks of the Fund, using concise, straightforward, and easy to understand language. A Fund should use document design techniques that promote effective communication. The prospectus should emphasize the Fund's overall investment approach and strategy.

(b) The prospectus disclosure requirements in Form N-1A are intended to elicit information for an average or typical investor who may not be sophisticated in legal or financial matters. The prospectus should help investors to evaluate the risks of an investment and to decide whether to invest in a Fund by providing a balanced disclosure of positive and negative factors. Disclosure in the prospectus should be designed to assist an investor in comparing and contrasting the Fund with other funds.

(c) Responses to the Items in Form N-1A should be as simple and direct as reasonably possible and should include only as much information as is necessary to enable an average or typical investor to understand the particular characteristics of the Fund. The prospectus should avoid: including lengthy legal and technical discussions; simply restating legal or regulatory requirements to which Funds generally are subject; and disproportionately emphasizing possible investments or activities of the Fund that are not a significant part of the Fund's investment operations. Brevity is especially important in describing the practices or aspects of the Fund's operations that do not differ materially from those of other investment companies. Avoid excessive detail, technical or legal terminology, and complex language. Also avoid lengthy sentences and paragraphs that may make the prospectus difficult for many investors to understand and detract from its usefulness.

…

[246] Form N-1A, 1. The Form may be obtained from http://www.sec.gov/divisions/investment/formn1a2versions.htm.

2. Form N-1A is divided into three parts:

(a) *Part A*. Part A includes the information required in a Fund's prospectus under section 10(a) of the Securities Act. The purpose of the prospectus is to provide essential information about the Fund in a way that will help investors to make informed decisions about whether to purchase the Fund's shares described in the prospectus. …

(b) *Part B*. Part B includes the information required in a Fund's SAI.[247] The purpose of the SAI is to provide additional information about the Fund that the Commission has concluded is not necessary or appropriate in the public interest or for the protection of investors to be in the prospectus, but that some investors may find useful. Part B affords the Fund an opportunity to expand discussions of the matters described in the prospectus by including additional information that the Fund believes may be of interest to some investors. The Fund should not duplicate in the SAI information that is provided in the prospectus, unless necessary to make the SAI comprehensible as a document independent of the prospectus.

(c) *Part C*. Part C includes other information required in a Fund's registration statement.[248]

Fees: Specific Requirements for Mutual Fund Prospectuses – Part A

Fee Table

Item 3 of Part A of the Form requires a mutual fund prospectus to include a "Fee Table" as part of the required risk/return summary. In the words of the immediate-past Chairman of the SEC:

> The fee table is intended to present fund investors with expense disclosure that can be understood easily and that facilitates comparison of expenses among funds.
>
> The fee table is a uniform, tabular presentation that shows the fees and charges associated with a mutual fund investment. The table reflects both (i) charges paid directly by a shareholder out of his or her investment, such as front- and back-end sales loads, and (ii) recurring charges deducted from fund assets, such as management fees and 12b-1 fees. The table is located at the beginning of the prospectus. It is accompanied by a numerical example that illustrates the total dollar amounts that an investor could expect to pay on a $10,000 investment if he or she received a 5% annual return and remained invested in the fund for various time periods.[249]

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[247] Statement of Additional Information. See Form N-1A, 5, under the heading "Definitions".

[248] Form N-1A, 6-7. It is unnecessary for the purposes of this review to examine Part C.

[249] House Subcommittee on Finance and Hazardous Materials, Committee on Commerce, Concerning Transparency in the United States Debt Market and Mutual Fund Fees and Expenses,

It is convenient to reproduce the entire fee table requirement and then the ancillary Instructions:

Item 3. Risk/Return Summary: Fee Table

Include the following information, in plain English under rule 421(d) under the Securities Act, after Item 2 (unless the Fund offers its shares exclusively to one or more separate accounts):

Fees and expenses of the Fund

This table describes the fees and expenses that you may pay if you buy and hold shares of the Fund.

Shareholder Fees (fees paid directly from your investment)

Maximum Sales Charge (Load) Imposed on Purchases (as a percentage of offering price)	_____%
Maximum Deferred Sales Charge (Load) (as a percentage of ____)	_____%
Maximum Sales Charge (Load) Imposed on Reinvested Dividends [and other Distributions] (as a percentage of ____)	_____%
Redemption Fee (as a percentage of amount redeemed, if applicable)	_____%
Exchange Fee	_____%
Maximum Account Fee	_____%

Annual Fund Operating Expenses (expenses that are deducted from Fund assets)

Management Fees		_____%
Distribution [and/or Service] (12b-1) Fees		_____%
Other Expenses		_____%
_____	_____%	
_____	_____%	
_____	_____%	
Total Annual Fund Operating Expenses		_____%

Example

This Example is intended to help you compare the cost of investing in the Fund with the cost of investing in other mutual funds.

The Example assumes that you invest $10,000 in the Fund for the time periods indicated and then redeem all of your shares at the end of those periods. The Example also assumes that your investment has a 5% return each year and that the Fund's operating expenses remain the same. Although your actual costs may be higher or lower, based on these assumptions your costs would be:

1 year	3 years	5 years	10 years
$_____	$_____	$_____	$_____

You would pay the following expenses if you did not redeem your shares:

1 year	3 years	5 years	10 years
$_____	$_____	$_____	$_____

The Example does not reflect sales charges (loads) on reinvested dividends [and other distributions]. If these sales charges (loads) were included, your costs would be higher.

The Instructions ancillary to the fee table requirement are as follows:[250]

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http://www.sec.gov/news/testimony/testarchive/1998/tsty1398.htm (29 September 1998) under heading B.2. "Regulatory Framework for Mutual Fund Fees: Disclosure Requirements" (note omitted).

[250] Paragraph 3(d) of the Instructions to the fee table has been omitted.

Form N-1A, Item 3, Instructions to the Fee Table

2. *Shareholder Fees.*

(a) (i) "Maximum Deferred Sales Charge (Load)" includes the maximum total deferred sales charge (load) payable upon redemption, in installments, or both, expressed as a percentage of the amount or amounts stated in response to Item 8(a), except that, for a sales charge (load) based on net asset value at the time of purchase, show the sales charge (load) as a percentage of the *offering price* at the time of purchase. A Fund may include in a footnote to the table, if applicable, a tabular presentation showing the amount of deferred sales charges (loads) over time or a narrative explanation of the sales charges (loads) (*e.g.*, __% in the first year after purchase, declining to __% in the __ year and eliminated thereafter).

(ii) If more than one type of sales charge (load) is imposed (*e.g.*, a deferred sales charge (load) and a front-end sales charge (load)), the first caption in the table should read "Maximum Sales Charge (Load)" and show the maximum cumulative percentage. Show the percentage amounts and the terms of each sales charge (load) comprising that figure on separate lines below.

(iii) If a sales charge (load) is imposed on shares purchased with reinvested capital gains distributions or returns of capital, include the bracketed words in the third caption.

(b) "Redemption Fee" includes a fee charged for any redemption of the Fund's shares, but does not include a deferred sales charge (load) imposed upon redemption.

(c) "Exchange Fee" includes the maximum fee charged for any exchange or transfer of interest from the Fund to another fund. The Fund may include in a footnote to the table, if applicable, a tabular presentation of the range of exchange fees or a narrative explanation of the fees.

(d) "Maximum Account Fees." Disclose account fees that may be charged to a typical investor in the Fund; fees that apply to only a limited number of shareholders based on their particular circumstances need not be disclosed. Include a caption describing the maximum account fee (*e.g.*, "Maximum Account Maintenance Fee" or "Maximum Cash Management Fee"). State the maximum annual account fee as either a fixed dollar amount or a percentage of assets. Include in a parenthetical to the caption the basis on which any percentage is calculated. If an account fee is charged only to accounts that do not meet a certain threshold (*e.g.*, accounts under $5,000), the Fund may include the threshold in a parenthetical to the caption or footnote to the table. The Fund may include an explanation of any non-recurring account fee in a parenthetical to the caption or in a footnote to the table.

3. *Annual Fund Operating Expenses.*

(a) "Management Fees" include investment advisory fees (including any fees based on the Fund's performance), any other management fees payable to the investment adviser or its affiliates, and administrative fees payable to the investment adviser or its affiliates that are not included as "Other Expenses."

(b) "Distribution [and/or Service] (12b-1) Fees" include all distribution or other expenses incurred during the most recent fiscal year under a plan adopted pursuant to rule 12b-1 [17 CFR 270.12b-1]. Under an appropriate caption or a subcaption of "Other Expenses," disclose the amount of any distribution or similar expenses deducted from the Fund's assets other than pursuant to a rule 12b-1 plan.

(c) (i) "Other Expenses" include all expenses not otherwise disclosed in the table that are deducted from the Fund's assets or charged to all shareholder accounts. The amount of expenses deducted from the Fund's assets are the amounts shown as expenses in the Fund's statement of operations (including increases resulting from complying with paragraph 2(g) of rule 6-07 of Regulation S-X [17 CFR 210.6-07]).

(ii) "Other Expenses" do not include extraordinary expenses as determined under generally accepted accounting principles (*see* Accounting Principles Board Opinion No. 30). If extraordinary expenses were incurred that materially affected the Fund's "Other Expenses," disclose in a footnote to the table what "Other Expenses" would have been had the extraordinary expenses been included.

(iii) The Fund may subdivide this caption into no more than three subcaptions that identify the largest expense or expenses comprising "Other Expenses," but must include a total of all "Other Expenses." Alternatively, the Fund may include the components of "Other Expenses" in a parenthetical to the caption.

(e) The Fund may reflect actual operating expenses that include expense reimbursement or fee waiver arrangements in a footnote to the table. If the Fund provides this disclosure, also disclose the period for which the expense reimbursement or fee waiver arrangement is expected to continue, or whether it can be terminated at any time at the option of the Fund.

4. *Example.*

(a) Assume that the percentage amounts listed under "Annual Fund Operating Expenses" remain the same in each year of the 1-, 3-, 5-, and 10-year periods, except that an adjustment may be made to reflect reduced annual expenses resulting from completion of the amortization of initial organization expenses.

(b) For any breakpoint in any fee, assume that the amount of the Fund's assets remains constant as of the level at the end of the most recently completed fiscal year.

(c) Assume reinvestment of all dividends and distributions.

(d) Reflect recurring and non-recurring fees charged to all investors other than any exchange fees or any sales charges (loads) on shares purchased with reinvested dividends or other distributions. If sales charges (loads) are imposed on reinvested dividends or other distributions, include the narrative explanation following the Example and include the bracketed words when sales charges (loads) are charged on reinvested capital gains distributions or returns of capital. Reflect any shareholder account fees collected by more than one Fund by dividing the total amount of the fees collected during the most recent fiscal year for all Funds whose shareholders are subject to the fees by the total average net assets of the Funds. Add the resulting percentage to "Annual Fund Operating Expenses" and assume that it remains the same in each of the 1-, 3-, 5-, and 10-year periods. A Fund that charges account fees based on a minimum account requirement exceeding $10,000 may adjust its account fees based on the amount of the fee in relation to the Fund's minimum account requirement.

(e) Reflect any deferred sales charge (load) by assuming redemption of the entire account at the end of the year in which the sales charge (load) is due. In the case of a deferred sales charge (load) that is based on the Fund's net asset value at the time of payment, assume that the net asset value at the end of each year includes the 5% annual return for that and each preceding year.

(f) Include the second 1-, 3-, 5-, and 10-year periods and related narrative explanation only if a sales charge (load) or other fee is charged upon redemption.

The following observations may be made in respect of the fee table instructions:

- Itemisation – Item 3, Instructions para 2(a)(ii): where more than one type of sales charge is imposed, the table requires the charges to be cumulated and then component-itemised for analysis.
- Dollars or percentages
  - ♦ Exchange Fees [switching fees] – Item 3, Instructions para 2(c): the Instructions require disclosure of the maximum fee charge, which can be expressed in either actual dollar amounts or percentages.
  - ♦ Maximum Account Fees – Item 3, Instructions para 2(d): this item may be expressed in either dollar or percentage terms at the discretion of the issuer.
- Itemisation of Other Expenses – Item 3, Instructions para 3(c)(iii): the Instructions require this item to be subdivided into constituent subitems, but do not permit more than three such constituent subitems (being the largest such subitems) to be broken-out and identified. The alternative permitted by the Instructions (a parenthetical to the line item listing the constituents) is not as transparent as that provides no guidance as to the relative values of each constituent.

More generally, the fee table requirement is useful in enabling a prospective investor to identify the correct source of funding for their involvement in the fund. The fee table breaks up the investment in two main parts: investor fees, which are paid directly out of the investment corpus, and annual fund operating expenses, which are paid from fund assets. The former indicate to the investor what it will cost to get into or exit the fund; the latter indicate how much the fund costs to run. This is helpful for comparing funds: a fund which may ultimately be cheaper to enter may have greater ongoing expenses than other similar funds. The fund operating expenses figure is also somewhat more comprehensive than MER, which does not include commissions which the fee table would incorporate under the line item in respect of 12b-1 fees.

The example will probably not match the investment actually sought to be invested. In addition, the example does not give a simple indication of the dollar amount of expenses incurred by the fund manager on an annual basis.

Management's Discussion of Fund Performance

The prospectus is required to provide information under this heading unless the fund is a money market fund or the information is contained in a fund's annual report which is provided to prospectus recipients upon request.

The requisite information under this heading is to be disclosed in a line graph and must reflect (*inter alia*) the following:

- Sales loads – Item 5, Instructions para 2: the instructions simply posit that in the case of sales commissions, the line graph be computed so as to accurately reflect the effect of the commission. For example, in the case of up-front commissions deducted from the investment corpus, the graph should reflect investment results on the basis of the net amount available for investment. Similarly, for deferred sales loads, the graph should reflect the effect of deducting the loads from the investment account balance at the requisite deferral interval points.
- Account fees – Item 5, Instructions para 4: the graph must reflect the effect of any recurring account fees.

Management, Organisation and Capital Structure

Under this heading, the prospectus is required to describe the compensation paid to each investment adviser of the fund for the most recent fiscal year. The disclosure is to state the aggregate fee paid expressed as a percentage of average net assets or, if some other basis is used for calculating the adviser's fee, then that other basis must be described.[251]

[251] Form N-1A, Item 6(a)(1)(ii).

Shareholder Information

The prospectus must disclose to investors the procedures for redeeming shares in the mutual fund, including:

- Redemption charges – Item 7, para (c)(2): the collection method and the circumstances in which the charges will be waived must be disclosed.
- Broker-dealer redemption – Item 7, para (c)(4): if the fund permits investors to sell shares through a broker-dealer, the prospectus must note any charges that may be imposed for such a service. The Instruction to this particular requirement provides that the specific fee itself need not be disclosed.
- Street name accounts – Item 7, para (c)(7): any costs associated with transferring from street name accounts must be disclosed. A street name is the default registration position for purchasers of securities. Legal title to the securities is vested in the name of the broker effecting the purchase, with the security certificate noting the purchaser as the beneficial owner of the securities.[252]

Distribution Arrangements

There are two aspects to disclosure in respect of distribution arrangements: sales loads[253] and Rule 12b-1 fees.

- Sales loads – Item 8, para (a)(1): sales loads (including deferred sales loads) that apply to purchases of shares in the mutual fund must be described. Front-end loads (commissions deducted from the investment corpus immediately prior to investment) must be disclosed in tabular form as a percentage of both the offering price and the net amount invested. The Instructions to this particular requirement are as follows:

[252] SEC, *Holding Your Securities – Get The Facts*, http://www.sec.gov/investor/pubs/holdsec.htm.

[253] The 1940 Act (15 USC 80a-2(a)(35)) defines a sales load as:

> the difference between the price of a security to the public and that portion of the proceeds from its sale which is received and invested or held for investment by the issuer…less any portion of such difference deducted for trustee's or custodian's fees, insurance premiums, issue taxes, or administrative expenses or fees which are not properly chargeable to sales or promotional activities.

Instructions.

1. If the Fund's shares are sold subject to a front-end sales load, explain that the term "offering price" includes the front-end sales load.

2. Disclose, if applicable, that sales loads are imposed on shares, or amounts representing shares, that are purchased with reinvested dividends or other distributions.

3. Discuss, if applicable, how deferred sales loads are imposed and calculated, including:

   (a) Whether the specified percentage of the sales load is based on the offering price, or the lesser of the offering price or net asset value at the time the sales load is paid.

   (b) The amount of the sales load as a percentage of both the offering price and the net amount invested.

   (c) A description of how the sales load is calculated (*e.g.*, in the case of a partial redemption, whether or not the sales load is calculated as if shares or amounts representing shares not subject to a sales load are redeemed first, and other shares or amounts representing shares are then redeemed in the order purchased).

   (d) If applicable, the method of paying an installment sales load (*e.g.*, by withholding of dividend payments, involuntary redemptions, or separate billing of a shareholder's account).

Disclosure of sales loads must also include description of any arrangements that result in the elimination of sales loads (eg: letters of intent, accumulation plans, dividend reinvestment plans, withdrawal plans, exchange privileges, employee benefit plans and redemption reinvestment plans).[254]

- Rule 12b-1 fees – Item 8, para (b): the prospectus must disclose any fees for distribution of fund shares which have been authorised by a plan adopted pursuant to Rule 12b-1.[255] The Rule is pursuant to s 12(b) of the 1940 Act,[256] which prohibits registered open-end companies from acting as the distributors of their own securities (except through an underwriter) unless such companies comply with any rules prescribed by the Commission as necessary or appropriate in the public interest or for the protection of investors.

  Rule 12b-1 prohibits a mutual fund from making payments in respect of the distribution of fund shares (eg: advertising, compensation of dealers and sales personnel, printing and mailing) where the fund is also the distributor unless the fund has first adopted "a written plan describing all material aspects of the proposed financing of distribution" and the plan has been approved by a majority of the outstanding voting securities and of the board of directors, and the plan

[254] Form N-1A, Item 8(a)(2).
[255] 17 CFR 270.12b-1.
[256] 15 USC 80a-12(b).

will not continue in effect for more than a year unless approved annually by the said majorities.[257]

Disclosure of such fees in the fund prospectus, in addition to the disclosure mandated by the fee table, requires stating the amount of the distribution under the plan and statements to the following effect:[258]

> (1) The Fund has adopted a plan under rule 12b-1 that allows the Fund to pay distribution fees for the sale and distribution of its shares; and
>
> (2) Because these fees are paid out of the Fund's assets on an on-going basis, over time these fees will increase the cost of your investment and may cost you more than paying other types of sales charges.

- Dealer compensation: for the purposes of clarification, it should be noted that the National Association of Securities Dealers ("**NASD**") has imposed upon its members specific rules in respect of the compensation (in the form of sales charges) allowable for and permitted sales practices in respect of the distribution of mutual fund shares.[259]

  Rule 2830(d) of the NASD Rules provides that:

> No member shall offer or sell the shares of any open-end investment company…if the sales charges described in the prospectus are excessive. Aggregate sales charges shall be deemed excessive if they do not conform to the following provisions:
>
> (1) Investment Companies Without an Asset-Based Sales Charge
>
> (A) Aggregate front-end and deferred sales charges described in the prospectus…shall not exceed 8.5% of the offering price.
>
> …
>
> (2) Investment Companies With an Asset-Based Sales Charge
>
> (E) No member shall offer or sell the shares of an investment company with an asset-based sales charge if:
>
> (i) The amount of the asset-based sales charge exceeds .75 of 1% per annum of the average annual net assets of the investment company; …
>
> …

[257] 17 CFR 270.12b-1(b).

[258] Form N-1A, Item 8(b). If the Rule 12b-1 plan also encompasses service fees, then the Instructions require the statements to be modified accordingly.

[259] NASD Rule 2830: "Investment Company Securities". The NASD Manual (incorporating the NASD Rules) can be accessed at http://www.nasdr.com/nasd_manual.htm, and then selecting the Books on Screen internet version of the Manual.

(5) No member…shall offer or sell the securities of an investment company if the service fees paid by the investment company, as disclosed in the prospectus, exceed .25 of 1% of its average annual net assets or if a service fee paid by the investment company, as disclosed in the prospectus, to any person who sells its shares exceeds .25 of 1% of the average annual net asset value of such shares.[260]

It appears from the foregoing NASD Rule that, in the case of investment companies having an asset-based sales charge, there is a cap on Rule 12b-1 fees in the order of 1% of average net assets, being the aggregate of 0.75% in respect of distribution expenses and 0.25% in respect of service fees. The Rule is a conduct rule, which prohibits NASD members from selling or offering for sale fund shares where the Rule 12b-1 component fees exceed the allowable caps.

Financial Highlights Information – Ratios and Supplemental Data

Item 9 of the Form requires the prospectus to provide, in comparative columnar form, ratios in respect of a range of financial indicators over at least the immediately preceding five year period. The ratios must be preceded by the following narrative:

Financial Highlights

The financial highlights table is intended to help you understand the Fund's financial performance for the past 5 years [or, if shorter, the period of the Fund's operations]. Certain information reflects financial results for a single Fund share. The total returns in the table represent the rate that an investor would have earned [or lost] on an investment in the Fund (assuming reinvestment of all dividends and distributions). This information has been audited by _____, whose report, along with the Fund's financial statements, are included in [the SAI or annual report], which is available upon request.

[260] NASD Rule 2830(b) provides definitions of "sales charge" and "service fees" as follows:

(8) "Sales charge" and "sales charges," as used in paragraph (d), shall mean all charges or fees that are paid to finance sales or sales promotion expenses, including front-end, deferred and asset-based sales charges, excluding charges and fees for ministerial, recordkeeping or administrative activities and investment management fees. For purposes of this Rule, members may rely on the sales-related fees and charges disclosed in the prospectus of an investment company.
   (A) An "asset-based sales charge" is a sales charge that is deducted from the net assets of an investment company and does not include a service fee.
   (B) A "deferred sales charge" is any amount properly chargeable to sales or promotional expenses that is paid by a shareholder after purchase but before or upon redemption.
   (C) A "front-end sales charge" is a sales charge that is included in the public offering price of the shares of an investment company.

(9) "Service fees," as used in paragraph (d), shall mean payments by an investment company for personal service and/or the maintenance of shareholder accounts.

Of greatest interest for the purposes of this review is the ratio of expenses to average net assets. Average net assets are to be based on "the value of net assets determined no less frequently than the end of each month".[261]

Additional Requirements for Mutual Fund Prospectuses – Part B

The registration statement requires the preparation of a Statement of Additional Information ("**SAI**") which, as discussed,[262] provides additional information which the SEC has determined is not necessary in the interests of investor protection but may be useful to those seeking more detail.

The SAI provides disclosure of the following in respect of fees and charges associated with investments in mutual funds:

- Investment Advisory and Other Services – Item 15:
  - Advisers: the SAI is required to disclose the method of calculating the advisory fee payable by the fund including total dollar amounts paid to the adviser for the last three years.[263] Disclosure should also include any credits which reduced those payments,[264] as well as any expense limitation provision.[265] If the fee payable by the fund varies in accordance with the fund's investment performance in relation to a stated investment standard or benchmark, the SAI must describe that standard and provide a tabular fee schedule. Examples may also be shown to illustrate the way in which investment performance will ultimately affect the advisor's fee, provided that the examples show the maximum and minimum fee percentages that could be earned.[266]
  - Service agreements: the SAI must summarise the substantive provisions of any management-related service contract that may be of interest to investors, indicating the total dollar amount paid under any contracts for the past three years.[267]

[261] Form N-1A, Item 9, Instructions, para 4(a).
[262] See above n 247 and text thereto.
[263] Form N-1A, Item 15(a)(3)(i).
[264] Form N-1A, Item 15(a)(3)(ii).
[265] Form N-1A, Item 15(a)(3)(iii).
[266] Form N-1A, Item 15(a)(3), Instructions, para 1.
[267] Form N-1A, Item 15(d).

- Other advice: if persons other than directors, employees, appointed advisers and the like regularly advise the fund in return for some form of remuneration, those persons must be disclosed in the SAI together with the remuneration paid for the advice over the last three years.[268]
- Dealer reallowances: the SAI must disclose any front-end sales load reallowed to dealers, expressed as a percentage of the offering price for fund shares.[269]
- Rule 12b-1 plans: if the fund has adopted such a plan, the SAI must describe the material aspects of the plan including a list of the principal activities for which payments are or will be made, including the dollar amount paid during the last fiscal year.[270] Disclosure under this requirement also requires an indication of whether the fund merely reimburses the distributor or pays compensation regardless of the distributor's expenses,[271] disclosure of any unreimbursed expenses incurred in the previous year to be carried over (in dollars and as a percentage of net assets),[272] and the method of splitting shared or joint distribution costs where the fund engages in joint distribution with another fund series or fund issuer.[273]
- Other service providers: unless disclosed in response to the requirements under the heading "Service agreements", the SAI must identify any person who provides significant administrative or business affairs management services and the compensation paid for such services.[274]

- Brokerage Allocation and Other Practices – Item 16:
  - Brokerage: the SAI is required to disclose the aggregate amount of any brokerage commissions paid by the fund during the previous 3 fiscal years.[275]
  - Commissions: the SAI is required to state the aggregate dollar amount of brokerage commissions paid by the fund during the three preceding years to any broker affiliated with the fund directly or via another person affiliated

[268] Form N-1A, Item 15(e).
[269] Form N-1A, Item 15(f).
[270] Form N-1A, Item 15(g)(1). Activities including advertising, printing and mailing, compensating underwriters, broker-dealers and sales personnel, and interest, carrying or other financing charges.
[271] Form N-1A, Item 15(g)(2).
[272] Form N-1A, Item 15(g)(3).
[273] Form N-1A, Item 15(g)(4).
[274] Form N-1A, Item 15(h)(1).

with the fund.[276] This more-specific disclosure simply requires that, where brokerage is paid to affiliates, the SAI discloses that fact and the percentage of the aggregate brokerage so paid to each affiliate, in addition to the percentage of the fund's aggregate dollar amount of transactions involving commission payments so effected through affiliated brokers.[277]

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[275] Form N-1A, Item 16(a).
[276] Form N-1A, Item 16(b)(1).
[277] Form N-1A, Item 16(b)(2).

SAMPLE PROSPECTUSES

The *Credit Suisse Funds Prospectus* (1 January 2002) in respect of the "Global Health Sciences Fund" and the "Global Technology Fund" provides the following fee table:

INVESTOR EXPENSES

FEES AND FUND EXPENSES

This table describes the fees and expenses you may bear as a shareholder. Annual fund operating expense figures are for the fiscal year or period ended August 31, 2001.

	GLOBAL HEALTH SCIENCES FUND	GLOBAL TECH-NOLOGY FUND
Shareholder fees (paid directly from your investment)		
Sales charge "load" on purchases	**NONE**	**NONE**
Deferred sales charge "load"	**NONE**	**NONE**
Sales charge "load" on reinvested distributions	**NONE**	**NONE**
Redemption fees	**NONE**	**NONE**
Exchange fees	**NONE**	**NONE**
Annual fund operating expenses (deducted from fund assets)		
Management fee	1.00%	1.00%
Distribution and service (12b-1) fee	.25%	.25%
Other expenses	.61%	.57%
Total annual fund operating expenses*	1.86%	1.82%

* Fee waivers and expense reimbursements or credits reduced expenses for the funds during 2001 but may be discontinued at any time. Actual fees and expenses for the fiscal year or period ended August 31, 2001 are shown below:

EXPENSES AFTER WAIVERS AND REIMBURSEMENTS	GLOBAL HEALTH SCIENCES FUND	GLOBAL TECH-NOLOGY FUND
Management fee	.74%	.89%
Distribution and service (12b-1) fee	.25%	.25%
Other expenses	.60%	.51%
Total annual fund operating expenses	1.59%	1.65%

EXAMPLE

This example may help you compare the cost of investing in these funds with the cost of investing in other mutual funds. Because it uses hypothetical conditions, your actual costs may be higher or lower.

Assume you invest $10,000, each fund returns 5% annually, expense ratios remain as listed in the first table on the opposite page (before fee waivers and expense reimbursements or credits), and you close your account at the end of each of the time periods shown. Based on these assumptions, your cost would be:

	ONE YEAR	THREE YEARS	FIVE YEARS	10 YEARS
GLOBAL HEALTH SCIENCES FUND	$189	$585	$1,006	$2,180
GLOBAL TECHNOLOGY FUND	$185	$573	$985	$2,137

The Financial Highlight Information mandated by Item 9 of Form N-1A is as follows; it includes the ratio of expenses to average net assets:

FINANCIAL HIGHLIGHTS

The figures below have been audited by the fund's independent auditors, PricewaterhouseCoopers LLP, whose report on the fund's financial statements is included in the *Annual Report*.

PERIOD ENDED:	8/01	8/00	8/99	8/98	8/97[1]
Per-share data					
Net asset value, beginning of period	$69.11	$41.22	$20.54	$17.30	$15.00
Investment activities:					
Net investment income/(loss)	(0.75)	(0.44)	(0.04)	(0.01)	0.02
Net gains or losses on investments (both realized and unrealized)	(36.86)	29.56	23.56	4.29	2.28
Total from investment activities	(37.61)	29.12	23.52	4.28	2.30
Distributions:					
From realized capital gains	(2.39)	(1.23)	(2.84)	(1.04)	–
Total distributions	(2.39)	(1.23)	(2.84)	(1.04)	
Net asset value, end of period	$29.11	$69.11	$41.22	$20.54	$17.30
Total return	(55.72)%	70.99%	120.73%	25.38%	15.33%[2]
Ratios and supplemental data					
Net assets, end of period (000s omitted)	$147,504	$471,455	$65,165	$718	$569
Ratio of expenses to average net assets	1.67%[3]	1.66%[3]	1.65%	1.65%	1.65%[4]
Ratio of net income to average net assets	(1.14)%	(0.89)%	(0.35)%	(0.03)%	0.16%[4]
Decrease reflected in above operating expense ratios due to waivers/reimbursements	0.15%	0.11%	0.87%	5.21%	6.73%[4]
Portfolio turnover rate	100%	143%	203%	169%	43%

[1] For the period December 4, 1996 (commencement of operations) through August 31, 1997.
[2] Not annualized.
[3] Interest earned on uninvested cash balances is used to offset portions of the transfer agent expense. These arrangements resulted in a reduction to the net expense ratio by .02% for the year ended August 31, 2001, and 2000, respectively. The operating expense ratio after reflecting these arrangements was 1.64% for each of the years ended August 31, 2001 and 2000.
[4] Annualized.

The *Ariston Internet Convertible Fund – Elite Shares Prospectus* (1 May 2001) provides the following fee table:[278]

FEES AND EXPENSES OF INVESTING IN THE FUNDS

The tables describe the fees and expenses that you may pay if you buy and hold shares of the Fund.

	Convertible Securities Fund	Internet Convertible Fund Elite Shares
Shareholder Fees (fees paid directly from your investment)		
Maximum Sales Charge (Load) Imposed on Purchases	NONE	NONE
Maximum Deferred Sales Charge (Load)	NONE	NONE
Redemption Fee	NONE	NONE
Exchange Fee	NONE	NONE
Annual Fund Operating Expenses (expenses that are deducted from Fund assets)		
Management Fees1	2.24%	2.08%
Distribution (12b-1) Fees[2]	0.00%	NONE
Other Expenses	0.01%	0.17%
Total Annual Fund Operating Expenses	2.25%	2.25%

[1] The management fee is equal to 2.25% of the average value of the daily net assets of the Ariston Internet Convertible Fund, minus Trustee fees allocated to the Fund. The Trustee fees are allocated between the classes based on their relative net assets, and because the relative net assets varied over the fiscal period, there is a difference in the Trustee fees expressed as a percentage of daily net assets for the two classes, and thus a difference in the management fee expressed as a percentage of daily net assets.

[2] The Ariston Convertible Securities Fund has adopted a 12b-1 Plan that permits the Fund to charge 12b-1 fees of up to 0.25% annually. The Fund's expenses will not be affected by the 12b-1 Plan because the Fund's advisor does not intend to activate the Plan through April 30, 2002.

Example:

The example below is intended to help you compare the cost of investing in the Funds with the cost of investing in other mutual funds. The example uses the same assumptions as other mutual fund prospectuses: a $10,000 initial investment for the time periods indicated, reinvestment of dividends and distributions, 5% annual total return, constant operating expenses, and sale of all shares at the end of each time period. Although your actual expenses may be different, based on these assumptions your costs will be:

	1 year	3 years	5 years	10 years
Convertible Securities Fund	$236	$728	$1245	$2664
Internet Convertible Fund Elite Shares	$236	$728	$1245	$2664

[278] The prospectus is also a prospectus in respect of a broader convertible securities fund, hence the additional fee table information in respect of the Convertible Securities Fund.

Financial Highlight Information, including the ratio of expenses to average net assets, is as follows:

Ariston Internet Convertible Fund - Elite Shares

	Period ended Dec. 31, 2000 (a)
Selected Per Share Data	
Net asset value, beginning of period	$ 10.00
Income from investment operations:	
Net investment loss	(0.13)
Net realized and unrealized gain (loss) on investments	(2.16)
Total from investment operations	(2.29)
Less distributions:	
Distributions from net investment income	0.00
Distributions from net realized gains	0.00
Total distributions	0.00
Net asset value, end of period	$ 7.71
Total Return	(22.90)% (b)
Ratios and Supplemental Data	
Net assets, end of period (000)	$666
Ratio of expenses to average net assets	2.25% (c)
Ratio of net investment income to average net assets	(2.02)% (c)
Portfolio turnover rate	40.64% (c)

(a) May 1, 2000 (commencement of operations) through December 31, 2000.
(b) For a period of less than a full year, the total return is not annualized.
(c) Annualized

The *CSI Capital Management Prospectus* (2 January 2002) in respect of the "CSI Equity Fund – Investor Shares" and the "CSI Fixed Income Fund" provides the following fee table:

FEES AND EXPENSES

Costs are an important consideration in choosing a mutual fund. Shareholders indirectly pay the costs of operating a Fund, plus any transaction costs associated with buying and selling the securities a Fund holds. These costs will reduce a portion of the gross income or capital appreciation a Fund achieves. Even small differences in these expenses can, over time, have a significant effect on a Fund's performance.

The following table describes the fees and expenses that you will pay directly or indirectly in connection with an investment in each of the Funds. The annual operating expenses, which cover the costs of investment management, administration, accounting and shareholder communications, are shown as an annual percentage of the average daily net assets.

Shareholder Transaction Fees (fees paid directly from your investment)

	Equity Fund Investor Shares	Fixed Income Fund
Maximum Sales Charge (Load) Imposed on Purchases	5.75%(1)	None
Maximum Deferred Sales Charge (Load) Imposed on Certain Redemptions	1.00%(2)	None
Sales Charge (Load) Imposed on Reinvested Dividends	None	None
Redemption Fees(3)	None	None
Exchange Fees(4)	None	None

Annual Operating Expenses (Expenses that are deducted from the Funds' assets)

	Equity Fund Investor Shares	Fixed Income Fund
Management Fee	1.00%	1.00%
Distribution and Service (12b-1) Fees	None	None
Other Operating Expenses	0.45%	0.48%
Total Fund Operating Expenses	1.45%	1.48%(5)

(1) As a percentage of offering price. Reduced rates apply to purchases of Investor Shares over $50,000, and the sales charge is waived for certain classes of investors. An investor who has paid a front-end sales charge will not be subject to a contingent deferred sales charge.

(2) If you are in a category of investors who may purchase Investor Shares without a front-end sales charge, you will be subject to a 1.00% contingent deferred sales charge if you redeem your shares within one year of purchase.

(3) A shareholder electing to redeem shares by telephone will be charged $10 for each such redemption request.

(4) A shareholder may be charged a $10 fee for each telephone exchange.

(5) The investment adviser has voluntarily agreed to waive fees and/or reimburse expenses so that the ratio of total operating expenses for the Fixed Income Fund do not exceed 1.00% of the average daily net assets through August 31, 2002.

Example:

The following expense example shows the expenses that you could pay over time. It will help you compare the costs of investing in the Funds with the cost of investing in other mutual funds. The example assumes that you invest $10,000 in a Fund, you reinvest all dividends and distributions in additional shares of the Funds, you redeem all of your shares at the end of the periods indicated, you earn a 5.00% annual return, and each Fund's operating expenses remain the same. Because actual return and expenses will be different, the example is for comparison only.

Based on these assumptions, your costs would be:

	1 Year	3 Years	5 Years	10 Years
Equity Fund—Investor Shares(1)(2)	$714	$1,007	$1,322	$2,210
Fixed Income Fund(3)	$151	$ 468	$ 808	$1,768

(1) The above example assumes payment of the maximum initial sales charge of 5.75% at the time of purchase. The sales charge varies depending upon the amount of Investor Shares that an investor purchases. Accordingly, your actual expenses may vary. If you are in a category of investors who purchase Investor Shares without a front-end sales charge and you redeem your shares at the end of one year, your costs would be $248.

(2) If you are in a category of investors who purchase Investor Shares without a front-end sales charge, and you hold your shares for more than one year, your costs would be:

	1 Year	3 Years	5 Years	10 Years
Equity Fund—Investor Shares	$148	$459	$792	$1,735

(3) Should the investment adviser continue the voluntary operating expense limitation for the periods shown below, your costs would be:

	1 Year	3 Years	5 Years	10 Years
Fixed Income Fund	$102	$318	$552	$1,225

Information in respect of sales charges for "Investor Shares of the Equity Fund" is as follows:

Sales Charges—Investor Shares of the Equity Fund

If you purchase your Investor Shares through a broker-dealer, the broker-dealer firm is entitled to receive a percentage of the sales charge you pay in order to purchase Investor Shares. The following schedule governs the percentage to be received by the selling broker-dealer firm.

Amount of Purchase At the Public Offering Price	Sales Charge as a Percentage of Offering Price	Sales Charge as a Percentage of Net Amount Invested	Dealer Discount as Percentage of Offering Price
Less than $50,000	5.75%	6.10%	5.00%
$50,000 but less than $100,000	4.50%	4.71%	3.75%
$100,000 but less than $250,000	3.50%	3.63%	2.75%
$250,000 but less than $500,000	2.50%	2.56%	2.00%
$500,000 but less than $1,000,000	2.00%	2.04%	1.75%
$1,000,000 or more	1.00%	1.01%	1.00%

The Financial Highlight information for the "Equity Fund", including the ratio of expenses to average net assets, is as follows:

EQUITY FUND—INVESTOR SHARES

FOR A SHARE OUTSTANDING THROUGHOUT EACH PERIOD

Investor Class Shares

	Years ended August 31, 2001	Years ended August 31, 2000	Years ended August 31, 1999	Period ended August 31, 1998*
Per Share Operating Performance				
Net asset value, beginning of period	**$ 18.37**	**$ 13.36**	**$ 9.88**	**$ 10.00**
Income from investment operations—				
Net investment income (loss)	0.01	(0.02)	(0.02)	0.02
Net realized and unrealized gain (loss) on investments	(3.45)	5.03	3.52	(0.14)
Total from investment operations	**(3.44)**	**5.01**	**3.50**	**(0.12)**
Less distributions—				
Distributions from net investment income	—	—	(0.02)	—
Distributions from capital gains	(1.31)	—	—	—
Total distributions	(1.31)	—	(0.02)	—
Net asset value, end of period	**$ 13.62**	**$ 18.37**	**$ 13.36**	**$ 9.88**
Total Return	**(19.32)%**	**37.50%**	**35.21%**	**(1.20)%**
Ratios/Supplemental Data				
Net assets, end of period (000's)	$104,283	$113,673	$52,924	$26,576
Ratio to average net assets—				
Expenses (A)	1.45%	1.44%	1.50%	1.50%**
Expenses—net (B)	1.44%	1.44%	1.50%	1.49%**
Net investment income (loss)	0.06%	(0.14)%	(0.15)%	0.42%**
Portfolio turnover rate	17.16%	22.69%	12.91%	8.16%

* Commencement of operations of the Investor Shares was October 14, 1997.

** Annualized

(A) The expense ratio has been increased to include custodian fees which were offset by custodian credits for the period ended August 31, 1998 and for the year ended August 31, 2001.

(B) The expense ratio—net reflects the effect of the custodian fee credits the Fund received for the period ended August 31, 1998 and for the year ended August 31, 2001.

MUTUAL FUND FEE CALCULATOR

According to the SEC, uniform disclosure in the form of the fee table is insufficient and thus "the Commission has mounted an extensive investor education campaign to improve the financial literacy of investors" [279] with respect to mutual funds and their costs.

> One concern that runs through all of the disclosure initiatives that the Commission has undertaken with regard to mutual funds and variable products is that fees and charges be clearly disclosed to the investor.
>
> In this regard, the Commission recently developed and placed on its website the Mutual Fund Cost Calculator, which is designed to close the gap between the fee table for mutual funds and investors' ability to use the fee table to make a real-world investment decision. Using the new tool, an investor can sit down with the prospectus for a fund he or she is considering and compute the effect of fund costs over the period the investor expects to hold the fund – in dollars and cents. And the investor can compare that dollars and cents number to the dollars and cents number for another fund.[280]

The Mutual Fund Cost Calculator[281] requires the user to input the requisite fee and charge information via successive entry screens. Progress through the screens continues until all required information is entered and a final calculation is presented. The process is somewhat slower than the Canadian equivalent.

The introductory page to the calculator is as follows:

---

[279] Testimony of Chairman Arthur Levitt before the Subcommittee on Finance and Hazardous Materials, Committee on Commerce, concerning Transparency in the United States Debt Market and Mutual Fund Fees and Expenses (29 September 1998) http://www.sec.gov/news/testimony/testarchive/1998/tsty1398.htm, under the heading "Current Initiatives: Investor Education" (notes omitted).

[280] Speech by Paul Roye, Director, Division of Investment Management, SEC – Speech given at the National Association for Variable Annuities Regulatory Affairs Conference (28 June 1999) http://www.sec.gov/news/speech/speecharchive/1999/spch285.htm, paragraphs 11-12 under the heading "Disclosure".

[281] http://www.sec.gov/investor/tools/mfcc/mfcc-int.htm.

Mutual Fund Cost Calculator - Microsoft Internet Explorer

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Address http://www.sec.gov/investor/tools/mfcc/mfcc-int.htm Go

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U.S. Securities and Exchange Commission

The SEC Mutual Fund Cost Calculator: A Tool for Comparing Mutual Funds

The Mutual Fund Cost Calculator enables investors to easily estimate and compare the costs of owning mutual funds. The Cost Calculator takes the mystery and math out of the cost equation, revealing how costs add up over time.

Mutual fund costs take a big chunk out of any investor's return. That's why it's important for investors to know what costs they are paying, and which cost structure is best for them. By using the Cost Calculator investors will find answers quickly to questions like this: Which is better, a no-load fund with yearly expenses of 1.75% , or a fund with a front-end sales charge of 3.5% with yearly expenses of 0.90% ?

The Cost Calculator is great for understanding costs, but costs aren't the only thing that should be considered when investing in a mutual fund. Other things to assess include:

- the number of years needed to reach an investment goal,
- the type of stocks, bonds, or other securities that the fund buys,
- the risk of the fund,
- the fit between the fund and the investor's portfolio (diversification),
- the fund company or portfolio manager who runs the fund,
- the fund's track record or performance over time, and
- the types of services offered by the fund company.

You can learn what factors to consider before investing in a mutual fund by reading Mutual Fund Investing: Look at More Than a Mutual Fund's Past Performance.

Please review the frequently asked questions before beginning. This page provides answers and an e-mail address for comments. The FAQ page will be updated from time to time, so be sure to check back often.

Run the JavaScript SEC Cost Calculator (requires a JavaScript-enabled browser, such as Netscape Navigator™ 2.0 or higher, or Microsoft® Internet Explorer 3.0 or higher.)

http://www.sec.gov/investor/tools/mfcc/mfcc-int.htm

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Internet

The Frequently Asked Questions are as follows:

Mutual Fund Cost Calculator - FAQ - Microsoft Internet Explorer

File Edit View Favorites Tools Help

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Address http://www.sec.gov/investor/tools/mfcc/mfcc-faq.htm Go

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U.S. Securities and Exchange Commission

Frequently Asked Questions About the Mutual Fund Calculator

Contents

Q1. What is the Mutual Fund Cost Calculator?

A1. The SEC's Mutual Fund Cost Calculator is an easy-to-use computer program that allows investors to compare the total costs of owning different mutual funds. It also provides definitions for terms that users will come across while investing in mutual funds.

Q2. Why has the SEC created this program?

A2. The Cost Calculator serves two primary purposes. First, it enables investors to compare the cost of owning funds before buying them. Second, it clearly demonstrates the effect that fees have on foregone earnings and total costs.

Q3. What is included in "total costs"?

A3. Total costs is the sum of the fees paid plus the foregone earnings. Fees include payments made when the account is opened or closed as well as operating expenses. Once these fees are paid to the fund company rather than being invested in the fund, an investor foregoes earnings. Therefore, the higher the fees, the higher foregone earnings there will be.

Q4. What costs are not included in the Cost Calculator?

A4. This program does not include all fees that you may be charged (for example, exchange fees, or account maintenance fees). These fees, however, are relatively small. In addition, deferred sales charges (discussed later in the Cost Calculator) are based on the lesser of the initial investment or the values of the investment at redemption, but some funds may base the charge solely on the initial investment.

Q5. How do you access the Cost Calculator?

A5. To run the cost calculator on the SEC website, you must use a JavaScript enabled browser.

Q6. What kind of computer or other equipment do you need?

A6. The JavaScript version requires a JavaScript enabled web browser, such as Netscape Navigator™ 2.0 or higher, or Microsoft® Internet Explorer 3.0 or higher.

Q7. Where do I get the information to enter into the Cost Calculator?

A7. All of this information is in the prospectus of the specific fund you are considering.

Q8. Where can I find definitions of the terms such as **sales charge** or **operating expense**?

A8. Simply click on the underlined term in the program.

Q9. Can the Cost Calculator download information directly from any mutual funds or mutual fund rating agencies, such as Morningstar or Lipper?

A9. No. The Cost Calculator is not connected to a database and only generates answers from the information that you provide. In addition, the program does not collect any information about you.

Q10. Does the Cost Calculator cost anything to use?

A10. No.

Q11. Who can I contact with questions?

A11. Let us know how we can improve the Cost Calculator by e-mailing us at help@sec.gov. Be sure to check this page often, as we will be adding both questions and answers from time to time. In addition, the SEC Office of Investor Education and Assistance has publications on this website that can answer many of your basic investing questions.

Q12. Where can I get more information about mutual funds and fees?

A12. We've provided a list of publications on the basics of investing in mutual funds and more information about fees. You'll also find information here from the Department of Labor about fees and 401(k) plans.

Q13. The fee table of my fund has two numbers for operating expenses. My total annual fund operating expenses are 1.36% and net operating expenses are 1.31%. Which number should I use?

A13. Some funds have fee waivers or expense reimbursements that reduce the operating expenses. Total annual fund operating expenses are the amounts paid if there were no fee waivers or expense reimbursements. Net operating expenses – the lower number – is the amount paid as a result of fee waivers or expense reimbursements. The cost can be estimated by entering either the total annual fund operating expenses or the net operating expenses, or by calculating the cost using each number to see the difference

Q14. I want to try the calculator using a fund I already own. The fund has multiple classes but I don't remember which class I invested in. How can I find out which class I invested in?

A14. Check the confirmation you received when you purchased shares in your fund or your account statement for information about the fund's class. Otherwise contact your broker, if you are using one, or the fund company.

http://www.sec.gov/investor/tools/mfcc/mfcc-faq.htm

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Internet

Running the calculator from the welcome page produces the following screen:

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Getting Started

Click here to skip the introduction

The SEC Cost Calculator estimates the cost of investing in a mutual fund based on information you provide. The results should be compared for several funds or different classes of a single fund.

Before you begin, take out the prospectus or profile for the funds you want to evaluate. You will need to plug in information from the expense section of these documents.

Continue

http://www.sec.gov/investor/tools/mfcc/get-started.htm

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Internet

Clicking on “Continue” raises two additional screens of information which can be avoided by clicking on “Click here to skip the introduction”. Those additional screens are (in edited form) as follows:

Mutual Fund Cost Calculator - About Costs - Microsoft Internet Explorer

File Edit View Favorites Tools Help

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Address http://www.sec.gov/investor/tools/mfcc/about-costs.htm Go

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U.S. Securities and Exchange Commission

About Mutual Fund Costs

Higher expenses do not assure superior performance. A high cost fund will have to perform better to provide you with the same return as a low cost fund.

All mutual funds have costs. These include: **(1)** fees you pay for specified transactions, such as when you buy, sell, or exchange your shares; and **(2)** ongoing expenses. Slightly larger fees can make a big difference in the value of your investment over time.

Continue

http://www.sec.gov/investor/tools/mfcc/about-costs.htm

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How this program works.

You will enter how long you expect to hold your investment, the dollar amount of your investment, and the expected annual rate of return. Next, you will be asked to look in the prospectus or profile for information about fees.

After calculating the cost of investing in a particular fund, you can quit, evaluate a different fund, or start a new calculation.

Continue

http://www.sec.gov/investor/tools/mfcc/how-it-works.htm

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Done Internet

Clicking “Continue” at this point raises the first entry screen for the calculator; following the instructions raises the subsequent screens:

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U.S. Securities and Exchange Commission

How many years do you plan to hold the fund?

(For example, type 10 and press **ENTER** on your computer.)

10 years

http://www.sec.gov/investor/tools/mfcc/holding-period.htm

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U.S. Securities and Exchange Commission

Enter the dollar value of your investment.

(For example, type 10,000 with or without commas and press **ENTER** on your computer.)

$ 10000

http://www.sec.gov/investor/tools/mfcc/dollar-amount.htm

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NOTE: To get the best comparison, you should compare similar types of funds.

For example, you should not compare a **stock fund** to a **money market fund**. Instead, you should compare the cost between two or more stock funds.

What type of fund best describes what you want to analyze?

(Click on the appropriate button.)

Money Market | Bond | Stock

A stock fund has been assumed, together with an optimistic 12% return:

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U.S. Securities and Exchange Commission

Stock Fund

NOTE: The average return for a stock index (S&P 500) over the past 30 years has been approximately 12%.

Enter the annual rate of return you expect to receive.

(For example, type 5 and press **ENTER** on your computer.)

12 %

http://www.sec.gov/investor/tools/mfcc/rate-of-return.htm

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U.S. Securities and Exchange Commission

Later, the program gives you the option to print the results of your cost calculation. Enter a title or label (such as the fund name and its class) that will be meaningful to you should you choose to print the results.

(For example, type **XYZ Class A Fund** and press **ENTER** on your computer.)

XYZ Class A Fund

http://www.sec.gov/investor/tools/mfcc/fund-label.htm

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U.S. Securities and Exchange Commission

Enter the percentage sales charge on purchases if you invest $ 10000 .

(For example, type 5 and press **ENTER** on your computer.)

2.5 %

Start over

New Fund

http://www.sec.gov/investor/tools/mfcc/front-load.htm

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U.S. Securities and Exchange Commission

Enter the percentage deferred sales charge after 10 years.

(For example, type 5 and press **ENTER** on your computer.)

0 %

Start over

New Fund

http://www.sec.gov/investor/tools/mfcc/back-load.htm

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Does this fund convert from one share class to another by year 10 ?

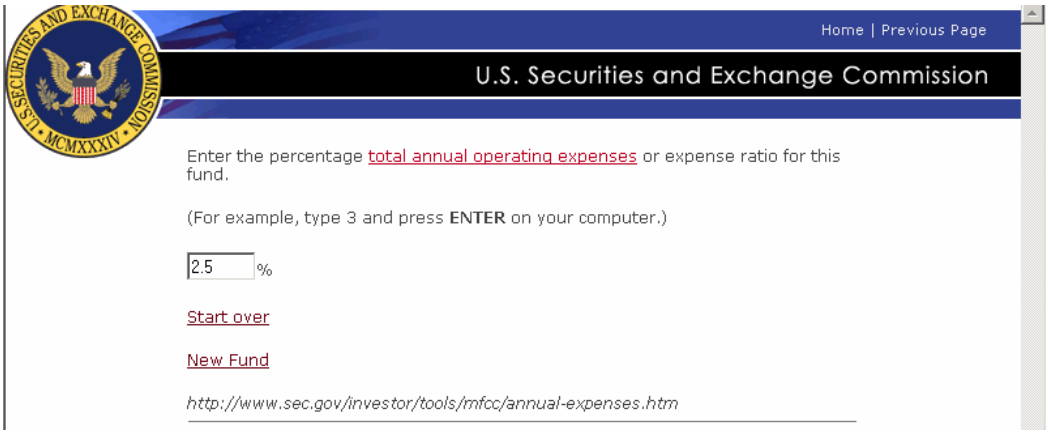
Yes No

Start over

New Fund

http://www.sec.gov/investor/tools/mfcc/convert.htm

Assuming the fund does not convert from one share class to another:



The final result is as follows:

Essentially, the SEC calculator provides the same information in respect of mutual fund cost as does the calculator provided by the Ontario Securities Commission. However, the SEC calculator does not provide a graphical representation, nor does it permit “on-the-fly” changes with immediate recalculation.

Appendix USA-1

401(k) Plan Fee Disclosure Form

ABC PLAN
401(k) PLAN FEE DISCLOSURE FORM
For Services Provided by XYZ Company[1]

Overview

The Employee Retirement Income Security Act of 1974, as amended (ERISA) requires employee benefit plan fiduciaries to act solely in the interests of, and for the exclusive benefit of, plan participants and beneficiaries. As part of that obligation, plan fiduciaries should consider cost, among other things, when choosing investment options for the plan and selecting plan service providers.

This 401(k) plan fee disclosure form may assist you in making informed cost-benefit decisions with respect to your plan. The purpose of this form is to help you determine the total cost of the plan. It is also intended to provide you with a means to compare investment product fees and plan administration expenses charged by competing service providers, regardless of how a particular service provider structures its fees.

The 401(k) plan fees included in this disclosure form represent the following: _____ actual 401(k) plan expenses for the period X/XX/XX through X/XX/XX or _____ estimated 401(k) plan expenses[2] for the period X/XX/XX through X/XX/XX. Additional investment product information regarding fees may be obtained from the product prospectus, annuity contract or other similar documents. Additional information relating to plan administration services and expenses is contained in documentation provided by the service provider, including the contract for plan services. Other plan expenses may include legal fees for initial plan design and ongoing amendments resulting from changes in pension law or plan design and the cost of a mandatory annual audit. You need to contact your legal advisor or accountant to determine these charges.

Selecting a service provider requires that you evaluate and differentiate services offered by competing companies. Cost is one of the criteria, but not the only criterion, for making this evaluation. Other factors of equal or greater importance to consider include the quality and type of services provided, the anticipated performance of competing providers and their investment products and other factors specific to your plan's needs. *The service provider offering the lowest cost services is not necessarily the best choice for your plan.*

Calculation of Fees

In general, fees are calculated in four ways:

- Asset-based: expenses are based on the amount of assets in the plan and generally are expressed as percentages or basis points.
- Per-person: expenses are based upon the number of eligible employees or actual participants in the plan.
- Transaction-based: expenses are based on the execution of a particular plan service or transaction.
- Flat rate: fixed charge that does not vary, regardless of plan size.

Fees may be calculated using one or any combination of these methods. Plan administration-related expenses can also be charged as one-time fees or ongoing expenses. One-time fees are typically related to start-ups, conversions (moving from one provider to another) and terminations of service. Ongoing fees are recurring expenses relating to continuing plan operation.

---

[1] There may be plan expenses incurred by other providers, other than the company completing this form. For a complete list of expenses charged to your plan, please contact all plan service providers with whom you contract or may contract and request fee information with respect to their services.

[2] If you are considering a conversion from an existing plan service provider to a new service provider, you will need to provide the service provider(s) with certain information about the plan, including the number of plan participants, the number of eligible participants and the amount of plan assets in order for the service provider(s) to be able to complete this form. Similarly, if you are considering starting a plan, you will need to provide the service provider(s) with estimates of plan participants and plan assets. When providing potential service providers with information regarding your plan, it is critical that you provide identical information to all of the competing companies in order to ensure equivalent comparisons.

ABC PLAN
401(k) PLAN FEE DISCLOSURE FORM
For Services Provided by XYZ Company
Total Plan Expenses

Contact Name: _____
Institution: _____
Phone: _____

		Amount/ Estimate[3]	
I.	**Investment Product Fees (See Schedule A)**		
	A. Collective Investment Fund(s)	$_____	
	B. Insurance/Annuity Product(s)	$_____	
	C. Mutual Fund(s)	$_____	
	D. Individually Managed Account(s)	$_____	
	E. Brokerage Window	$_____	
	F. Other Product(s) (Specify)	$_____	
	Total Investment Product Fees		$_____
II.	**Plan Administration Expenses (See Schedule B)**		
	Total Plan Administration Expenses		$_____
III.	**Plan Start-Up or Conversion Related Charges (See Schedule C)**		
	One Time Start-Up/Conversion expenses		$_____
IV.	**Service Provider Termination Related Charges (See Schedule D)**		
	Service Provider Termination expenses		$_____
	Total Plan Expenses		**$**_____

For definitions of terms used throughout this disclosure form, see Schedule E.

[3] Amounts are calculated based on rates charged, which are identified in attached schedules as applied to relevant information (for example amount of assets or number of participants). Certain calculations may be estimates based on information provided by you, the plan sponsor, and may vary as circumstances change.

ABC PLAN
401(k) PLAN FEE DISCLOSURE FORM
For Services Provided by XYZ Company
Schedule A

Investment Product Fees/Estimates

Collective Investment Fund	Assets (X/X/XX)	Management Fee	Other✚ (Specify)	Total Cost
Fund 1				
Fund 2				
Fund 3				
Fund 4				
TOTAL				

Insurance /Annuity Product	Assets (X/X/XX)	Management Fee	Mortality Risk and Administrative Expense (M&E Fee)	Other✚ (Specify)	Total Cost
Fund 1					
Fund 2					
Separate Account 1					
Separate Account 2					
TOTAL					

Mutual Fund	Assets (X/X/XX)	Expense Ratio[4]	Front-end Load	Other✚ (Specify)	Total Cost
Fund 1					
Fund 2					
Fund 3					
Fund 4					
TOTAL					

Individually-Managed Account	Assets (X/X/XX)	Management Fee	Other✚ (Specify)	Total Cost
Product 1				
Product 2				
Product 3				
Product 4				
TOTAL				

✚ Fees represent product-related charges paid by the plan. Fees associated with participants' transfer of account balances between investment options, including investment transfer expenses and any contingent back-end loads, redemption fees and surrender charges should be included in "other" expenses. In addition, any wrap fees or pricing charges for non-publicly traded assets should be included in the "other" expenses column. For investment product termination fees associated with plan termination or conversion, see Schedule D. Insurance companies incur marketing and distribution costs, which are recouped through charges assessed against the plan.

[4] Includes 12b-1 fee and management fee. (See the fee table in the fund prospectus).

ABC PLAN
401(k) PLAN FEE DISCLOSURE FORM
For Services Provided by XYZ Company
Schedule A, continued

Investment Product Fees/Estimates

Brokerage Window[5]	Assets (X/X/XX)	Commission (Range)	Transaction Fee (Range)	Other✚ (Specify)	Total Cost
Total Transactions					

Other Product[6]	Assets (X/X/XX)	Management Fee	Other✚ (Specify)	Total Cost
Product 1				
Product 2				
Product 3				
Product 4				

Total Investment Product Fees $_____

[5] When providing potential service providers with information/assumptions regarding the brokerage window plan feature, it is critical that you provide identical information to all of the competing companies in order to ensure equivalent comparisons.

✚ Fees associated with participants' transfer of account balances between investment options, including investment transfer expenses and any contingent back-end loads, redemption fees and surrender charges should be included in "other" expenses. In addition, any wrap fees or pricing charges for non-publicly traded assets should be included in the "other" expenses column. For investment product termination fees associated with plan termination or conversion, see Schedule D. Insurance companies incur marketing and distribution costs, which are recouped through charges assessed against the plan.

[6] Other products could include investment vehicles such as REITs and limited partnerships.

ABC PLAN DISCLOSURE FORM
For Services Provided by XYZ Company
Schedule B

PLAN ADMINISTRATION EXPENSES

Expense Type	Rate/ Estimate*	Bundled Service Arrangement (✔)[7]	Total Cost**	
Administration/Recordkeeping Fees:				
• Daily valuation	$_____	☐	$_____	
• Payroll processing	$_____	☐	$_____	
• Balance inquiry	$_____	☐	$_____	
• Investment transfer	$_____	☐	$_____	
• Contract administration charge	$_____	☐	$_____	
• Distribution processing	$_____	☐	$_____	
• QDRO processing	$_____	☐	$_____	
• Participant statements	$_____	☐	$_____	
• Plan sponsor reports	$_____	☐	$_____	
• VRU/Internet services	$_____	☐	$_____	
• Other (specify)	$_____	☐	$_____	
Subtotal				$_____
Participant Education/Advice:				
• Participant education materials/distribution	$_____	☐	$_____	
• Education meetings (frequency__)	$_____	☐	$_____	
• Investment advice programs	$_____	☐	$_____	
• Other (specify)	$_____	☐	$_____	
Subtotal				$_____
Trustee/Custodial Services:				
• Certified annual trust statement	$_____	☐	$_____	
• Safekeeping of plan assets	$_____	☐	$_____	
• Other (specify)	$_____	☐	$_____	
Subtotal				$_____

* Amounts represent the method by which the fee is calculated, for example as a percentage of plan assets under management, based upon number of participants or based upon number of transactions. For start-up or take-over situations, fees are based upon estimates and/or certain assumptions, i.e., regarding assets under management and number of participants. When providing potential service providers with information/assumptions regarding your plan, it is critical that you provide identical information to all of the competing companies in order to ensure equivalent comparisons. Without a standardized set of assumptions, service providers will certainly use differing assumptions, defeating the intended purpose of clarifying fee comparisons among service providers.

[7] Services provided under a bundled services arrangement are indicated by a check mark next to the specific service.

** Amounts represent flat dollar amount charges or total charges based upon the particular method of calculation. In some instances, these amounts represent estimates based on assumptions provided by you, the plan sponsor.

ABC PLAN DISCLOSURE FORM
For Services Provided by XYZ Company
Schedule B, continued

Expense Type	Rate/ Estimate*	Bundled Service Arrangement (✔)	Total Cost**	
Compliance Services:				
• Nondiscrimination testing	$_____	☐	$_____	
• Signature ready form 5500	$_____	☐	$_____	
• Annual audit	$_____	☐	$_____	
• Other (specify)	$_____	☐	$_____	
Subtotal				**$**_____
Plan Amendment Fee:				
• Plan amendment fee	$_____	☐	$_____	
• Plan document/determination letter fee	$_____	☐	$_____	
• Other (specify)	$_____	☐	$_____	
Subtotal				**$**_____
Loan Administration:				
• Loan origination fee	$_____	☐	$_____	
• Loan processing fee	$_____	☐	$_____	
• Loan maintenance and repayment tracking fee	$_____	☐	$_____	
• Other (specify)	$_____	☐	$_____	
Subtotal				**$**_____
Total separate charges			$_____	
Total bundled services			$_____	
(Less offsets/credits paid to plan)			$(_____)	
Total Plan Administration Expenses			**$**_____	

* Amounts represent the method by which the fee is calculated, for example as a percentage of plan assets under management, based upon number of participants or based upon number of transactions. For start-up or take-over situations, fees are based upon estimates and/or certain assumptions, i.e., regarding assets under management and number of participants. When providing potential service providers with information/assumptions regarding your plan, it is critical that you provide identical information to all of the competing companies in order to ensure equivalent comparisons. Without a standardized set of assumptions, service providers will certainly use differing assumptions, defeating the intended purpose of clarifying fee comparisons among service providers.

** Amounts represent flat dollar amount charges or total charges based upon the particular method of calculation. In some instances, these amounts represent estimates based on assumptions provided by you, the plan sponsor.

ABC PLAN
401(k) PLAN DISCLOSURE FORM
For Services Provided by XYZ Company
Schedule C

ONE TIME START-UP/CONVERSION EXPENSES

Expense Type	Rate/ Estimate*	Total Cost**
• Start-up/conversion education program	$ _____	$_____
• Start-up/conversion enrollment expense	$ _____	$_____
• Installation fee	$ _____	$_____
• Start-up/conversion plan document fee/filing fee	$ _____	$_____
• Other (specify)	$ _____	$_____
Total Start-up/Conversion expenses		$_____

* Amounts represent the method by which the fee is calculated, for example as a percentage of plan assets under management, based upon number of participants or based upon number of transactions. For start-up or take-over situations, fees are based upon estimates and/or certain assumptions, i.e., regarding assets under management and number of participants. When providing potential service providers with information/assumptions regarding your plan, it is critical that you provide identical information to all of the competing companies in order to ensure equivalent comparisons. Without a standardized set of assumptions, service providers will certainly use differing assumptions, defeating the intended purpose of clarifying fee comparisons among service providers.

** Amounts represent flat dollar amount charges or total charges based upon the particular method of calculation. In some instances, these amounts represent estimates based on assumptions provided by you, the plan sponsor.

ABC PLAN
401(k) PLAN DISCLOSURE FORM
For Services Provided by XYZ Company
Schedule D

SERVICE PROVIDER TERMINATION EXPENSES

Expense Type	Rate/ Estimate*	Total Cost**
Investment Product Expenses		
• Contract termination charges	$ _____	$ _____
• Back-end load	$ _____	$ _____
• Product termination fee	$ _____	$ _____
• Other (specify)	$ _____	$ _____
Total		**$** _____
Plan Administration Expenses		
• Service provider termination charge	$ _____	$ _____
• Service contract termination charge	$ _____	$ _____
• Other (specify)	$ _____	$ _____
Total Termination Expenses		**$** _____

* Amounts represent the method by which the fee is calculated, for example as a percentage of plan assets under management, based upon number of participants or based upon number of transactions. For start-up or take-over situations, fees are based upon estimates and/or certain assumptions, i.e., regarding assets under management and number of participants. When providing potential service providers with information/assumptions regarding your plan, it is critical that you provide identical information to all of the competing companies in order to ensure equivalent comparisons. Without a standardized set of assumptions, service providers will certainly use differing assumptions, defeating the intended purpose of clarifying fee comparisons among service providers.

** Amounts represent flat dollar amount charges or total charges based upon the particular method of calculation. In some instances, these amounts represent estimates based on assumptions provided by you, the plan sponsor.

ABC PLAN
401(k) PLAN FEE DISCLOSURE FORM
For Services Provided by XYZ Company
Schedule E

DEFINITION OF TERMS

Administration/Recordkeeping Fee: Fee for providing recordkeeping and other plan participant administrative type services. For start-up or takeover plans, these fees typically include charges for contacting and processing information from the prior service provider and "matching up" or mapping participant information. Use of this term is not meant to identify any ERISA Section 3(16)(A) obligations.

Annual Audit: Federal law requires that all ERISA-covered plans with more than 100 participants be audited by an independent auditor. It is also common to refer to a DOL or IRS examination of a plan as a plan audit. Any charge imposed by a service provider in connection with this audit is reflected on Schedule B.

Back-End Load: Sales charges due upon the sale or transfer of mutual funds, insurance/annuity products or other investments, which may be reduced and/or eliminated over time.

Balance Inquiry: Fee that may be charged each time a participant inquires about his or her balance.

Brokerage Commission: A fee paid to a broker or other intermediary for executing a trade.

Brokerage Window: A plan investment option allowing a participant to establish a self-directed brokerage account.

Bundled Services: Arrangements whereby plan service providers offer 401(k) plan establishment, investment services and administration for an all-inclusive fee. Bundled services by their nature are priced as a package and cannot be priced on a per service basis.

Collective Investment Fund: A tax-exempt pooled fund operated by a bank or trust company that commingles the assets of trust accounts for which the bank provides fiduciary services.

Contract Administration Charge: An omnibus charge for costs of administering the insurance/annuity contract, including costs associated with the maintenance of participant accounts and all investment-related transactions initiated by participants.

Contract Termination Charge: A charge to the plan for "surrendering" or "terminating" its insurance/annuity contract prior to the end of a stated time period. The charge typically decreases over time.

Conversion: The process of changing from one service provider to another.

Distribution Expense: The costs typically associated with processing paperwork and issuing a check for a distribution of plan assets to a participant. May include the generation of IRS Form 1099R. This fee may apply to hardship and other in-service withdrawals as well as to separation-from-service or retirement distributions.

Eligible Employee: Any employee who is eligible to participate in and receive benefits from a plan.

Expense Ratio: The cost of investing and administering assets, including management fees, in a mutual fund or other collective fund expressed as a percentage of total assets.

ABC PLAN
401(k) PLAN FEE DISCLOSURE FORM
For Services Provided by XYZ Company
Schedule E (continued)

Front-End Load: Sales charges incurred when an investment in a mutual fund is made.

Individually Managed Account: An investment account managed for a single plan.

Installation Fee: One-time fee for initiating a new plan or initiating new services.

Investment Transfer Expense: Fee associated with a participant changing his or her investment allocation, or making transfers among funding accounts under the plan.

Loan Maintenance and Repayment Tracking Fee: Fee charged to monitor outstanding loans and repayment schedule.

Loan Origination Fee: Fee charged when a plan loan is originally taken.

Loan Processing Fee: Fee charged to process a plan loan application.

Management Fee: Fee charged for the management of pooled investments such as collective investment funds, insurance/annuity products, mutual funds and individually managed accounts.

Mortality Risk and Administrative Expense (M&E Fee): Fee charged by an insurance company to cover the cost of the insurance features of an annuity contract, including the guarantee of a lifetime income payment, interest and expense guarantees, and any death benefit provided during the accumulation period.

Nondiscrimination Testing Expense: Tax qualified retirement plans must be administered in compliance with several regulations requiring numerical measurements. The fee charged for the process of determining whether the plan is in compliance is collectively called nondiscrimination testing expense.

Participant: Person who has an account in the plan.

Participant Education Materials/Distribution Expenses: All costs (including travel expenses) associated with providing print, video, software and/or live instruction to educate employees about how the plan works, the plan investment funds, and asset allocation strategies. There may be a one-time cost associated with implementing a new plan, as well as ongoing costs for an existing program.

Plan Document/Determination Letter Fee (Filing Fee): Fee charged for a written plan document. Fee can also include the costs associated with preparing and filing IRS required documentation, including the request for a determination letter (document issued by the IRS stating whether the plan meets the qualifications for tax-advantaged treatment).

Plan Loan: The law allows participants to borrow from their accounts up to prescribed limits. This is an optional plan feature.

ABC PLAN
401(k) PLAN FEE DISCLOSURE FORM
For Services Provided by XYZ Company
Schedule E (continued)

Product Termination Fee: Investment-product charges associated with terminating one or all of a service provider's investment products.

QDRO (Qualified Domestic Relations Order): A judgment, decree or order that creates or recognizes an alternate payee's (such as former spouse, child, etc.) right to receive all or a portion of a participant's retirement plan benefits.

Separate Account: An asset account established by a life insurance company, separate from other funds of the life insurance company, offering investment funding options for pension plans.

Service Provider Termination Charge: Plan administrative costs associated with terminating a relationship with a service provider, with the permanent termination of a plan, or with the termination of specific plan services. These may be termed "surrender" or "transfer" charges.

Signature Ready Form 5500: Fee to prepare Form 5500, a form which all qualified retirement plans (excluding SEPs and SIMPLE IRAs) must file annually with the IRS.

Start-up/Enrollment Expense: Costs associated with providing materials to educate employees about the plan, and enrolling employees in the plan. This may be part of, or included in, the education programs. There may be a one-time cost associated with implementing a new plan, as well as ongoing enrollment costs.

Trustee Services: Fees charged by the individual, bank or trust company with fiduciary responsibility for holding plan assets.

VRU: Voice Response Unit.

Wrap Fee: An inclusive fee generally based on the percentage of assets in an investment program, which typically provides asset allocation, execution of transactions and other administrative services.

12b-1 Fee: A charge to shareholders to cover a mutual fund's shareholder servicing, distribution and marketing costs.

Part 6

Options for Improved Disclosure

INTRODUCTION

In this section of the report options for improved disclosure of fees and charges in managed investments are proposed for the consideration of ASIC and industry.

It is worth recalling the Good Disclosure Principles from Policy Statement 168. These Principles were outlined in Part 2 of the report. According to the Principles, disclosure should:

- be timely;
- be relevant and complete;
- promote product understanding;
- promote comparison;
- highlight important information; and
- have regard to consumers' needs.

It has been said that the key purposes of disclosure standards in the area of fees and charges are to ensure that:[282]

- fees and commissions are transparent and readily understood by the average investor;
- investors have an understanding of the cost of entering into any contract;
- investors know the amount and timing of any remuneration to be received by the adviser from any investment decision;
- any investment decision is unbiased by the level of remuneration received by the adviser; and

[282] Phillips Fox, *Financial Services Reform Act: Product Disclosure of Fees, Charges and Commissions*, Report Prepared for ASIC, November 2000, p 5.

- investors can compare the cost of making an investment against alternate products in the marketplace.

As noted in Part 3 of this report, I believe there is a need for improved disclosure of fees and charges in relation to managed investments. This was a common theme running through many of the meetings with key stakeholders although not all stakeholders agreed in relation to the degree of improvement needed and what should be done to improve disclosure.

Part 3 of the report identifies a number of problems with existing disclosure of fees and charges. In that Part the results were presented of surveys of the adequacy of disclosure of fees and charges in prospectuses. These surveys showed there is considerable scope for the improvement of disclosure of fees and charges in prospectuses. This conclusion was reinforced by an examination of surveys, the results of which were summarised in Part 3, which have tested investors' understanding of fees and charges. The results of these surveys show that a significant number of investors fail to understand basic information about fees and charges.

Part 6 of the report contains the following sections:

- options for improved disclosure in Product Disclosure Statements (**PDSs**);
- options for improved disclosure in periodic member statements; and
- options for implementation and the role of ASIC and industry.

OPTIONS FOR IMPROVED DISCLOSURE IN PDSS

There are a number of issues that warrant consideration in relation to options for improved disclosure in PDSs. The issues discussed in this section are:

- standardised descriptions and definitions of fees;
- to what extent should fees be broken down?;
- entry/contribution fees;
- exit/withdrawal fees;
- capacity to increase fees/maximum fees;

- ongoing management charge/management expense ratio;
- showing the effect of fees on returns;
- disclosure in dollars versus disclosure in percentages;
- disclosure of fees paid to advisers;
- the buy/sell spread;
- disclosure of fees near returns; and
- disclosure of ability to negotiate rebates with advisers.

STANDARDISED DESCRIPTIONS AND DEFINITONS OF FEES

In Policy Statement 168, ASIC states that an example of a disclosure issue that may benefit from clarification, particularly if greater comparability of products is to be achieved, is "standardised description of like fees and charges (such as commissions), including the basis for showing the future impact of fees and charges".

It is clear from a perusal of existing prospectuses (see Part 3 of this report) that much more can be done to standardise descriptions and definitions of fees. The same fees are sometimes given different descriptions. Key stakeholders consulted as part of this project were generally supportive of more standardised descriptions of fees. In addition, relevant fees are not always disclosed in the section which deals with fees. For example, it is sometimes the case that switching fees are discussed not in the fees section of the prospectus but in another section. A potential investor therefore has to peruse all of the prospectus to identify whether fees may or may not apply.

Particular types of fees are discussed below. However, as a matter of principle, I see considerable merit in the following principles being adopted by those who prepare PDSs:

- All relevant fees are to be referred to in the fees section of the PDS (in some circumstances it might be appropriate for more detailed discussion of particular fees to be located elsewhere in the PDS provided there is an appropriate cross-reference from the fees section of the PDS where the fee is identified to the more detailed discussion elsewhere in the PDS).

- Even if a fee which is commonly imposed is not imposed in relation to a particular product, the fact that this fee is not imposed should be disclosed in the fees section of the PDS. For example, if a particular product does not have an entry fee, exit fee or switching fees applying to it, then this should be stated in the fees section of the PDS. This has the advantage of enhancing comparability of PDSs and eliminates the need on the part of a potential investor to search the entire PDS to identify whether a fee is imposed.
- The purpose of any fee which is imposed should be disclosed in the fees section of the PDS.
- To the maximum extent possible, there should be standardised descriptions and definitions of fees (specific fees are discussed below).
- Consideration should be given to a standardised table across all PDSs for financial products which would identify significant fees (such as entry, exit, switching and investment management fees), state whether or not each fee applies to the particular product and, if so, state the amount of the fee.

There can be a higher degree of complexity of fees in relation to superannuation than some other financial products. However, it is still possible to have a table which identifies whether or not significant fees are applicable and, if so, the amount of the fees. Such a table in relation to a superannuation product could include the following:

Type of Fee	**Amount (state Nil if not applicable)**
Establishment fee Contribution fee Administration fee Investment management fee Switching fee Withdrawal fee	

The table can also be used for non-superannuation products (although the reference to establishment fee may need to be removed). This, or a similar type of table, would be located in the fees section of the PDS. In the same section of the PDS there would be a description of each of the relevant fees and also a statement about the purpose why each fee is imposed.

I now turn to discuss the extent to which fees should be broken down in a PDS and, following this, I discuss specific types of fees.

TO WHAT EXTENT SHOULD FEES BE BROKEN DOWN?

There is debate concerning the extent to which fees should be broken down and disclosed in PDSs. At one end of the spectrum, there is an argument that if it is possible to come up with a single global figure which captures all fees, then this has strong advantages for potential investors in terms of simplicity and enhancing comparability of PDSs. At the other end of the spectrum, there is the argument that separate disclosure of all applicable fees means that potential investors have all information in order to make an investment decision.

Both of these positions have difficulties and disadvantages associated with them. To come up with a single global figure which captures all fees may be impossible to do in any meaningful way. Some types of fees may be fixed dollar fees imposed each month or year. An administration fee in a superannuation fund is often this type of fixed dollar fee. Other types of fees are typically fixed percentage fees of certain amounts, such as the amount invested or the amount in the fund. To combine a fixed dollar fee and a percentage fee in a meaningful way is difficult and requires additional calculations.

A more significant difficulty with endeavouring to have a single global figure is that some fees are mandatory while others are discretionary. For example, a fund may impose switching fees. However, this fee will of course only apply to those investors who actually switch their investment. This means that a fee which is discretionary needs to be disclosed separately from those fees which are mandatory otherwise the single global figure has the potential to be very misleading. A similar point can be made in relation to exit fees. Entry fees may also be discretionary to the extent to which some investors may pay the full entry fee relevant to a financial product while others may have all or part of the entry fee rebated to them. In other words, disclosure of a single global figure which captures all fees may have initial attractions yet it can quickly be seen that a number of important fees would need to be disclosed separately.

I also note that of those countries whose disclosure requirements were reviewed for the purposes of this project, none had a single global figure which captures all fees (see Part 5 of this report).

In relation to whether or not all fees relating to a financial product should be disclosed separately in the PDS, the question is whether this can lead to an excess of information being disclosed to investors. For example, a manager of a fund may pay one or more custodian fees, typically of a small amount when compared to other fees. These fees are usually not disclosed and it is understandable why they are not as it would be unusual for these fees to impact upon the investment decision of a potential investor.

There is an important point in relation to the breakdown of fees between administration and investment management. I see considerable merit in requiring these fees to be disclosed separately. The reasons for this are as follows. First, they are different functions. Second, separate disclosure of both administration and investment fees enables investors to compare how efficient each of these aspects is across a variety of financial products. Third, it is typically the case that investment management fees are the largest ongoing fees. It is important that the fee which is most directly related to the performance of the fund be separately disclosed. Finally, the distinction between administration and investment has become more important with the growth of master funds and IDPSs.

I now turn to discuss specific fees.

ENTRY/CONTRIBUTION FEES

As stated above, there is merit in moving to more standardised descriptions and definitions of fees. A fee which is paid to invest in a particular financial product may have different names. The review of prospectuses (summarised in Part 3 of this report) reveals that this fee can be called an entry fee, a contribution fee or a deposit fee. References to it being a deposit fee are rare. Usually, it is called a contribution fee in relation to superannuation products and an entry fee in relation to managed funds.

I see merit in seeing if it is possible to adopt common terminology for this fee across superannuation and managed funds. This would fit with the Financial Services Reform

Act objective of enhancing comparability of financial products. The challenge is that both of the terms are well entrenched in the marketplace. It might be possible to interpret the term entry fee as implying that it is a one-off payment (ie paid only when an investor first invests or "enters"). In fact, it is common for these fees to be paid on further investments in the same fund by the same investor although a reduced fee might be applicable. In these circumstances, the term contribution fee would seem to be more accurate. A contribution fee can be paid when one first invests and can also be paid in relation to subsequent investments or contributions. In summary, I see merit in determining whether the term contribution fee can be used across both superannuation and managed funds.

As noted above, even if a particular financial product does not have a contribution/entry fee, then this fact should be disclosed in the fees section of the PDS – as part of the fee disclosure table recommended above.

I recommend that the purpose of fees which are imposed be disclosed in the PDS. In relation contribution/entry fees, if this fee is to be used for adviser remuneration, then it is appropriate that this purpose be disclosed. After all, this fee can constitute a substantial percentage of an initial investment.

EXIT/WITHDRAWAL FEES

A similar issue in relation to terminology arises with this fee as with entry/contribution fees. An exit fee can also be called a withdrawal fee. I make recommendations in relation to this fee that are similar to my recommendations relating to entry/contribution fees. In particular:

- there is merit in having common terminology across both superannuation and managed funds to enhance comparability;
- it may be that the term withdrawal fee is more accurate than exit fee as a reference to exit fee may imply that one is entirely withdrawing an investment from a fund whereas a fee would still be payable for only a partial withdrawal;
- if no exit/withdrawal fee is applicable, this should be clearly stated as part of the fee disclosure table recommended above; and

- if an exit/withdrawal fee is payable, then the purpose of this fee should be disclosed.

CAPACITY TO INCREASE FEES/MAXIMUM FEES

I recommend that the capacity to increase fees and the maximum fees applicable be disclosed in the fees section of the PDS. Key stakeholders consulted as part of this project were generally supportive of this position. Given that fees can typically be increased (perhaps substantially) without the approval of investors it is important that investors be aware of this capacity to increase fees. It becomes even more important if a particular financial product has significant exit/withdrawal fees. If the capacity to increase fees and the maximum amount to which they can be increased is not disclosed, then an investor can be severely disadvantaged if fees are increased and an investor who wishes to withdraw is then subject to a high exit fee.

In summary, where fees which are disclosed in the PDS can be increased this fact should be specifically stated in the fees section of the PDS and the maximum amount to which the fees can be increased should also be disclosed in this section.

ONGOING MANAGEMENT CHARGE/MANAGEMENT EXPENSE RATIO

This section discusses the ongoing management charge ("**OMC**") and the management expense ratio ("**MER**"). It provides an overview of the OMC/MER and then makes several recommendations for improved disclosure.

Overview of OMC/MER

The OMC and MER are broadly similar, although they do have differences. In the case of the MER, the Investment and Financial Services Association ("**IFSA**") has published IFSA Standard No 4.00 which specifies the principles to be adopted by its members when calculating MERs. IFSA Standard No 4.00 is an Appendix to this part of the report.

Paragraph 6.1 of Standard No 4.00 states that the purpose of the Standard is to:

- specify the principles to be adopted when calculating MERs;

- provide guidance in the interpretation and application of those principles; and
- specify the manner in which MERs are disclosed in offer documents and other reports to investors.

In relation to the purpose of MERs, paragraph 6.3 of Standard No 4.00 states:

> The MER is to capture expenses, which are incurred by the operation of an unlisted Scheme. Expenses, which would be incurred by a direct investor in the same assets, should be excluded where these can be identified and isolated. The aim is to show investors what extra costs they are paying by using an unlisted managed vehicle.

Two important features of the MER are to be noted. First, it is intended to provide a measure of ongoing costs and expenses. Second, it is a measure of the *additional* ongoing costs arising from the use of a managed investment vehicle. Consequently, the MER excludes:

- entry and exit fees (as these are not ongoing costs);
- government taxes and charges unless a direct investor would not have paid these;
- transaction costs such as brokerage and stamp duty as these would be incurred by a direct investor; and
- operating costs and expenses that would be incurred by a direct investor such as, in the case of property investments, repair, maintenance and refurbishment costs (Standard No 4.00, paragraph 10.1).

The MER is to be presented in tabular form for the last three completed financial years (if the fund has existed for this period of time), made up as at the fund's balance date, together with a brief description of the method of calculating the MER (Standard No 4.00, paragraph 9.1).

For funds that offer more than one investment choice, a separate MER is required for each of those investment choices.

The MER is expressed as a percentage. There is no requirement to convert it to a dollar amount by applying the percentage to a specified sample dollar amount (for example, $10,000 as occurs in the case of superannuation).

In the case of superannuation, calculation of the OMC is governed by Schedule 10 of the Corporations Regulations 2001. The formula was outlined in Part 4 of this report. There are specific disclosure obligations for the OMC which exceed those for the MER under the IFSA Standard. In particular, in the case of superannuation, the dollar amount of the OMC is to be shown by applying the OMC percentage to an account balance of $10,000. Schedule 10B of the Corporations Regulations 2001 requires different disclosure of the OMC depending upon whether the PDS has a single investment strategy or multiple investment strategies. To make this clear, it is useful to repeat in this part of the report the table in Part 4 of the report summarising the disclosure of OMCs under the Corporations Regulations.

OMC Disclosure
Schedule 10B – Corporations Regulations

Single Strategy

cl. 8.1

- Preamble statement
- Overall OMC%, investment-mgmt OMC% and non-investment-mgmt OMC%

cl. 8.4

- Explanation of effect of OMC
- Example based on $10,000 for overall fund/product
- Statement of charges included in each of overall OMC, investment-management OMC and non-investment-management OMC
- Prescribed statements
  - Warning to read charges section
  - Notice that past charges do not necessarily indicate future charges
- Description of OMC and signpost

Multiple Strategy

cl. 8.1

- Preamble statement

cl. 8.2

- "For each identified investment strategy": OMC% and converted amount, for each of overall OMC, investment-mgmt OMC and non-investment-mgmt OMC

OR

- "In respect of all investment strategies": a statement of the highest and lowest OMC% and converted amount, for each of overall OMC, investment-mgmt OMC and non-investment-mgmt OMC, and a notice that OMC calculations specific to particular strategies is available on request

cl. 8.4

- Explanation of effect of OMC
- Example based on $10,000 for overall fund/product
- Statement of charges included in each of overall OMC, investment-mgmt OMC and non-investment-mgmt OMC
- Prescribed statements
  - Warning to read charges section
  - Notice that past charges do not necessarily indicate future charges
- Description of OMC and signpost

The OMC and the MER are broadly similar. The key difference between the two measures is in relation to expenses that would have been incurred by a direct investor (such as brokerage, stamp duty and costs associated with the maintenance of a property investment). Under IFSA Standard No 4.00 these types of expenses are excluded from the calculation of the MER. However, under the definition of the OMC in Part 7.9 of the Corporations Regulations and the calculation of the OMC under Schedule 10 of the Regulations, these expenses are included in the calculation of the OMC.

The Value of OMC/MER

It has been argued that a shortcoming of the OMC/MER is that the measures exclude entry/contribution fees and exit/withdrawal fees. This is true but it needs to be remembered that the concept of the OMC/MER is *ongoing* management expenses or charges. Entry and exit fees are not automatic ongoing charges and therefore it is not appropriate to include them in the OMC/MER. In addition, the OMC/MER represents charges that have in fact been paid. Entry and exit fees can be discretionary fees. They may or may not be paid depending upon the circumstances of the investor. For example, an investor may have all or part of their entry fee rebated by an investment adviser.

A limit of the OMC/MER is that it is based on the cost to the average fund member or investor and not the actual cost to the member or investor. In summary, both the OMC/MER express all ongoing fees as a percentage of the average value of the fund during the relevant year. This will not necessarily be the actual fee paid by the investor. However, it is typically recognised that the OMC/MER provides useful information relating to relative costs across similar funds and can identify trends in relation to ongoing management charges and expenses over time. It is to be noted that similar operating expense ratios are used in other countries such as Canada, New Zealand and the United States (see the international review in Part 5 of this report). Later in this section I make recommendations concerning improved disclosure of fees and charges in periodic member statements. If adopted, the recommendations will improve disclosure to investors of fees and charges based on their individual circumstances.

However, I do have recommendations for improved disclosure concerning the OMC/MER and I now turn to these recommendations.

Standardised Terminology and Improved Descriptions

A key objective of the Financial Services Reform Act is to improve the ability of investors to compare financial products. The OMC/MER essentially reflect the same thing – a ratio of ongoing management charges. However, comparability across superannuation and managed funds is reduced when different terminology for the two ratios is used and there is a difference in the calculation of the two ratios (in particular, the MER excludes expenses that would have been incurred by a direct investor such as brokerage, stamp duty and costs in maintaining a property investment, while these expenses are included in the calculation of the OMC).

I have two specific recommendations. First, I see merit in having the same terminology used across both superannuation and managed funds. To the extent to which the ratio reflects ongoing management charges, the use of the term OMC would seem to be more accurate than MER. I recognise that both terms are well entrenched in their respective parts of the financial sector. I see merit in IFSA being invited to consider changing from the use of the term MER in its Standard No 4.00 to the use of the term OMC.

The second recommendation concerns the difference in the way the two ratios are calculated. This detracts from the ability to compare products. I see merit in IFSA being invited to consider amending its Standard No 4.00 so that expenses which would be incurred by a direct investor are included in the MER. This would align the MER with the OMC. It has the advantage of making the MER a more comprehensive ratio of ongoing charges. It also makes the MER a more straightforward and clearly explained ratio as it is not necessary to explain that it excludes expenses that would have been incurred by a direct investor.

In addition to the above two recommendations, I also see merit in having a standardised description of the OMC/MER for all financial products. My review of disclosure documents reveals wide variation in the way these ratios are described. This is not helpful for investors.

I suggest the following may be a useful starting point as a possible precedent which could be discussed with industry participants.

> The Management Expense Ratio/Ongoing Management Charge is a measure of the ongoing expenses associated with your investment. It is expressed as a percentage of the total assets of the fund (excluding liabilities). It includes:
>
> - **The ongoing investment management fee** – this is the annual fee the fund pays to [……] to manage your investment. In 2002 this fee was [……%] – see page [……]; and
> - **Other fees and expenses paid from the fund** – this includes certain administration costs associated with managing your investment such as the cost of maintaining the registry of members; printing costs of product disclosure statements, annual reports and member statements; the cost of producing cheques; postage expenses; fees charged by the fund's auditor and fees paid to custodians who hold the assets of the fund.
>
> The MER/OMC excludes entry/contribution fees, exit/withdrawal fees and switching fees.

I also see merit in a statement which would be required in all PDSs that past fees should not be taken as an indication of future fees. Currently, this statement is required only for superannuation products.

In addition, should it turn out to be the case that the MER and the OMC continue to be calculated differently, then it would be important to have an additional statement in relation to the disclosure of the MER that costs such as brokerage and stamp duty are not included in the MER although they are paid from the fund.

Dollar Value of the MER

As noted above, Schedule 10B of the Corporations Regulations 2001 requires the OMC to be converted to a dollar amount for an account balance of $10,000. There is a question whether this type of calculation should also be required for non-superannuation products.

I note this has been done in one of the first PDSs for managed funds produced under the new FSR regime. In Colonial First State's FirstChoice Investments PDS dated 6 May 2002, the dollar value of the MER (which Colonial First State calls the "Ongoing Management Fee") is shown for an account balance of $10,000. Interestingly, this disclosure is made for each of the 15 investment options to which the PDS relates. The investment options range from cash through fixed interest and property securities to

geared global shares. The disclosure is made in a table which had three items – the investment option, the MER as a percentage and the MER converted to dollars based on a sample account balance of $10,000.

I see merit in this type of disclosure given that surveys of investors show that where possible, investors can relate more easily to disclosure which is in dollars. Because improvement of the ability of investors to compare products is a feature of the new FSR regime, there is merit in endeavouring to have similar disclosure across both superannuation and managed funds. I see a role for ASIC in facilitating industry discussion with a view to determining whether industry is prepared to include this type of disclosure in PDSs for managed funds. As we have seen, one of the major fund managers has already voluntarily implemented such disclosure.

SHOWING THE EFFECT OF FEES ON RETURNS

An important issue is whether the effect of fees on returns should be disclosed in PDSs. Currently, this is not required for either superannuation or managed funds.

The key stakeholders consulted as part of this review expressed a broad range of views on this issue. On the one hand, the view was expressed that this is essential information for investors. The contrary view is that while it may be useful in theory, because of the assumptions required, which may prove to be inaccurate, the information cannot be rendered useful. The types of assumptions that need to be made are:

- the likely future returns;
- the likely future fees; and
- the likely future contributions by the investor.

Another limitation is that projected returns should vary across asset classes. Thus, over time, we would expect returns on shares to exceed returns on fixed interest investments. Consequently, there is an argument that specifying the one rate of return across all classes of asset or investment type is too limited. On the other hand, to have

different rates of returns specified for different asset classes or investments will complicate disclosure in PDSs which offer multiple investment options.

Despite these difficulties I note that some major countries require this type of disclosure. In particular, as noted in the international survey in Part 5 of this report, the United Kingdom, the United States and Canada require this type of disclosure for certain of their financial products. Where this disclosure is required, the regulator needs to specify what the future rate of return is in order to avoid the understandable incentive on the part of product issuers to maximise the future rate of return.

In the United Kingdom, the Financial Services Authority ("**FSA**") did, at one stage, consider withdrawing from prescribing projections on a standardised basis in product disclosure documents. However, the FSA concluded that it was undesirable to do so as the following extract from one of the FSA's publications shows:[283]

> We have considered whether the regulator should withdraw from prescribing the production of projections on a standardised basis. The arguments in favour of such a withdrawal are that consumers may place undue reliance on the figures precisely because they are standardised; that projections may give a misleading impression of what growth might be achieved; and that they imply a greater degree of certainty, and predictability than is warranted.
>
> However, withdrawal would be difficult where products are targeted at achieving a particular outcome (eg mortgage or school fee repayment). For non-targeted products there is a different problem. The consumer appetite for an indication of "what will I get back" is so strong that in practice any void the regulator creates is likely to be filled by uncontrolled and unrecorded "back of the envelope" calculations, which give scope for unscrupulous advisers to use inappropriate rates or place an unwarranted emphasis on past performance. It could also be difficult to show the impact of charges on investment return without projections…
>
> For these reasons, our current thinking is that on balance it will be necessary to continue using projections in the new product disclosure regime.

There are other reasons why showing the effect of fees on returns can be useful. First, an increase in fees can reduce substantially future returns. For example, a 1% increase in a fund's annual fees and charges can reduce an investor's final account balance in that fund by 18% after 20 years.[284]

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[283] Financial Services Authority, *Informing Consumers: A Review of Product Information at the Point of Sale*, November 2000, paras 73-75.

A second reason why disclosure of the effect of fees on returns is important for investors is that some investment choices require this sort of information. For example, it is increasingly popular to offer investors different fee choices in relation to the same financial product. For example, a particular financial product may offer investors two choices concerning fees – (i) a nil entry fee with a higher OMC option or (ii) an entry fee with a lower OMC option. How is the investor to tell which is the preferred option without having some insight into the effect of the different fee options on returns? With the increase in choice being made available by product issuers there is also a greater obligation on them to disclose information concerning fees and charges.

The above considerations leads to the view that there is merit in disclosing the effect of fees on returns subject to:

- a specified rate of return being set for industry participants; and
- appropriate disclosure about the assumptions which have been made.

The Australian Consumers' Association ("**ACA**") in a recent submission to the Parliamentary Joint Committee on Corporations and Financial Services inquiry into:

- ASIC Policy Statements made under the Financial Services Reform Act; and
- regulations made under that Act,

proposed a table for superannuation products which shows the effect of fees on returns.

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[284] United States Securities and Exchange Commission, *Report on Mutual Fund Fees and Expenses*, January 2001, p 4.

ACA FEE DISCLOSURE MODEL

Name:
Date of birth:
Commencing salary:
Contributions:
Account balance at inception:

Fee structure for XXX Super fund

Administration fees	**Fund manager fees**
• $x per week/month/year • -% of contributions	• $x per week/month/year • -% of account balance
Trustee fees	**Other fees**
• $x per week/month/year • -% of account balance	• $x per week/month/year • -% contributions • -% of account balance

Sample Table for Disclosure Model

		Gross investment return			
Years	**Salary $**	**6% p.a**		**8% p.a**	
		No Fees $	**XXX Fees $**	**No Fees $**	**XXX Fees $**
5	39,600	16,451	15,885	17,268	16,671
10	44,800	41,085	39,147	45,389	43,215
To age 55	56,000	116,940	108,629	142,694	132,188
To age 60	66,000	185,339	169,626	239,943	218,652
To age 65	71,400	281,466	253,670	387,656	347,209

Note: Fees expressed in $'s, contributions and salaries increase by 3% p.a

Ageing Agendas, in its report to ASFA, also recommended disclosure of the effect of fees on returns and proposed the following table (see Part 3 of this report).

AGEING AGENDAS (REPORT TO ASFA) FEE DISCLOSURE MODEL

Effect of fees on account balance – no entry fee option

Impact on account balance from	**Compulsory employer contributions of 9% on annual pay of $20,000 ($1,800)**	**Compulsory employer contributions of 9% on annual pay of $40,000 ($3,600)**
If withdrawn	Impact of Fees	Impact of Fees
after 2 years	$ 250	$ 410
after 5 years	$ 490	$ 730
after 10 years	$1,440	$2,260
after 20 years	$5,720	$9,630

Colin Grenfell, an actuary, has recommended a series of tables for superannuation PDSs designed to show the effect on returns of expenses (but not investment charges which would be disclosed separately) for periods up to 40 years. The tables he has proposed are included in Appendix Part 6-2 of this report. Mr Grenfell put forward these tables for consideration when consulted as part of this project and also in his submission to the current inquiry being conducted by the Senate Select Committee on Superannuation into superannuation and standards of living in retirement.

I see merit in ASIC facilitating industry discussion about the merits of a table, which would show the effect of fees on returns, being included in PDSs relating to all superannuation products. As stated above, I believe it important that investors have access to information which discloses the effect of fees upon returns. Later in this Part, I make recommendations concerning the possible introduction of a fee calculator on the ASIC website. It would seem appropriate that, if this recommendation is adopted, disclosure of the effect of fees on returns be made on the website.

DISCLOSURE IN DOLLARS VERSUS DISCLOSURE IN PERCENTAGES

There is strong evidence that investors better understand and feel more comfortable with disclosure which is in dollars rather than percentages. Some of this evidence was referred to in Part 3 of this report. Research in other countries has reached similar conclusions.[285]

[285] Financial Services Authority, above n 283, para 92.

On the other hand, use of percentages can facilitate comparison across funds in relation to certain matters. For example, disclosure of the MER/OMC as a percentage can make it easy to compare these ratios across a number of different PDSs.

I therefore conclude that, where possible, disclosure should be made in both percentages and dollars. Sometimes, only dollar disclosure will be required. For example, a fund may impose a switching fee of $50 per switch.

The MER has traditionally been described only as a percentage and this is what is required by IFSA Standard No 4.00. However, as noted above, a major fund manager has already in a recent PDS converted the MER for 15 investment options offered in that PDS to a dollar figure by applying the MER to a sample investment of $10,000. This type of disclosure is desirable.

I therefore recommend that ASIC facilitate discussion among industry participants concerning the extent to which fees and charges can be expressed in both dollar terms and percentage terms.

DISCLOSURE OF FEES PAID TO ADVISERS

I recommend that the fees section of PDSs contain disclosure of fees paid to advisers – both upon an initial investment and on an ongoing basis. Even for a PDS which offers multiple investment options, this disclosure can be done by way of a table which lists the investment options and then has two further columns – the fee paid to the adviser upon initial investment and also the ongoing trail paid per annum. I note that a number of PDSs already contain this type of disclosure. However, others do not and there is considerable variation in the quality of disclosure.

I also recommend that the source for the payment of these fees to advisers be stated in PDSs. In the case of the ongoing trail, this will be the investment management fee. In the case of the initial investment, this will typically be the entry/contribution fee paid by the investor.

Sometimes disclosure documents contain a simple statement to the effect that fees paid to advisers are paid from the manager's own resources without any further disclosure.

This may create the impression that fees paid to advisers are not in effect borne by investors. Consequently, I believe it is appropriate for the source of fees paid to advisers to be disclosed in the PDS.

There is also the question about disclosure of "soft commissions" ie, other payments made to advisers which may include things such as bonuses for having clients invest specified amounts in certain financial products. Where these exist, I recommend that the PDS draws attention to the fact that arrangements may exist between the fund manager and financial advisers. Because of the variety of these arrangements and the fact that a fund manager may have different arrangements with financial advisers, it may be that only a general statement concerning the existence of such arrangements can be made in the PDS together with a statement that the investor should refer to the Financial Services Guide and Statement of Advice received from the adviser for specific details of these arrangements.

THE BUY/SELL SPREAD

A matter of confusion in disclosure documents is the so-called buy/sell spread. There is considerable variation in disclosure documents concerning this and, based upon consultations with key stakeholders conducted as part of this project, I am advised that it is a continuing source of concern for investors.

I see scope for improved disclosure in PDSs concerning the buy/sell spread. A useful precedent, drawn, with some changes, from a current PDS, is the following:

> **What is the difference between entry and exit unit prices?**
>
> There is a difference between the entry and exit unit price for the fund on any business day. The difference relates to transaction costs and is often called a "buy/sell spread". When investors make new investments or withdrawals from the fund, the fund incurs some costs in buying new investments (when money is added to the fund) or selling investments (when withdrawals are made). So that existing investors do not continually bear the transaction costs resulting from new investments or withdrawals, all investors pay a set, average amount (a buy/sell spread) when they transact. This is calculated according to the particular types of investments the fund holds. Currently, the buy/sell spread is [….] %. Not all new investments or withdrawals cause transaction costs to be payable to the fund, for example, where an investment does not incur any significant costs, or when a new investment coincides with a withdrawal by someone else. However, to be consistent, we generally apply transaction costs to all investments and withdrawals from the fund.

> Please note that transaction costs (buy/sell spread) are not fees paid to [the manager]. They are paid to the fund, to ensure equality between all investors. They may be altered at any time.
>
> To give you an example, the transaction costs (buy/sell spread) on an investment of $10,000 are $50.

I see considerable merit in developing a standardised definition of the buy/sell spread. ASIC can play a role in facilitating industry discussion to achieve this.

DISCLOSURE OF FEES NEAR RETURNS

During the course of the consultations with key stakeholders conducted as part of this project, some stakeholders expressed the view that it is important to avoid having investors simply choose the option of investing in cash to avoid paying fees. To the extent to which this problem may exist for some uninformed investors, I suggest that it is appropriate for the fees section of PDSs to be adjacent to that section of the PDS which discloses returns. However, I do not suggest that this be mandatory. It is appropriate for those who design PDSs to have discretion regarding this matter. In addition, the recommended disclosure of the purpose of investment management fees should assist (see above discussion under the heading "Standardised Descriptions and Definitions of Fees").

DISCLOSURE OF ABILITY TO NEGOTIATE REBATES WITH ADVISERS

A matter on which conflicting views were presented to me by key stakeholders during the consultation process was whether it is desirable to have in the fees section of a PDS a statement about the ability of an investor to have part or all of the entry fee rebated to the investor. My review of current disclosure documents reveals a variety of practices. In some documents, there is no disclosure. However, there is such disclosure in other documents. For example, to take disclosure documents by three prominent product issuers, ASGARD discloses that the initial fee is [%] "unless your financial adviser agrees to rebate part or all of their deposit fee remuneration". Colonial First State has the following statement in its recent PDS: "Your adviser determines the entry fee you pay, up to the maximum shown. Where you do not use an adviser the maximum applies." BT has the following statement: "Your adviser must specify any current and future rebates on the application form before we receive your investment."

I see merit in having more standardised disclosure in this area. Investors can be disadvantaged by inadequate disclosure. It is appropriate to have some statement to the effect that, where applicable, it is the adviser who determines the amount of the entry/contribution fee paid.

OPTIONS FOR IMPROVED DISCLOSURE IN PERIODIC MEMBER STATEMENTS

A theme running through the consultations with key stakeholders was the need to improve disclosure of fees and charges in periodic statements sent to members/investors. As noted earlier in this report, disclosure of fees and charges in these types of statements varies to an extraordinary degree. Some periodic statements make no disclosure about fees and charges. This is unfortunate because it is this document which provides the opportunity for an investor to ascertain precisely what fees and charges have been paid in relation to their investment. This cannot be done in a selling document (PDS) where there is a limit to the information that can be tailored to individual circumstances. In addition, as noted earlier in this report, it seems sensible to assume that member/investor statements may be more closely read than many PDSs. This is for several reasons. First, the typical member/investor statement is considerably shorter than the typical selling document. Second, it is the member/investor statement which gives details of the value of the existing investment and the investor therefore has a financial incentive to review the statement.

As noted in Part 3 of this report, there are member/investor statements which provide no details concerning fees and charges. The statement may provide only a dollar value for the opening balance at the beginning of the period and a dollar value for the closing balance at the end of the relevant period, with no indication of the amount of fees and charges which have been paid. Although member/investor statements may be given quarterly, six-monthly or yearly, once a year the investor will receive, along with the statement, an annual report. In this annual report, there can be expected to be reference to the MER. However, it is often the case that there is no reference on the member/investor statement to the fact that the MER is disclosed in the annual report and, in any event, the MER does not always give a precise measure of the actual fees and charges relevant to a particular investor.

I note that there is concern at an international level with the inadequacy of disclosure of fees and charges in periodic member statements. In the United States, the General Accounting Office published a report in June 2000 on mutual fund fees. It is stated in this report:[286]

> Mutual fund investors generally receive quarterly statements detailing their mutual fund accounts. These statements usually indicate the beginning and ending number of shares and the total dollar value of shares in each mutual fund owned. They do not show the dollar amount of operating expense fees that were deducted from the value of these shares during the previous quarter. This contrasts with most other financial products or services, such as bank accounts or brokerage services, for which customer fees are generally disclosed in specific dollar amounts…
>
> One suggestion for increasing investor awareness was that mutual funds should disclose to each investor the actual dollar amount of the portion of the funds' fees they paid…Fund adviser officials GAO interviewed indicated that calculating such amounts exactly would entail systems changes and additional costs, but they also acknowledged that less costly means of calculating such amounts may exist. For example, instead of calculating the exact amount of fees charged to each account daily, a fund adviser could provide an estimate of the fees an investor paid by multiplying the average number of shares the investor held during the quarter by the fund's expense ratio for the quarter. Another alternative would be to provide the dollar amount of fees paid for preset investment amounts, such as $1,000, which investors could use to estimate the amount they paid on their own accounts.

More recently, the United States Securities and Exchange Commission has considered improved disclosure of fees and charges in periodic member statements.[287] The SEC's Division of Investment Management has recommended that additional fee information, including the dollar amount of fees, should be provided in periodic member statements. According to the Commission, "one advantage of this approach is that it would enable investors to not only compare the fees of funds but also to evaluate the fee information that would be contained in the reports to investors alongside other key information about the fund's operating results, including management's discussion of the fund's performance".[288]

The Commission notes that this additional information about actual fees paid could be presented in a variety of ways. One way is to multiply the fund's per share (unit) asset value by the fund's expense ratio, multiply the result by the average number of shares

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[286] United States General Accounting Office, *Mutual Fund Fees: Additional Disclosure Could Encourage Price Competition*, June 2000, pp 13-14.
[287] United States Securities and Exchange Commission, *Report on Mutual Fund Fees and Expenses*, January 2001.
[288] Ibid, p 5.

(units) an investor owned during the period, and show the result in the investor's account statement.

A second (and less costly) way to provide improved information about actual fees is to require reports to include a table showing the cost in dollars incurred by an investor who invested a standardised amount (eg $10,000) in the fund, paid the fund's actual expenses, and earned the fund's actual return for the period. The Commission states that it could require, in addition, that the table include the cost in dollars, based on the fund's actual expenses, of a standardised investment amount (eg $10,000) that earned a standardised return (eg 5%). Because the only variable for this calculation would be the level of expenses, investors could easily compare funds to one another.

The reason the Commission has proposed the second alternative is that it is conscious of the costs that could be imposed in terms of changing computer systems for the calculation of actual fees paid by investors in mutual funds. These costs would ultimately be borne by investors.

My main conclusion is that there is considerable scope for improved disclosure of fees and charges in periodic member statements. I recommend that where actual fees relating to a member's investment can be calculated, then these fees should be disclosed on the statement. In relation to those funds where the calculation of such fees might prove to be costly, I recommend that ASIC obtain information from industry about the costs of providing this disclosure. This would allow a cost/benefit analysis to be undertaken.

The United States General Accounting Office, in its report on mutual fund fees, calculated that the costs to provide annual statements with improved disclosure would be less than $1 per investor per year.[289] It would be important to ascertain what the costs of improved disclosure would be in the Australian context.

However, even if the costs of providing precise disclosure are significant, such is the importance of improving disclosure of fees in periodic member statements that I make

[289] United States General Accounting Office, above n 286, p 79.

a further recommendation. I recommend that ASIC facilitate discussions with industry about the recommendations proposed by the US Securities and Exchange Commission and the US General Accounting Office. The first alternative provides more detailed information. The second alternative involves providing information about the dollar amount of fees that were paid during the relevant period for preset investment amounts. This would require investors to then estimate the amount they paid on their own accounts. However, there can be no doubting that this would be a substantial improvement over the current situation where little, if any, meaningful disclosure is made in many periodic member statements.

OPTIONS FOR IMPLEMENTATION AND THE ROLE OF ASIC AND INDUSTRY

I see an important role for ASIC and industry in ensuring there is improved disclosure of fees and charges in both PDSs and periodic member statements. I have already made a number of specific recommendations to improve disclosure of fees and charges where I believe ASIC can facilitate industry discussion.

There are, however, three further issues which warrant discussion. These are:

- consumer testing of the recommendations contained in this report;
- the possible introduction of a calculator for fees and charges on the ASIC website; and
- facilitation of industry discussion concerning disclosure of fees and charges to trustees.

CONSUMER TESTING OF RECOMMENDATIONS

A view expressed by a number of those consulted as part of this project was the need to undertake consumer testing of recommendations where appropriate. I believe this is desirable. It has the advantage of ensuring that suggestions for improved disclosure of fees and charges are subject to evaluation by those who use disclosure documents for financial products. I therefore recommend that industry and consumer groups be invited to undertake consumer testing of the recommendations contained in this report, preferably in consultation with ASIC.

FUND FEE CALCULATORS

The Rationale for Calculators

The advent of the internet has signalled the emergence of web-enabled business models and technologies which have been embraced by the investment industry. The web has extended the marketing reach of financial product issuers, thus affording prospective investors with more information delivered in different ways.

Some product issuers and regulators have made available fee calculators on their websites. Issuers might make available such calculators in order to obtain a competitive advantage: investors may regard the offering of a calculator as a sign of honesty, integrity and transparency which may increase the perception of the issuer relative to other issuers. Regulators might make available calculators as part of their regulatory and oversight mandate: the deployment of calculators by bodies having an authoritative role in the market may lead to an increase in investor confidence in the market, as well as improve investor knowledge and understanding more generally. The emergence of web-enabled calculation software seems to have coincided with an increase in the complexity and variety of financial products.

Overview of the Calculators

Part 5 of this report contains details of fee calculators made available by regulators in other countries. The United States Securities and Exchange Commission ("**SEC**") hosted fee calculator is rich in information. The calculator proceeds on a screen-by-screen basis, requiring the user to input information gleaned from fund prospectuses before proceeding through the subsequent screens. At the end, the calculator provides a detailed report outlining the quantum of fees attaching to the product, as well as information in respect of earnings foregone as a result of fees having been paid over the duration of the investment. The calculator is therefore able to contextualise fees against investment returns, which can be varied.

The rationale behind the SEC's introduction of the calculator may be gleaned from the Chairman's remarks upon the launch of the facility:

> For some time…I have been concerned that the financial literacy of Americans has not kept pace with the growth of fund investments. I especially worry that investors do not understand the costs they pay for their mutual funds – and how those costs affect the amounts they will have in retirement or for their children's educations.
>
> Our own research shows that less than half of mutual fund investors know that fund expenses are deducted on an ongoing basis. Only 8 percent say they completely understand the expenses that their funds charge. These figures and other findings demonstrate how much education still needs to be done and the Cost Calculator can help.
>
> …[T]he Cost Calculator will allow investors to understand the true cost of owning a particular fund, without being confused by the fund's packaging. It will help us close the gap between the knowledge fund investors have and the knowledge they need.[290]

The SEC envisaged the calculator as reinforcing the aims of the prospectus fee table:

> We have found…that there is a gap between the widespread availability of mutual fund cost information in the fee table and investors' ability to use that information effectively. …
>
> The Cost Calculator is designed to…close the gap between the fee table and investors' ability to use the fee table information to make a real-world investment decision.[291]

The Ontario Securities Commission ("**OSC**") hosted calculator is almost identical to the SEC calculator in approach: it is information rich and contextualises fees against returns. However, that is the extent of the similarities, for the OSC calculator is a one-screen software item that is fully-functional and variable in realtime. Unlike the SEC calculator, the OSC calculator enables the user to input all variables without proceeding through a series of input screens, and immediately thereupon calculates the fee and return results. The OSC calculator also presents a detailed report but does so immediately and in graphical pie-chart form. Although the OSC and SEC calculators are essentially the same, the OSC calculator is faster, more flexible and arguably more meaningful.

The Association of Superannuation Funds of Australia Limited ("**ASFA**"), in an important initiative, recently launched a web-based fee calculator. Unlike the preceding calculators, the ASFA calculator is not made available by a securities regulator but rather by an industry body. In a sense, an industry calculator seems to straddle the roles played by regulator calculators on the one hand and issuer calculators

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[290] SEC, *Remarks of Chairman Levitt: Media Briefing on Mutual Fund Cost Calculator* (6 April 1999), http://www.sec.gov/news/extra/mfcalc.txt.

[291] SEC, *Remarks of Paul Roye: Media Briefing on Mutual Fund Cost Calculator* (6 April 1999), http://www.sec.gov/news/extra/mfroye.txt.

on the other. However, the ASFA calculator is, understandably, given the role of ASFA, limited to superannuation funds.

FSA Comparative Tables

The UK Financial Services Authority does not provide a calculator as such but a set of user-definable Comparative Tables which set out the charge and deduction information for a range of products falling within the user's selected category. Insofar as the Tables serve as a calculator, they simply aggregate the readily-available fee and charge information for the products. The Tables are quite comprehensive in respect of the number of products covered. Throughout the consultation process in advance of the launch of the Tables, the FSA was keen to ensure that the Tables were as comprehensive as possible, covering as many products and issuers as possible, on the most relevant and objectively-verifiable data that would be of use to investors for comparative purposes. What the Tables lack in customisability, they make up for in comparability and range. It remains to be seen whether comparability and range outweigh the need for personalisation, the hallmarks of fee calculators.

Policy Considerations Underlying the FSA Comparative Tables

The FSA's concern with comparability stems from its educative mandate:

> The tables are a key element of the FSA's campaign to boost consumers' understanding of financial services by arming them with accurate and relevant information before shopping around for the best deal.[292]

In earlier consultations promoting the FSA's educative strategy,[293] the FSA noted that "many consumers are 'put off by the unfamiliarity, complexity and lack of transparency of market offerings'". The FSA was also concerned with "consumers' overall low levels of financial literacy, awareness of financial needs, understanding of what is available, and their ignorance of where and how to find out what they need to know".[294]

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[292] FSA, *New Comparative Tables Will Help Shift Power to the Consumer* (Press Release, 30 May 2001), http://www.fsa.gov.uk/pubs/press/2001/062.html.

[293] FSA, *Consultation Paper 15: Promoting Public Understanding of Financial Services: A Strategy for Consumer Education* (November 1998).

[294] FSA, *Consultation Paper 28: Comparative Information for Financial Services* (October 1999), ¶4.1.

The FSA took the preliminary view that comparative information would overcome the weaknesses in the levels of consumer information which it had observed. The underlying rationale was to: [295]

- increase consumer confidence;
- provide information and knowledge to consumers;
- increase competition within the market;
- provide understandable and meaningful information to consumers;
- encourage consumers to seek professional advice;
- optimise the purchase process by assisting consumers to shop around; and
- do so reliably and authoritatively.

In that regard, the FSA concluded that a comparative information scheme would achieve those stated aims by: [296]

- serving as a non-advisory sales route for either an efficient immediate outcome or inspiration to seek advice;
- presenting information clearly and comparably;
- improving consumers' informational position vis-à-vis advisers; and
- allowing consumers simply to compare and contrast the charges of products and improve consumers' general bargaining position.

The FSA consequently concluded that such an approach would provide issuers with a great incentive to compete on price and quality. Combining these incentives with an improvement in consumers' understanding and bargaining position, the desired regulatory outcome of an efficient and fair market would be much more readily achieved with less regulatory intervention than might otherwise be required.[297]

Evaluation and Options

The OSC calculator appears to provide the most meaningful and user-friendly solution to the problem of personalised fee and charge calculations. It is easy to use, operates

[295] Ibid, ¶¶4.4-4.26.
[296] Ibid, ¶4.27-4.30.

by way of a graphic interface and provides detailed and comprehensive results, with pictorial representations.

I recommend that ASIC deploy a calculator similar to the OSC calculator. The justification for such an approach is found in the increasing need by investors to obtain personalised investment information and to obtain such information accurately, authoritatively and meaningfully.

ASIC would play an important role by serving as the authoritative delivery mechanism for the calculator. The FSA, in the lead up to the launch of the Comparative Tables, stressed the need for such a tool to be provided by an authoritative source.[298] The deployment of such a calculator by ASIC would preserve the authoritative integrity of the calculator and, moreover, would contribute significantly to ASIC's educative mandate.

TRUSTEES' UNDERSTANDING OF FEES AND CHARGES

This project is concerned with disclosure of fees and charges in PDSs and periodic member statements. As previously noted, I see an important role for ASIC in facilitating industry discussion of the key issues identified earlier in this Part.

However, during the course of research for this project, I was made aware of the recent publication of the UK Pension Fund Disclosure Code. This Code of practice was drawn up by a joint working party of members of the Investment Management Association and the National Association of Pension Funds. The objective of the Code is transparency in order to assist pension fund trustees' understanding of the fees and charges levied on pension fund assets for which they have responsibility. The background to the Code is a concern that a lack of comprehensive, clear and standardised disclosure has not allowed trustees and their advisers to monitor and compare all costs incurred during the management of fund assets.

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[297] Ibid, ¶4.31.

[298] FSA, *Response to Consultation Paper 28: Comparative Information for Financial Services* (June 2000), ¶¶4.4-4.7.

The details of the main features of the Code are specified below. Because:

- a number of the key issues raised in the Code are similar to those which lie at the heart of this project; and
- improved disclosure of fees and charges to trustees has the potential to improve disclosure to retail investors;

I raise for the consideration of trustee and other industry bodies the desirability or otherwise of industry adopting a Code which would be similar to the UK Pension Fund Disclosure Code.

UK INVESTMENT MANAGEMENT ASSOCIATION

PENSION FUND DISCLOSURE CODE

2002

1 Scope

The Code is designed to:

- be adopted by the managers of UK pension fund mandates;
- be applied to portfolios, or portions of portfolios, consisting of listed securities (including suspended securities previously listed), derivatives (where the underlying instruments are securities, financial indices, interest rates, dividends or foreign exchange), cash and pooled funds/collective investment schemes that invest in any of the above assets.
- address all explicit costs incurred by client pension funds, including broker commissions (direct, soft and recaptured), fund management and custody fees, foreign exchange charges, bank charges, taxation (stamp duty, VAT, etc) and any other costs.
- consider also the impact of implicit execution costs, eg the bid/ask spread, market impact and also opportunity costs.

The Code is limited to those custody costs borne directly by the fund, where the manager undertakes custody or has appointed custodians on behalf of clients. Withholding taxation on income is outside the scope of this Code.

In respect of those pooled funds/collective investment schemes managed by the manager or an associate, the Code provides that managers should disclose the costs incurred by each pooled fund as a whole. Attempts to attribute portions of costs to individual pension funds would be onerous and the results would not be meaningful. Although this "global" information is not currently disclosed in collective investment scheme report and accounts, it should be readily obtainable for "in-house" managed funds. The Code recognises, however, that it may not be possible for managers to obtain this level of detail from third-party funds and from investment trusts which, although they may be managed "in-house", are the responsibility not of the manager but of the relevant boards of directors. In such circumstances, the Code requires prominent disclosure of any proportion of the portfolio that is invested in assets that are not compliant with the Code.

2 Disclosure Requirements

The Code only requires quantitative disclosure of costs that can be measured with certainty. For the other costs listed in Appendix 2, a description of the manager's approach to handling them is required. The Code seeks to encourage disclosure of such costs without advocating any particular methodology as to how this is achieved. However, there is a requirement to state key aspects of methodology, so that informed readers can draw their own conclusions as to the usefulness of the narrative information presented.

It is both permissible and desirable that different house fund management styles, products and specific client requirements result in varying types of reporting. If any particular costs addressed by the Code are on occasion not relevant, or are perhaps more clearly explained by narrative rather than quantitative reporting, this should be noted in the relevant reports.

There are two distinct types of disclosure covered by the Code:

- Level One: company-wide policies, processes and procedures in relation to the management of costs incurred on behalf of clients (see Appendix 1).
- Level Two: client-specific information (see Appendix 2). The most important requirement here is for disaggregation by counterparties to transactions, to the extent and level of detail that provide meaningful information for clients.

The Code envisages that the frequency of client reporting will vary according to the type of disclosure. Level One disclosure should be updated annually, while the quantitative client-specific Level Two disclosure should be made at least six-monthly. In the event of any material Level One changes, these should be reported promptly to clients, not left until the next annual reporting date. These frequencies mirror FSA rules that require certain transaction reports to be made at minimum six-monthly intervals and, in the case of soft commissions, at least annually. More generally, clear, consistent, consolidated reporting is regarded as critical: it will not be helpful to trustees if managers disclose the various costs listed in the Code, or comply with FSA requirements, in a number of different reports or with different reporting dates.

Managers responsible for mandates of a number of different portfolios or asset classes for one scheme, should carefully consider whether it would be more helpful to the trustees if reporting was not fully consolidated but reported at portfolio or asset class level.

APPENDIX 1

LEVEL ONE DISCLOSURE

MANAGER'S POLICIES, PROCEDURES AND CONTROL PROCESSES

Period to which disclosure relates:

Dealing venues and methods – description of the various dealing venues used, eg different types of brokers, dealing for commission and dealing net, internal crossing, crossing networks, etc. How the manager decides between these alternatives and the impact that these decisions have on client transaction costs.

Broker selection and transaction volume allocation process – manager's processes, how brokers' relative competence is established with regard to execution, research, etc. How this results in business level targets for each broker/dealing avenue, how this is split between commission bearing, soft commission and net dealing and how progress towards and variations from these targets are monitored on an ongoing basis. Cross-reference to Level Two Disclosure, based on Appendix 2.

Variations in rates of commission – manager's processes for negotiating commission rates and the impact on rates of investment in different markets, eg UK/overseas, bond/equity, liquid/illiquid.

Soft commissions – manager's internal policy, justification (ie against potential lower commissions) and control processes to ensure compliance with current FSA regulations. Any change in this policy since the last report.

Commission recapture – if applicable to the particular client, a description of the process.

Dealing efficiency monitoring – manager's policy and procedures designed to maximise the value of client portfolios and to control transaction costs while still trading effectively. This will include policy, procedures and assumptions for assessing execution costs, including bid/offer spreads, market impact and opportunity costs, whether the manager measures these and how the results are used.

Conflicts of interest – procedures for complying with FSA requirements for fair treatment of clients in the execution of orders and allocation of trades, and procedures to identify and manage actual and potential conflicts of interest (including dealing through associates). How the manager complies with current FSA regulations on inducements. An approximate number, type and overall value of inducements logged over the period.

External and internal research – differentiation, reasons for choice and evaluation of the benefit received by clients from internal research relative to the cost of external research.

Access to and allocation of Initial Public Offerings and sub-underwriting – manager's policy plus procedures for complying with relevant FSA regulations and evaluation of the benefit received by clients relative to the cost of the necessary commissions paid.

Custody services – where the manager appointed the custodian, an outline of the manager's selection, monitoring and review processes. Costs include transaction and holding charges.

Placing of deposits – manager's policy on spreading deposits, in particular as regards placing deposits with associates, policy on credit ratings, use of money-market funds.

Foreign exchange transactions – manager's policy in spreading foreign exchange transactions, in particular as regards placing these through associates, and policy on credit ratings.

APPENDIX 2

LEVEL TWO DISCLOSURE

Period to which disclosure relates:

Percentage of portfolio at period end not covered by the Code
eg, in third-party collective investment schemes, investment trusts, direct property, private equity, or in commodities.

Fund management fees and any other income derived by the manager

Custody costs borne directly by the fund, and to whom paid

Transaction values/commissions paid

- Transactions traded without commission, as percentage of total transactions
- Transactions subject to broker commissions, as percentage of total transactions
- Transactions subject to soft commissions, as percentage of total transactions
- Total commissions incurred for the period

Taxation

- VAT on Fund Management fees
- VAT on Custody fees
- Stamp duty paid on purchases
- Any other transaction taxes or levies

Other de minimis costs, eg PTM levy on transaction contract notes, need not be disclosed.

Appendix: Part 6 - 1

IFSA Standard No 4.00

Management Expense Ratio

Main features of this Standard are:

- **to specify the principles to be adopted when calculating MER's; and**
- **to provide guidance on the application of those principles, with particular emphasis placed on inter fund and master fund arrangements.**

Table of Contents

IFSA STANDARD NO. 4.00

1 **Title**

1.1 This Standard may be cited as IFSA Standard No. 4.00 "Management Expense Ratio".

2 **Standards and Commentary**

2.1 The standards set out in this Standard are shown in bold print, commentary is shown in normal print, immediately after a standard, as an aid to the interpretation of those standards.

3 **Date of Issue**

3.1 Originally issued 19 July 1999; updated May 2000.

4 **Effective Date**

4.1 This Standard should be applied in the calculation and presentation of MER's on or after 1 August 2000. Earlier application of this Standard is permitted and encouraged.

5 **Application**

5.1 This Standard shall be applied by Scheme Operators when calculating and presenting the Management Expense Ratio ("MER") for an unlisted Scheme or wholesale offering as defined in the IFSA Guidance Note No. 5.00 "Industry Terms and Definitions" ("Scheme").

5.2 Where there is a conflict between the requirements of this Standard, applicable legislation, and the constituent documents of a Scheme, the requirements of this Standard should, having regard to the purpose of the Standard, be modified appropriately so that, as far as is practicable, the Scheme Operator complies with the requirements of this Standard.

5.3 The application of this Standard is not required for superannuation and life insurance products where legislation requires an Ongoing Management Charge to be calculated and disclosed.

5.4 If a member is unsure of the application of this Standard it should consult the IFSA Secretariat. The Secretariat will maintain a precedents file, but when it is unable to decide, guidance can be given by a special subcommittee of the Standards & Community Relations Committee.

5.5 Unincorporated investment vehicles that are listed on the stock exchange have their prices adjusted by the market to take account of their costs and performance. Therefore the cost of running these vehicles should not be taken into account when determining the MER of a Scheme which invests in them (in

the same way that an equity trust does not include the costs of running the companies in whose shares it invests).

6 Statement of Purpose

6.1 The purpose of this Standard is to:

- specify the principles to be adopted when calculating MER's;
- provide guidance in the interpretation and application of those principles; and
- specify the manner in which MER's are disclosed in offer documents and other reports to investors.

6.2 The purpose of the MER is to provide useful information for a potential investor. Directors have a responsibility to ensure statements made in offer documents and other reports to investors are not misleading. If for any reason a Scheme Operator considers the MER as calculated may be misleading, the MER should still be quoted with further information provided to investors whic h clarifies matters. Circumstances where additional disclosures may be provided may include:

- MER's calculated for periods which are not indicative of the future; or
- periods in which fees were waived or expenses were borne directly by the Scheme Operator.

6.3 The MER is to capture expenses, which are incurred by the operation of an unlisted Scheme. Expenses, which would be incurred by a direct investor in the same assets, should be excluded where these can be identified and isolated. The aim is to show investors what extra cost they are paying by using an unlisted managed vehicle.

7 Application of Materiality

7.1 Failure by a Scheme Operator to adopt or implement this standard is material if such failure has the potential to adversely affect the confidence of investors, prospective investors, other scheme operators, and other interested parties involved in the Managed Investments and Life Insurance industries.

8 Definitions

8.1 Refer to IFSA Guidance Note No. 5.00 "Industry Terms and Definitions".

9 Presentation

9.1 The MER shall be presented in tabular form for the last three completed financial years where possible, made up as at the Scheme's balance date, together with a brief description of the method of calculating the MER.

9.2 Where the financial year for the Scheme differs from June 30 the financial year for the Scheme shall be used and appropriate mention made in the MER table.

This is particularly relevant for Master Funds where a range of MERs are called for (see 13.7 and 13.9 below), and where MERs for some of the corresponding periods are unavailable.

9.3 Where the basis of the calculation of fees or expenses is changed or proposed to be changed and where the change would have affected the MER for the last completed financial year if such a change had been in effect, disclosure of the effect of the change shall be made.

9.4 In the case of an initial offer document no MER is required. The document may indicate that a cap will be applied to expenses.

9.5 Where a Scheme has not been in existence for a complete financial year the MER shall be shown either on an annualised basis with reference to the period covered and to the fact that the MER has been annualised or on an 'estimated' basis. (Refer 10.2 below).

10 **Formula**

10.1 For Schemes established for more than one year, the MER shall be calculated in accordance with the following formula:

$$\text{MER} = \frac{(\text{Fees} + \text{Recovered Expenses} - \text{ITCs})}{(\text{Average Scheme Size})} \times 100$$

Where:

Fees = fees that have been or will be deducted from the Scheme in respect of the period covered by the MER, including all the ongoing fees received by the Scheme Operator, whether in the form of cash or other consideration, (up-front and exit fees should not be included); all the fees of a trustee; any other fees such as local and overseas manager and custodian fees or audit fees; and any trailing commissions paid from the Scheme, expressed as a fixed amount. "Fees" include any amounts paid by the trust to the Australian Taxation Office under the GST Reverse Charge provisions.

Recovered Expenses = all expenses recovered from or paid out of the Scheme, incurred by the operation of the Scheme adjusted for the items set out below.

Expenses that would also be incurred by a direct investor in the underlying assets should not be included, for example, transaction costs; brokerage; and repair, maintenance and refurbishment costs.

Government taxes and charges, such as FID or BAD, on purchases and sales of the securities forming the Scheme's underlying assets should be excluded.

Government taxes and charges for transacting on the investors account should be included if they are paid out of the Scheme but may be excluded if they are charged directly to the investor and the offer document discloses this.

GST incurred by the Fund will usually form part of the expense to which it relates (ie , GST charged on management fees). If the expense forms part of the MER, so then will the GST paid in relation to this expense. Therefore, if the expense falls outside the MER calculation, so will the GST paid in relation to this expense.

Schemes, which pay income or other tax (including capital gains tax), should exclude these expenses from the calculation.

Schemes, which undertake specific borrowings for the purpose of investing, should exclude the interest expense on these borrowings from the calculation.

ITCs = Input Tax Credits received or receivable from the Australian Taxation Office on expenses paid or payable by the Scheme, under the GST legislation. The reference to Input Tax Credits includes "Reduced Input Tax Credits".

Average Scheme Size = the result of a calculation made on a daily, weekly or monthly basis, using the same timing as the calculation (accrual) of a Scheme Operator's fees, obtained by:

(i) adding together the Net Asset Values of the Scheme, including net income less expenses on an accrued basis, used at each fee calculation point during the financial year; and

(ii) dividing the amount in (i) above by the number of days, weeks or months in the financial year in question, as appropriate.

10.2 For Schemes which have not been in existence for a complete financial year, the MER shall be calculated either:

(i) **On an annualised basis**

The formula in 10.1 is to be used, but on an annualised basis, with reference to the period covered and to the fact that the MER has been annualised;

OR

(ii) **On an estimated basis**

For example, Estimated MER = A + B + C

Where:

A = all variable fees defined as a percentage of assets (ie. Scheme Operator's fees, Trustee fees, and capped recovered expenses less ITCs recovered) added together. For example 1.5% + 0.5% + 0.1% = 2.1% The reference to "fees" above includes any amount paid or payable by the trust to the Australian Taxation office under the GST Reverse Charge provisions.

B = all other estimated costs (ie. bank charges, audit fees, etc less ITCs expected to be recovered or recoverable) divided by the expected average Scheme size for the coming year expressed as a percentage. For example $20,000/$15,000,000 = 0.1%.

C = a percentage to give an amount of conservatism to the estimated MER (this may be necessary given that MERs are higher when a Scheme is in a growth stage. For example 0.2%) The manager may elect that it be zero%.

The total estimated MER = 2.4%

10.3 Where fees and expenses covered by the definition in 10.1 above are met directly by the Scheme Operator out of its management fee, they would not be included in the calculation of the MER.

11 Inter-fund investments

11.1 Inter-Fund investments may occur between funds operated by one manager (internal interfund investments) or between funds operated by different managers (discretionary and non discretionary master funds).

11.2 The principles underlying the issue of disclosure by all types of inter-fund investments are:

- the MER shall disclose all fees and expenses involved in investing through an interfund structure;
- the definition of an MER for master funds shall be robust enough to capture all types of master fund, namely, those where the investment mix is at the manager's discretion; and those where the investment mix is at the investor's discretion; and
- there must be consistency between all types of inter-fund investments.

12 Internal inter-fund investments

12.1 If there are inter-fund investments between funds operated by the same Scheme Operator then fees and expenses may be rebated in one or more of the funds. Where this is the case, only the annual fees of the trustee and/or Scheme Operator actually charged, and expenses actually recovered, in all funds in the inter-fund chain to the underlying asset portfolio should be included in the MER calculation e.g. where fees and expenses of one fund are rebated in full, there will be no amount included for that fund.

12.2 Conversely there may be duplication of trustee fees, particularly where there is a different trustee in one or more of the funds. In this case, all trustee fees actually charged in each fund should be added together in order to determine the MER of the head Scheme.

13 Master Funds

13.1 Master Funds where Scheme Operator makes asset allocation decisions

13.2 The total MER shall include both:

- the MER of the master fund itself, as defined by the MER formula at 10.1 above; plus
- the weighted average of the MERs of the funds in which the master fund has invested. This should be derived by calculating the average asset allocation percentage for the year in the underlying funds, applying these percentages to the latest available MERs of the underlying funds, and then totalling these amounts.

Example (1):

Scheme A is a master fund that invests in underlying Schemes B, C and D.

Scheme A's own MER is 1.50%

For ease of illustration, it is assumed that Scheme A calculates Scheme Operator's fees every three months.

Scheme A's total MER is calculated as follows:

Scheme A's Asset Allocation ($M):

	Scheme B	Scheme C	Scheme D	Total Scheme
June-0X	10	15	20	45
Sep-0X	10	25	15	50
Dec-0X	30	15	10	55
Mar-0Y	35	20	5	60
	85	75	50	210
	(40.5%)	(35.7%)	(23.8%)	(100%)

MER of Underlying Schemes (%):

	Scheme B	Scheme C	Scheme D
Mar-0Y	1.30	1.50	2.00

Scheme A's Weighted MER (%):

	Scheme B	Scheme C	Scheme D	Total
Mar-0Y	0.53	0.54	0.48	1.55

12 month weighted average (%): 1.55

Scheme A should disclose an MER of 3.05% (ie. 1.55 + 1.50)

13.3 Where the master fund invests in products for which an MER is not published (eg. an insurance bond) the master fund promoter shall make reasonable enquiries to determine the costs of investing in that product. The information obtained should be used in the calculation of the MER of the Schemes.

13.4 The master fund MER should include all relevant information, which can be gained about the extra cost of investing (refer to 6.3 above) in that product. The master fund MER should also include a disclaimer to the effect that the MER is not complete, and note those products for which an MER is not known.

13.5 It is recognised that in some instances, perhaps master fund investing into several sub-funds, it may not be possible to calculate an MER strictly in accordance with the formula as all the necessary input information will not be available. In these instances a 'partial' MER should be calculated using as much information as is available, and this should be quoted with a note explaining where it differs from a 'full' MER. As an example, "The MER of X% has been calculated taking into consideration all the management expense of the A Master Fund, and the MERs of the underlying Schemes where obtainable. We have been unable to obtain MERs for L Scheme, M Scheme, N Scheme and O Scheme, so investors who incorporate these Schemes into their A Master Fund Portfolio should be aware that the effective MER of their investment could be higher than the X% quoted above".

13.6 *Master Fund with sliding fee scale*

13.7 Some Schemes may offer different management fees depending on the amount invested. Where this is the case two MERs should be calculated, one using the lowest management fee charged (x) and one using the highest management fee charged (y). The disclosure made should indicate that the Scheme's MER is in the range x to y. No average MER should be stated for the Scheme unless the corresponding average investment is also stated.

Example (2):

Assume Scheme A's management fees are as follows:

Less than $5,000 invested	1.00% pa.
$5,000 - 10,000	0.75% pa.
More than $10,000	0.50% pa.

Assume Scheme A's own MER without the management fee included is 0.5%. Add this to the weighted average MERs of Schemes B, C and D (using assumptions in previous example).

Scheme A's total MER is calculated as follows:

0.5% + 1.55% = 2.05%

Add Scheme A's lowest and highest fees:

2.05% + 0.50% = 2.55%

2.05% + 1.00% = 3.05%

Scheme A should disclose an MER in the range 2.55% to 3.05%.

13.8 *Master Fund where investor chooses underlying investments*

13.9 Where a master fund offers investors a choice between Schemes, the master fund MER and the MER of each underlying investment should be calculated and the total MER shown as a range of the lowest to the highest of the available options. In addition the latest MERs of the underlying Schemes should be shown separately where known along with the total MER, as these may affect an investor's choice of Schemes.

Example (3):

Scheme A offers investors a choice between Schemes B, C and D. Using the assumptions in Example (1) (ie. Scheme A's own MER is 1.5%) the MER for Scheme A would now contain the following information:

Scheme A's MER is in the range 2.8% to 3.5% depending on the choice of investments. The MERs of the underlying Schemes are:

	Underlying Scheme	Total MER
B	1.3%	2.8%
C	1.5%	3.0%
D	2.0%	3.5%

13.10 Where a master fund has a sliding fee scale as well as offering investors a choice of investments, the methodologies used in Examples (2) and (3) shall be combined to produce the lowest and highest range.

13.11 Some master funds offer investors the choice of options, which are not listed in the offer document (but may be made available by other means). In such cases the master fund offer document shall disclose the range of possible MERs but need not list separately the MERs of the available underlying funds.

Appendix: Part 6 - 2

Colin Grenfell Example

Expense Deduction Tables

COLIN GRENFELL EXAMPLE EXPENSE DEDUCTION TABLES

Table 1 – Retail Plan

The early years

Warning: If you cash in during the early years you could get less back than you have paid in. Annual contributions are assumed to increase by 4.5% each year. The last three columns assume that investments will grow at 7% a year.

At end of year	Total paid in to date	Your investment if no deductions (except contributions tax) plus 7% a year	Effect of deductions to date	W m
	Initial annual contrbution $2,500 :-			
1	$2,500	$2,200	$220	
2	$5,110	$4,650	$360	
3	$7,840	$7,370	$520	
4	$10,700	$10,400	$740	
5	$13,700	$13,700	$900	$
10	$30,700	$36,400	$3,200	$
15	$52,000	$72,400	$7,900	$
20	$78,400	$128,000	$17,000	$
30	$153,000	$340,000	$60,000	$
40	$268,000	$805,000	$177,000	$
	Initial annual contrbution $5,000 :-			
1	$5,000	$4,400	$350	
2	$10,220	$9,300	$560	
3	$15,680	$14,740	$840	$
4	$21,400	$20,800	$1,200	$
5	$27,400	$27,400	$1,600	$
10	$61,400	$72,800	$5,700	$
15	$104,000	$144,800	$14,800	$
20	$156,800	$256,000	$31,000	$
30	$306,000	$680,000	$114,000	$
40	$536,000	$1,610,000	$344,000	$1

What are the deductions for ?

The deductions include the cost of commissions, expenses and charges (except investment expenses) and any surrender penalties and other adjustments. The deductions exclude the cost of life cover and any disablement insurance.
The last line of the table (for an initial annual contribution of $5,000) shows that over a 40 year period the effect of the total deductions could amount to $344,000.
Putting it another way, this would have the same effect as bringing investment growth down from 7% a year to 5.87% a year

Table 2 – Industry Plan

The early years

Warning: If you cash in during the early years you could get less back than you have paid in. Annual contributions are assumed to increase by 4.5% each year. The last three columns assume that investments will grow at 7% a year.

At end of year	Total paid in to date	Your investment if no deductions (except contributions tax) plus 7% a year	Effect of deductions to date	What you might get back
	Initial annual contribution $2,500 :-			
1	$2,500	$2,200	$70	$2,130
2	$5,110	$4,650	$110	$4,540
3	$7,840	$7,370	$160	$7,210
4	$10,700	$10,400	$230	$10,170
5	$13,700	$13,700	$300	$13,400
10	$30,700	$36,400	$700	$35,700
15	$52,000	$72,400	$1,400	$71,000
20	$78,400	$128,000	$2,400	$125,600
30	$153,000	$340,000	$7,000	$333,000
40	$268,000	$805,000	$16,000	$789,000
	Initial annual contrbution $5,000 :-			
1	$5,000	$4,400	$70	$4,330
2	$10,220	$9,300	$110	$9,190
3	$15,680	$14,740	$160	$14,580
4	$21,400	$20,800	$230	$20,570
5	$27,400	$27,400	$300	$27,100
10	$61,400	$72,800	$700	$72,100
15	$104,000	$144,800	$1,400	$143,400
20	$156,800	$256,000	$2,400	$253,600
30	$306,000	$680,000	$7,000	$673,000
40	$536,000	$1,610,000	$16,000	$1,594,000

What are the deductions for ?

The deductions include the cost of commissions, expenses and charges (except investment expenses) and any surrender penalties and other adjustments. The deductions exclude the cost of life cover and any disablement insurance.
The last line of the table (for an initial annual contribution of $5,000) shows that over a 40 year period the effect of the total deductions could amount to $16,000.
Putting it another way, this would have the same effect as bringing investment growth down from 7% a year to 6.95% a year

Table 3 – Bases

Plan Design		Retail Plan	Industry Plan
Non-Investment Fees			
Contribution 1st Yr Fee	(Add'l)	3.00%	0.00%
Contribution Annual Fee		2.00%	0.00%
Annual Charge		$48.00	$49.40
Charges linked to		CPI	AWOTE
Annual Charge Inflation		3.00%	4.50%
Management Fee	(of Assets)	1.00%	0.00%
Benefit Charge		$60.00	$20.00
Benefit Charge Inflation		3.00%	4.50%
Investment Fee	(of Assets)	0.50%	0.50%
Assumptions			
Earning Rate (net of tax)		7.50%	7.50%
Salary Increases		4.50%	4.50%
SG Rate		9.00%	9.00%
Earning Rate net of Investment Fee		**7.00%**	**7.00%**
Earning Rate net of Investment and asset based Management Fees		6.00%	7.00%

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