BMO Mutual Funds

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Paola Cifelli
Legal & Policy Counsel
Manager, Compliance
Tel: (416) 643-1820
Fax: (416) 867-4015
paola.cifelli@bmo.com

VIA E-MAIL

Joint Forum Project Office
Joint Forum of Financial Market Regulators
5160 Yonge St. 17th Floor, Box 85
North York, ON M2N 6L9
jointforum@fsco.gov.on.ca

RE: REQUEST FOR COMMENT – PROPOSED FRAMEWORK 81-406

BMO Investments Inc. ("BMOII"), a member of the Mutual Fund Dealers Association of Canada and fund manager of the BMO mutual funds, welcomes the opportunity to provide this submission in response to your request for comment on Proposed Framework 81-406 ("81-406").

BMOII strongly supports the principles embodied within 81-406 relating to better, simplified and more meaningful disclosure for retail mutual fund investors. We commend the Joint Forum for their efforts to create a more level playing field between mutual funds and segregated funds. We welcome the Joint Forum's proposal to replace the simplified prospectus as the primary regulatory disclosure document with an abridged fund summary document that provides investors with key information standardized across fund companies in a user-friendly layout ("Fund Facts"), and agree that prospectuses should only be delivered to investors when specifically requested. The purpose of this letter is to identify and provide context in relation to specific and significant concerns we have with certain aspects of 81-406. Our comments will cover the proposed delivery model under 81-406 as well as the form and substance of the Joint Forum's Fund Facts sample. They will also cover areas that, while not directly impacting BMOII's business model, affect mutual fund investors and the health and efficiency of the mutual fund industry generally.

A. Delivering Fund Facts

BMOII is concerned that the significant challenges in meeting the methods of delivery proposed in 81-406 within the various distribution channels through which mutual funds are sold will ultimately decrease access to mutual fund investing for retail investors.

(i) Face-to-Face Sales Channels

A requirement to actively deliver Fund Facts before a transaction takes place may not meet investors' needs and expectations in some face-to-face sales environments. Salespersons in the IDA channel who offer a broad range of investment products may be less likely to recommend a suitable mutual fund if they do not have the fund's corresponding Fund Facts on hand and in deliverable format, or because it may not be immediately possible to ensure that the version they do have on hand is the most up-to-date. Investment dealers may have to be selective about the range of mutual funds or fund families they will offer because maintaining hard copies of all corresponding Fund Facts is subject to space and mobility constraints, and because monitoring updates made to the Fund Facts of a full suite of mutual funds is simply impractical. Further, dealers may be more likely to recommend another type of investment product to the client not because it is the most suitable product, but because it also meets the client's objective to effect a transaction quickly and contemporaneously with a single meeting with their advisor. If investors feel inconvenienced or delayed by prescriptive delivery requirements, they may simply wish to move on to less regulated investment options for no other reason than ease of transacting. This would create an unleveled playing field between mutual funds and riskier exempt offerings until such time as regulators prescribe equivalent disclosure requirements for such investments.

Mutual fund salespersons do not always meet with clients in a branch where they have access to printers or stockpiled Fund Facts, and sometimes meet at the client's home or place of business where web downloading and printing may not be possible. The salesperson will not always have the benefit of knowing in advance which funds will be appropriate for the client as this would be determined by a suitability discussion yet to come, and may not have the corresponding Fund Facts on hand. We do not believe that a delay in implementing a recommended solution will help to instill investor confidence in the mutual fund investing process.

(ii) Call Centres

BMOII provides secure and convenient telephone access to investors who do not wish to, or simply cannot, attend in person at a branch or use online access to transact in their mutual fund accounts. As the winner of the 2006 Dalbar Mutual Fund Service Award, BMO Investment Centres have been recognized for meeting and exceeding the needs and expectations of our customers in the telephone sales environment. BMOII employs approximately 35 investment specialists at each of our two investment centres at any given time, who respond to inbound calls from investors six days a week. Our call centre complement increases by over 50% during peak periods. These figures speak to the sheer volume of investors who use this service as a convenient and expeditious means of transacting remotely throughout the year and in particular at key times of year. If sales representatives were required to lengthen every call to explain and arrange fax, email or mail delivery of a document, customer response times and overall call quality will be compromised at the expense of our investors. For this reason and for the reasons below, we believe it is imperative that 81-406 offer investors some flexibility in the telephone environment.

When investors contact our investment centres, they are typically initiating a mutual fund transaction. As such, the adage that "mutual funds are sold, not bought" generally does not apply to the telephone environment. In most cases, our clients who transact by phone are already familiar with the product they wish to purchase, have researched it on their own and call simply to place their desired trade.[1] They expect that they will be able to effect their desired or recommended transaction in real time during one session. We have no reason to believe that investors would welcome being told that they cannot transact during one call but rather must receive an email, fax or mailing first and then call back to confirm their trading instruction. In fact, such a process would defeat the purpose for which many investors use telephone access, which allows them to continue investing while they are on vacation or otherwise away from their residence without access to email, personal fax or a near-by branch.

[1] By way of example, on October 9, 2007, a client phoned the BMO Investment Centre to make a contribution to her child's RESP, with the express wish to make a purchase of BMO MatchMaker Strategic Security Portfolio 2. The client did not require any product advice, knew what product she intended to purchase and how much she wished to invest before she called. The bulk of the 4 minute conversation was spent confirming the client's identity and discussing recent changes to RESPs under the 2007 Federal Budget.

A requirement to actively deliver Fund Facts before a transaction can take place could be detrimental to clients toward the end of RRSP season when the timing of a transaction is of the essence. Historically, our call centre volumes spike from approximately 650 calls per day during regular periods to over 2500 in peak periods such as the remaining days of RRSP season, the last day in particular, when investors are anxious to make their contribution quickly and already feel as though they are "fighting the clock". If investors were told they have to wait even longer to first receive and read a document and then call back, we are concerned that not only would a negative client experience result at a time of heightened anxiety, but in some cases investors would fail to meet a crucial deadline. In periods of high volatility in either market downturn or upswing, when investors are anxious to move quickly, delays caused by rigid delivery requirements could expose dealers to complaints for losses incurred or gains forgone.[2]

We are concerned that this delivery requirement would be particularly harmful to our more mature or less mobile clients who rely almost exclusively on telephone access and may not have an email account or access to a personal fax machine. At a minimum, if 81-406 proceeds as proposed, we strongly urge the Joint Forum to give investors some flexibility to waive active point of sale delivery of Fund Facts where they simply cannot offer their telephone representative a real-time method of delivering it. Without this alternative, the discussion will simply lead to an impasse when investors attempt in vain to negotiate a timelier outcome, leaving them feeling ill-served when we are unable to offer them any other option but to visit a branch or wait for the mail.

A highly developed and sophisticated mutual fund industry must be flexible enough to offer investors better than requiring them to either receive direct emails if they wish to transact by phone, or otherwise face the inherent delays of mail delivery. Consumers generally do not receive personalized emails from their financial institutions unless they have an established relationship with a representative there or have subscribed to a service, and may have legitimate concerns about this proposal in light of warnings in the marketplace regarding "phishing", fraud, spam, unsolicited marketing and viruses. Although we recognize that a call centre representative will have advised the client that an email would be forthcoming, what we wish to stress is that emails from financial institutions are not so commonplace that investors should be expected to either accept them or be forced to wait for the mail or visit a branch to transact in an account they may have had for years. Additionally, email is not yet considered a completely secure environment. Emails can be diverted despite the sender's best efforts, which could result in the actual recipient learning that the intended recipient named in the email has investment dealings with BMO.

(iii) Online Click-through

BMOII provides up-to-date regulatory disclosure about our funds directly on our website, which investors are able to view at their leisure during their online session. Fund Facts for BMO funds would also be posted to the site, and investors could consult them if they chose to at any time.

The Joint Forum should clarify what it envisions in terms of a "click-through" Fund Facts, as this proposal appears to require more than simply posting Fund Facts on the website and giving investors access to it during their online session. A common feature of a "click-through"

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[2] By way of example, during the period of market correction in mid-August, the BMO Investment Centre received a call from a very anxious client who wished to move the entirety of his investments from aggressive growth mutual funds into BMO T-Bill Fund. The client was very concerned about the recent market downturn and reiterated his need to "move into something secure and low risk" immediately. The client even asked the representative to proceed more quickly in taking down his trading instructions. The client became calmer when the representative advised him that the transaction would occur as of that day's date and that day's price.

document is the ability to click "I Agree" to confirm having read, and usually acknowledging an understanding of, the contents, or conversely, to click "I disagree" and not be permitted to continue. This process, however, would not be consistent with the Joint Forum's position that dealers will not be required to have investors acknowledge receipt of the Fund Facts, nor would it provide a consistent experience as between online clients and clients who transact in a face-to-face environment. It is unclear what other features the online Fund Facts would be expected to have. Would the Fund Facts need to "pop up" automatically when the mutual fund is selected for purchase? Would a link placed on the transaction site to a PDF version of the Fund Facts be sufficient? Dealers require further details to assess any technological requirements they would need to add to their online environments, as well as the complexity and cost of such technology.

One option for the Joint Forum to consider is whether Fund Facts documents in the online environment could exist in a consolidated forum owned by either industry or regulators. A deep link from the dealer's website to the Fund Facts posted on SEDAR may be an option, assuming that the SEDAR environment can be made more easily navigable for investors in conjunction with the Point of Sale initiative. This would avoid having each individual dealer ensure that the most up-to-date Fund Facts for every non-proprietary mutual fund it offers is available on its own website at all times, which would increase the likelihood that some investors will receive outdated documents and that some dealers will scale back their online offerings to accommodate space limitations on their servers. Having dealer sites that deep link into a fund manager's website also presents challenges, including each dealer having to ensure at all times that the fund manager has not changed or disabled the linked page.

(iv) Exemptions – Discretionary Managed and Self-Directed Accounts; Portfolio Managers

Although 81-406 is silent on whether any particular sales channels would be exempt from the proposed delivery requirements, we submit that delivery of Fund Facts in the discretionary management environment is neither necessary nor relevant and should be exempt. In these arrangements, investors have entrusted the selection and management of their investments to a manager based on predetermined criteria and without the expectation of consultation about individual investment choices. Currently, such investors would not necessarily receive disclosure materials. Similarly, portfolio managers who manage a fund of funds product should be exempt from having to receive the Fund Facts for purchases made of the underlying mutual funds. Clearly 81-406 was not meant to address either scenario. Clients who have opted for a self-directed environment have clear expectations about the timeliness and convenience in the conduct of their trades and should not be subjected to prescriptive disclosure requirements. While these investors should no doubt have access to information, this can be achieved by the various electronic channels through which Fund Facts could be made available to the public on a continuous basis.

(v) Subsequent transactions

BMOII does not agree with delivering Fund Facts for subsequent transactions as a matter of course. We fully support actively providing it to clients who ask for it at any time and posting the most recent Fund Facts onto our website, but do not believe that all investors should bear the cost of automatic delivery for subsequent transactions when in many cases the Fund Facts may not have changed materially since the investor last received it. If there has been no material change at the next purchase date, there is no reason to inundate the investor with redundant information. We also note that robust information about the fund is available in the continuous disclosure domain. Also, the majority of transactions that occur after account opening occur through continuous purchase plans, over the phone or online; we direct the Joint Forum to our comments above regarding the challenges of the proposed delivery model for Call Centre and Internet transactions.

B. Alternative Methods of Delivery

BMOII looks forward to participating in further discussions with the Joint Forum, IFIC and other industry participants to help arrive at a delivery model that accords with business realities and investor expectations, while ensuring that investors have access to information that will help them make informed investment decisions. Industry participants are considering various alternatives to the methods of delivery proposed in 81-406, specifically for sales environments that are not traditional "bricks and mortar" branch offices. One alternative is to deliver Fund Facts at account opening and require dealers to actively advise investors during the account opening process, such as through the proposed Relationship Disclosure Document, about the ongoing availability of Fund Facts. Fund Facts could then be made available on a continuous basis electronically, either on the fund manager's website or on a common industry or regulator-owned database. Fund Facts could also accompany the trade confirmation, which can leverage off the *SmartProspectus* infrastructure already in place.

Flexibility is especially needed in the telephone sales environment. Investors who use call centres should be given the opportunity to waive mandatory pre-transaction delivery of Fund Facts, but could still be advised that Fund Facts is available to review before they make their purchase decision. This treats investors fairly, gives them choice and flexibility to decide how quickly they wish to proceed with their transaction. It also gives investors the opportunity to advise us if they already reviewed the fund's Fund Facts online prior to contacting the call centre and therefore do not need to see it again.

C. Producing and Filing Fund Facts

BMOII also wishes to comment on the form and content of the sample Fund Facts document and the proposed filing requirements.

(i) Presentation

A presentation of Fund Facts on a stand-alone basis does not address the prevalence of portfolios. Investors are not necessarily looking for one fund in isolation but at a long-term portfolio solution, and advisors are increasingly devising long-term and diversified plans for their clients, presenting them with a series of portfolio options rather than simply selling them a mutual fund. A minority of accounts held at BMOII holds a single fund; most hold multiple funds, including portfolios offered under an asset allocation service. 81-406 should allow fund managers some flexibility to consolidate Fund Facts on a basis that they consider most useful to their investors and to advisors.

We also urge the Joint Forum to allow, at a fund manager's option, some form of consolidation for a portfolio of mutual funds offered under an asset allocation service and sold as a single solution. This would present the investor with more accurate information, as the stand-alone Fund Facts for each of the underlying funds would not reflect each fund's proportional representation in the portfolio, past performance of the portfolio, or the portfolio's overall risk ranking.

Certain other key fund-specific information that currently appears in the simplified prospectus should be transitioned to Fund Facts. This includes investment objectives and purchase minimums, both of which merit a prominent position on Fund Facts.

(ii) Fund of Funds

We would ask the Joint Forum to clarify its expectations around the look and feel of the Fund Facts of a mutual fund whose underlying investments are other mutual funds rather than individual securities. To ensure simplicity and continuity with other regulatory disclosure documents, the requirements for determining the "Top 10" investments and "Investment mix" for a Fund of Funds product should follow the method of calculation used in National Instrument 81-106.

(iii) Flesch-Kincaid Grade Level 5.0

We do not believe it is necessary to prescribe a specific readability level for Fund Facts. The mutual fund industry supports a plain language approach and has demonstrated its ability and willingness to produce user-friendly documents without being tied to strict form requirements.

(iv) Performance Reporting

Further clarity is needed around the method of calculating fund performance. The calculation used for determining average return would need to be prescribed in order to avoid the use of different methodologies from one fund company to another. The requirements around presenting performance data for young funds, including whether to exclude performance data until a prescribed period of time has passed, must also be included in 81-406.

The Joint Forum should consider including standard performance data in Fund Facts. These returns reflect industry reporting standards, are widely published, appear on fund manager websites and are reported by research firms. Fund Facts should strive to report performance in a manner that is consistent with other sources of information that investors may consult.

With respect to the growth of $1,000, we note that the line graph representing the growth of $10,000 was repealed from National Instrument 81-101FI when National Instrument 81-106 came into effect. While we are not opposed to showing the growth of $1,000, the explanation of the growth must be meaningful for investors. For example, there is no indication how redemptions or the reinvestment of distributions, or their payout, affect the investment's growth.

(v) Risk Ranking

The risk disclosure section of Fund Facts may not provide sufficient information to meaningfully explain risk relativity. With reference to the Fund Facts sample, "moderate risk" alone does not tell clients what "risk" measures or what the ranking means. Some explanation is needed because standard deviation is not an intuitive concept. If the sentence "When you invest in a fund, the value of your investment can go down as well as up" is meant to appear in the Fund Facts for any mutual fund, even a money market fund, it begs the question as to what makes one fund's risk ranking different from another's. Under "Who is this fund for?", stating that the fund is suitable for an investor who "can handle the ups and downs of the stock market" overlooks investors' real concern, which is the *degree* and *frequency* of volatility associated with a particular investment.

If fund companies were permitted to consolidate Fund Facts where appropriate, they could add a fuller discussion of risk and the risk management qualities of diversification in a common section without making the fund-specific Fund Facts any longer. For a portfolio under an asset allocation service, the risk section would give investors a truer sense of the volatility of the overall portfolio.

(vi) Cost and Compensation Disclosure

BMOII fully supports transparency with respect to the costs of investing in mutual funds and the compensation paid to our salespersons, but does not believe that the Fund Facts document is the appropriate place for such disclosure. Rather, we believe that cost and compensation disclosure should be made at account opening, possibly in the proposed Relationship Disclosure Document. In fact, the present draft of the MFDA's sample Relationship Disclosure Document includes explanatory information about the costs of purchasing and holding investments, as well as sales fees paid to dealers and their representatives. Proposed National Instrument 31-103 also proposes that cost and compensation information appear in the Relationship Disclosure Document of non-SRO members. By placing this information in a fund summary document, costs and compensation information that is dealer/account specific would be excluded. As a general principle, Fund Facts should focus on the fund and not merge "dealer" and "manufacturer" concepts. Moreover, the fact that the mutual fund salespersons of bank-owned dealers are salaried employees of the bank with various incentive pay arrangements does not fit within the Fund Facts model. BMO mutual funds, when purchased through BMO Investments Inc., are no load funds. The no load option is not contemplated at all on Page 2 of the sample Fund Facts.

(vii) Rights of Withdrawal and Rescission

In its 2003 *Point of Sale Disclosure* Consultation Paper, the Joint Forum states that the right of withdrawal is directly tied to the fact that dealers are not required to deliver the prospectus until after the purchase agreement has been entered into. Under 81-406, the right of withdrawal is tied to the giving of instructions rather than to delivery of the Fund Facts; it is therefore unclear what need the cooling-off period is meant to address. If the cooling-off right is retained, it is crucial that it be drafted to ensure that other unitholders and the fund itself are not harmed in any way when one unitholder exercises it. Further dialogue between industry and regulators is required to identify and close any gaps that a cooling off period may present in order to ensure that it cannot be manipulated at the expense of other unitholders. Only then will the mutual fund industry preserve the integrity and consumer confidence it presently enjoys.

(viii) Timing of Filings

With respect to the timing of filing, the proposal states that Fund Facts will have to be filed with the fund manager's prospectus documents as well as filed and updated annually and semi-annually with its continuous disclosure documents. For fund companies like BMOII whose prospectus renewal date is typically within one month of its interim disclosure, it is unclear what value to investors is achieved by back-to-back filings. Another concern with timing an updated Fund Facts to coincide with a prospectus renewal date that immediately precedes interim disclosure is that the Fund Facts that is filed with the prospectus, presumably based on information that appears in the fund's interim financial statements, would release financial data via Fund Facts to new unitholders before existing unitholders receive this information through the release of the financial statements and the interim Management Reports of Fund Performance (MRFPs)). Further clarity is therefore required with respect to the reporting periods to be used.

D. Other Regulatory Mandates

(i) SRO Auditing

The delivery methods proposed in 81-406 present significant compliance challenges with respect to retaining and producing proof of delivery of every email and fax sent to clients. One such challenge would be developing a suitable archival and retrieval system, in particular because emails and faxes would constitute "relationship records" under National Instrument 31-103, the retention requirement for which means that dealers would effectively have to keep emails and faxes to long-term clients in perpetuity.

(ii) Integration with other initiatives

BMOII is committed to ensuring our clients have access to the most current information about the mutual funds we offer, but while we firmly support *better* disclosure, we do not support duplicative disclosure in multiple documents, in particular when unitholders bear the cost. We believe that 81-406 creates an opportunity to consider all regulatory disclosure, present and proposed, in tandem with a view to dispensing with, merging or streamlining disclosure where duplication exists. For example, consideration should be given to whether some portions of the simplified prospectus can now be streamlined or should be transitioned elsewhere if clients will no longer be receiving it as a matter of course. Frequent and short-term trading restrictions and penalties is just one topic that merits more prominent disclosure than in a document that virtually no one will receive. The Joint Forum should also consider whether there are opportunities to streamline MRFP and Quarterly Portfolio Disclosure requirements. We believe it is a disservice to investors that they bear the cost of repackaging information that is already publicly available without a meaningful review of whether opportunities exist to reduce their overall costs.

The Joint Forum makes reference to the paradox of "information overload" in its proposal document, which we fear will not be assuaged by adding an additional layer of disclosure without first critically examining what investors already have access to and what they may receive in the future under other regulatory initiatives. We also see opportunities to integrate the Fund Facts discussion with the proposed Relationship Disclosure Document, other aspects of the Client Relationship Model and the Registration Reform Project. A coordinated and holistic approach to disclosure can only serve to benefit investors.

BMOII thanks the Joint Forum for the opportunity to provide our thoughts on Proposed Framework 81-406. We are strongly in favour of a simplified, reader-friendly and standardized fund summary document, and we look forward to further consultation regarding its contents and how to introduce it to the sales process so that it meets investors' needs and expectations. Should you have any questions about this submission please feel free to contact the undersigned.

Yours truly,

Paola Cifelli
Legal & Policy Counsel
Manager, Compliance