

June 9, 2000

Securities Review Advisory Committee
c/o Purdy Crawford
Osler, Hoskin & Harcourt LLP
Barristers & Solicitors
Box 50, 1 First Canadian Place
Toronto, Ontario M5X 1B8

Dear Mr. Crawford:

Re: Securities Review Advisory Committee – Response to Request for Comments

This submission is made by the Government Relations Committee of the Investment Counsel Association of Canada (“ICAC”) in response to the Securities Review Advisory Committee (“SRAC”) request for comments dated April 28, 2000. The ICAC is an association representing 55 investment counsel/portfolio management member firms across Canada with responsibility for managing approximately \$200 billion of client assets on a segregated or pooled basis (as opposed to public mutual funds).

The ICAC is pleased to have the opportunity to comment on the existing securities legislation and to express the needs of the portfolio management community for more up-to date securities regulation. We support the objective of securities regulation to protect investors and to foster a fair and efficient marketplace. The issues affecting Investment Counsel/Portfolio Managers raised below are the more important items that need to be addressed in the context of reviewing and revising the current statutory regime. Other issues raised on your Issues List could be dealt with on a consultative basis at another time.

I. UNDERLYING PRINCIPLES - POOLED FUNDS

In-house managed pooled funds are used by portfolio managers for cost efficiency, similarity of performance and fairness in trade allocation with resulting lower transaction costs for clients with similar investment mandates. The term "Pooled Fund" in contrast to the term "mutual fund" has no definition under securities legislation but is a term commonly used in the investment industry. A Pooled Fund is used in the context of a collective investment vehicle in which contributions of clients with a common investment objective are pooled for the purposes of investment. The pooling of client funds in this way is undertaken as part of the discretionary portfolio management services rendered to clients rather than with a view of "trading in securities". Management fees for discretionary portfolio management services provided are based on assets under management not trade execution. The current regime does not account for the fact that fee based discretionary advisory services are increasingly being

delivered through the use of Pooled Funds, whose purpose is to deliver the same services as are available on a segregated basis to clients while attracting lower transaction and administrative costs.

A. PROSPECTUS EXEMPTIONS: SPRINKLING RELIEF NEEDED / DEFINITION OF ACCREDITED INVESTOR SHOULD EXTEND TO COVER MANAGED ACCOUNTS.

The current statutory regime treats units of Pooled Funds within the definition of "mutual fund" rather than "private mutual fund". The result is that each time units of Pooled Funds are issued, regard must be had to available prospectus exemptions. This does not foster efficient capital markets in that the use of pooled funds, whose purpose is to more efficiently deliver investment management services, creates a regulatory barrier where none would otherwise exist in the context of a discretionary relationship. In particular, the prospectus exemption regime is problematic for discretionary investment management services through Pooled Funds as no sprinkling relief is available within a family of in-house managed Pooled Funds. The Commission has not entertained applications for ad hoc relief in this area since the early 90's. Typically, money is managed through Pooled Funds with different investment objectives e.g. Canadian equities, bonds, money market, US, EAFE, Global. The requirement for a prospectus makes little sense as the portfolio manager is making the investment decision pursuant to discretionary authority in accordance with the client mandate. The legislation needs to recognize that the portfolio manager should be deemed to be acting as principal for accounts fully managed by it. Ontario has recognized that concept only through Rule 45-504 [Prospectus Exemption for Distributions of Securities to Portfolio Advisers on Behalf of Fully Managed Accounts} but that 'sprinkling relief' does not extend to in-house managed-Pooled Funds. There are contradictions in a system that allows a portfolio manager to purchase any amount of an individual security for a client's segregated discretionary account while restricting the Portfolio Manager from making smaller investments, on behalf of a client's discretionary account, in a diversified pool of securities.

The development of a draft rule pursuant to the concept paper "Revamping the Exempt Market" should recognize the concept of a portfolio manager being deemed to be acting as principal for a Managed Account and include Managed Accounts on the list of Accredited Investors. There should be no regulatory impact of discretionary funds being managed on a pooled vs. segregated basis, when the purpose of pooling is to provide additional cost efficiencies and fairness in trade allocation for the benefit of clients. Cooperative efforts at the CSA level rather than unilateral provincial efforts on registration and prospectus exemptions in the exempt market are strongly encouraged with the *objective of integration and harmonization*.

B. FILING FEES

The need for prospectus exemptions for Pooled Fund investment necessitates the filing of forms and the payment of fees under the current regime. This regime does not account for discretionary investment management services being provided on a "portfolio basis" rather than "transaction basis" with management fees based upon "assets under management. For example, it does not contemplate or facilitate asset mix shifts within a family of funds. If money is managed using segregated money management, these issues do not arise and the client does not receive the benefits and efficiencies of pooling.

The payment of filing fees on a transactional basis represents direct taxation based on dollar values with no tapering of fees. This bears no relation to administrative services provided by the commission. Pension moneys or savings of individuals should not be taxed in this way. Fees and filings on Pooled Fund investments and fund on fund investments (amounting to double taxation) should be eliminated. Fees applied in the prospectus exempt market should be reflective of a user pay system.

II. FOCUS & SCOPE OF LEGISLATION

The following comments follow the numbering adopted in the published Issues List.

8. Nature of the Institution:

We support the proposition that regulation of financial services should focus more on the service provided rather than on the nature of the institution providing the service subject to the qualification that the regulation should focus more on the needs of the persons receiving such services. The current securities law regime favours various institutions, which promotes an unlevel playing field among competitors. Harmonization of regulation at both federal and provincial levels is both necessary and desirable.

Corporate Sponsored Plans:

Corporate sponsored plans invested in Pooled Funds should be treated with separate consideration and as different from a retail mutual fund product. With respect to participant directed corporate sponsored plans, we are of the view that the broad-brush implementation of the current securities law "prospectus regime" to fund on fund investment in a Pooled Fund is not the answer. A tailor-made approach to investor protection in this area should start with the needs of the plan participants. It should address the quality of the people explaining the information and the qualifications and track record of people managing the investment of assets. What is needed is a more flexible approach to securities regulation, with emphasis on education where choices are made available, to more adequately meet the needs of these investors.

10. Integration with *Commodity Futures Act*

The *Commodity Futures Act* should be integrated with the *Securities Act* as done in BC and Alberta with the securities commission to be given jurisdiction over derivatives. *The objective should be for registrants to deal with a more simplified and integrated set of regulations governing investment management services and to be subject to one statutory regime.*

Regulation Of Registrants

The ICAC considers the topic of regulation of registrants an important one . We are currently making our views known through the OSC committee set up to study this topic. We appreciate the opportunity to provide comments in this area and we support objectives to simplify and streamline registration. Generally, we do not support the introduction of broad concepts such as "otherwise advising with respect to securities" and "exert influence over decision-making" unless there are clear definitions adopted and meaningful guidelines. *There should be an objective of clarity and certainty for registrants.* Discretionary investment management services provided by portfolio managers should not be confused or mixed with dealers buying and selling securities.

Universal Registration

It is necessary to have a harmonized system of registration for registrants across Canada with a unified set of forms and standards. Streamlining and revamping categories should be dealt with at a national level through the CSA. The current regime is administratively very difficult and burdensome for registrants. *The objectives of streamlining and paperwork reduction are both necessary and highly desirable.*

17. Custody Services

It is desirable to have the provision of custody services regulated with proper controls given: i. the importance of the operations of the custody service providers to investors; ii. the concentration of and limited number of custody service providers in Canada; and iii. the considerable amount of assets held in custody. The responsibilities undertaken by custodians are considerable and proper conduct in the role of the custodian is vitally important to both investors and portfolio managers.

Continuous Disclosure Obligations -General

Enhanced disclosure for investors and accountability through monitoring and assessment efforts by the commission are desirable objectives for investors in the secondary market. The goal to make it simpler for companies to access the market while providing enhanced disclosure for investors is desirable. Investors need confidence in the reliability of the information provided.

Enforcement - Insider Trading

Early detection and enforcement of insider trading violations are necessary for the integrity of the financial markets. There should be more emphasis on enforcement to police insider trading for the sake of all market participants. If the commission considers that it is lacking enforcement authority in dealing with insider trading violations then that issue should be addressed immediately,

The forgoing highlights various issues affecting Investment Counsel/Portfolio Managers that need to be addressed in the context of reviewing and revising the current statutory regime. It has not been possible to comment on all the issues presented on the Issues List given the relatively short comment period. However, we would be pleased to provide further input on these and any other issues. In the event you have any questions or queries concerning the above, please respond to either of the following two contact persons both of whom are members of the Government Relations Committee of the ICAC:

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Yours truly,

The Investment Counsel Association of Canada
Per:

Robert H. Steinbach
President

cc. **Dan Iggers**, Corporate Secretary OSC & **Robert Day**, Manager, Business Planning OSC
Re: Statement of Priorities for Fiscal Year ending 3/31/01
Roberta Cowdery, OSC Capital Markets, Investment Funds
Jamie McVickers, OSC Capital Markets, Policy/Regulation

/sjm