

CSA PROPOSES NEW DISCLOSURE REQUIREMENT FOR EXCHANGE TRADED FUNDS

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On June 18, 2015, the Canadian Securities Administrators ("**CSA**") published proposed amendments (the "**Amendments**") to National Instrument 41-101 *General Prospectus Requirements* (the "**NI 41-101**"), Companion Policy 41-101CP to NI 41-101 and related consequential amendments for a 90-day comment period. The Amendments will require exchange-traded mutual funds (the "ETFs") to file and deliver a summary disclosure document to investors called "ETF Facts".

Background

The publication of the Amendments marks Stage 3 of the CSA's implementation of the point of sale disclosure project (the "**POS Project**"). Since July 2011, every mutual fund has been required to produce and deliver a fund facts document (the "**Fund Facts**") instead of a prospectus when an investor purchases mutual fund securities. As part of the final stage of the POS Project, the CSA is developing a CSA risk classification methodology for use in the Funds Facts and ETF Facts. The CSA risk classification methodology aims to establish a standardized scale for disclosing a fund's investment risk level.

Codification of Exemptive Relief

Under securities legislation, the requirement to deliver a prospectus is triggered when securities of an ETF are newly created and distributed (sometimes referred to as creation units). Creation units are issued by the ETF to dealers that resell them on the exchange. Investors purchasing ETF securities generally have no way of knowing whether their order is filled through creation units or previously issued ETF securities. Prior to the Amendments, ETF dealers had to rely on exemptive relief from the requirement to deliver a prospectus to the investor. The Amendments codify the exemptive relief which is applicable to all dealers acting as agents of investors purchasing ETFs.

Contents of ETF Facts

The Amendments have been tested with investors in two phases: (1) qualitative research by interviewing 28 investors and (2) quantitative research through an online questionnaire with 533 investors. The results of the

tests have informed the content of the ETF Facts.

The Amendments will require ETFs to create a summary disclosure document that contains key information investors require when trading in ETFs (i.e., risk, past performance, and the costs of investing in an ETF). Similar to Fund Facts, the ETF Facts must be in plain language and no more than two pages double-sided.

Unlike conventional mutual funds, ETFs are traded over an exchange and investors cannot subscribe directly for ETF securities. Since ETFs are traded over an exchange, the CSA proposes the inclusion of additional information related to market price, bid-ask spread, and premium/discount of market price to net asset value.

A separate ETF Facts is required for each class or series of securities of an ETF. Further, the ETF Facts must be made available on the ETF's and ETF manager's website.

The form requirements for the ETF Facts are set out in the Amendments as Form 41-101F4.

Filing Requirements

The ETF Facts must be filed concurrently with the ETF's prospectus. If the disclosed information in the ETF Facts changes materially, an amendment to the ETF Facts and an amendment to the ETF's prospectus must be filed.

Delivery Requirements

The Amendments require dealers to deliver ETF Facts within two days of an investor purchasing ETF securities. Delivery of the prospectus to the investor is not required but, the prospectus must be made available upon request, free of charge.

Prior to the Amendments, the obligation to deliver the prospectus was on the dealer acting as underwriter, that could not readily identify the purchaser. The Amendments shift the delivery obligation from the ETF underwriters to dealers acting as agents for ETF purchasers.

Transition

The Amendments will take effect in two transition phases.

The first transition phase will take effect nine months after the publication date of the final rules aimed at implementing the Amendments (the "Publication Date"). The first phase will require ETF managers to file ETF Facts for each class or series of the ETF within 14 months of the Publication Date .

The second transition phase will take effect 24 months after the Publication Date. The second phase will require dealers to deliver an ETF Facts to the investor within two days of an ETF purchase.

Investor Rights

The rights of an investor for a dealer's failure to deliver an ETF Facts will be consistent with the rights of an investor for a dealer's failure to deliver a prospectus. If the investor fails to receive the latest ETF Facts by midnight of the second business day after the purchase of securities, the investor will have a right to damages and a right to rescind the purchase.

Under current securities legislation, investors have a right of withdrawal within two business days after receiving the prospectus. Under the Amendments, there is no longer a prospectus delivery requirement for the purchase of ETFs and no right of withdrawal. The Amendments do not extend the right of withdrawal to investors in respect of the delivery of the ETF Facts.

Further, ETF Facts will be incorporated by reference into the prospectus. Accordingly, the existing rights of investors relating to misrepresentations in a prospectus will also apply to misrepresentations in the ETF Facts.

Purpose

With the Amendments, the CSA seeks to reduce the presence of information asymmetry between investors and participants in the ETF industry. With key information about an ETF, the ETF Facts allows investors to compare ETFs and make informed decisions, which is consistent with the OSC's 2015 Statement of Priorities to empower investors through better disclosure. The OSC's next steps are to continue to work with the CSA to implement the POS Project.

The CSA seeks feedback on several aspects of the Amendments, including:

- disclosure instructions for elements outlined in Form 41-101F4 (e.g., average daily volume, number of days traded, market price range, net asset value, average bid-ask spread etc.)
- whether there are other disclosure items/topics that should be added to reflect the difference between ETFs and conventional mutual funds
- appropriate transition period to file the initial ETF Facts
- the approach proposed to not extend the right of withdrawal to the delivery of ETF Facts.

The deadline for submitting comments to the CSA is September 16, 2015. Please contact a member of our [*Investment Funds & Asset Management Group*](#) if you have any questions or seek assistance with the preparation of a comment letter.

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A Cautionary Note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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