THE INVESTMENT FUNDS INSTITUTE OF CANADA
L'INSTITUT DES FONDS D'INVESTISSEMENT DU CANADA
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October 17, 2002

Ms. Denise Brosseau, Secretary
Commission des valeurs mobilières du Québec
800 Victoria Square, Stock Exchange Tower
P.O. Box 246, 22nd Floor
Montréal, Québec H4Z 1G3

Dear Ms. Brosseau:

Re: Notice of Proposed Amendments to National Instrument 81-102 and Companion Policy 81-102CP Mutual Funds and to National Instrument 81-101 Mutual Fund Prospectus Disclosure and Form 81-101F1 Contents of Simplified Prospectus and Form 81-101F2 Contents of Annual Information Form

Background

We are writing to you on behalf of The Investment Funds Institute of Canada's ("IFIC") Fund of Funds Working Group ("Working Group"). The Working Group was formed by IFIC's Regulatory Committee to comment on the recently released proposed amendments to mutual fund regulation. IFIC is the national association of the Canadian Investment Funds Industry, representing nearly 100% of the total mutual fund assets under management in Canada. IFIC's membership is comprised of fund managers, retail distributors and affiliates from the legal, accounting and other professions.

We appreciate this opportunity to comment on the proposed amendments to National Instrument 81-102 ("NI 81-102") and Companion Policy 81-102CP Mutual Funds ("NI 81-102CP") and to National Instrument 81-101 Mutual Fund Prospectus Disclosure ("NI 81-101") and Form 81-101F1 Contents of Simplified Prospectus ("81-101F1") and Form 81-101F2 Contents of Annual Information Form ("81-101F2").

We would like to preface our comments by stating that we are generally supportive of the CSA's proposed amendments and, in particular, the move toward permitting actively managed fund of funds structures. However, while we believe that the proposed amendments go a long way toward treating an investment in a bottom fund as merely "one of many potential investments that a portfolio adviser may make with the assets of a top fund", as described in the notice accompanying the publication of the draft amendments, we question certain of the conditions and restrictions which are imposed on funds of funds. Example of these conditions and restrictions include:

i) The requirement that a bottom fund be prospectus qualified in all the same jurisdictions as the top fund;

ii) The requirement that a bottom fund meet all of the requirements of NI 81-101 and NI 81-102;

iii) The restriction on a top fund from investing any percentage of its assets in bottom funds unless such an investment is specifically disclosed in the top fund's "Investment Objectives" section of its simplified prospectus ("SP"), thereby prohibiting a less fundamental investment in another mutual fund (for example, an investment of less than 10% of the net assets of a fund as is currently permitted under section 2.5 of NI 81-102);

iv) The prohibition against multi-tiered structures, other than RSP clone funds, in a marketplace in which many other comparable investments are available and acceptable under NI 81-102;

v) The prohibition against a bottom fund being permitted to charge a top fund an early redemption fee if the top fund redeems its securities within a specified period from the date of purchase;

vi) The prohibition against the flow of trail fees and other charges negotiated in an arm's length transaction even where such payments are duly disclosed to the investor; and

vii) The prohibition against a "duplication" of management fees.

We see these issues as being significant to the point that one could argue that the proposed amendments, taken as a whole, may even represent a step backwards in the CSA and the mutual fund industry's collective effort to develop a workable fund of funds regime to replace the current system which we wholeheartedly agree needs reforming.

A. <u>Response to "Specific Questions of the CSA Concerning the Fund of Funds Amendments"</u>

1. <u>Qualification of bottom fund in the local jurisdiction;</u> and
2. <u>Investments in funds other than those to which NI 81-101 and NI 81-102 apply</u>

We believe that the approach taken in the draft amendments with respect to these two issues is inconsistent with the principle that a mutual fund be considered one of many potential investments that could be made by a top fund. It is not currently a requirement under NI 81-102 that every issuer whose securities are purchased by a mutual fund be a "reporting issuer" in every jurisdiction in which the fund's securities are offered. Indeed, U.S. and international mutual funds hold primarily securities of issuers that are not "reporting issuers" anywhere in Canada. In fact, subject to the restrictions concerning illiquid assets, a traditional mutual fund is permitted to hold securities of an issuer that is not a "reporting issuer" or the equivalent anywhere in the world.

In our view, a top fund should be permitted to invest in any bottom fund that is subject, either by law or voluntarily through its constating documents, to NI 81-102 style investment restrictions designed to ensure diversification, relative safety in the nature of the underlying investments and liquidity. We can foresee, for example, a top fund portfolio adviser wishing to invest in a "niche" fund that is only offered by way of a SP qualified in one province. We can also foresee a mutual fund manager and portfolio adviser wishing to create a fund of funds using non-prospectus qualified "pooled" funds as bottom funds, because their management expense ratios tend to be lower than comparable prospectus qualified funds, or to access the expertise of portfolio managers who may not offer prospectus qualified retail funds. Accordingly, we submit that paragraph 2.5(1)(c) of the proposed amendments be amended to read:

> "The bottom fund or RSP clone fund (i) is qualified for distribution under a simplified prospectus in one or more of the jurisdictions in which the securities of the top fund are qualified for distribution, or (ii) if it has not qualified for distribution by simplified prospectus, it has adopted investment practices and restrictions and redemption features that comply with NI 81-102 were the bottom fund or RSP fund governed by NI 81-102"

We believe that adopting this type of approach in paragraph 2.5(1)(c) is both consistent with the level of mutual reliance CSA members should adopt in regulating mutual funds and addresses the goal of Part 2 of NI 81-102 in ensuring diversification, relative safety of investment and liquidity.

Top funds should be able to invest in pooled funds provided they are redeemable on demand. We believe that portfolio managers are qualified to assess the performance and portfolio holdings of such pooled investments and the historical track record of the portfolio manager of the pooled fund. Discretion should be left to the top fund's portfolio manager, acting in the best interests of the top fund, to assess the suitability of such pooled fund investments. The CSA should avoid micro-regulating on the basis of product structure (pooled funds versus prospectus qualified funds) and permit portfolio managers enhanced flexibility to do indirectly, what they can do directly, if they believe such actions are in the best interests of the funds that they manage.

Similarly, we believe that commodity pools that meet the requirements of NI 81-102 and NI 81-104 Commodity Pools should be permitted investments for a top fund.

3. Requirement to be a Top Fund and removing the existing 10% investment provision in section 2.5 of NI 81-102

The proposed amendments essentially require a fund to declare whether it will be a top fund or whether it will leave itself open to being a bottom fund. We do not see the logic in this policy. It is simply not in the best interests of a fund to have to make a choice between investing a percentage of its assets in another fund, which may be part of its strategy to achieve its objective (and be, in the opinion of the portfolio manager, the best possible investment available for that purpose) and preserving the status quo of being the potential bottom fund in which the portfolio manager of another fund (acting in the best interests of that other fund) may choose to invest. Forcing a fund manager to make this choice needlessly precludes a fund from attracting investments by other funds which, if permitted, could result in better diversification of the portfolio of the fund and lower per security fixed costs (as these costs would be spread out over a larger base). In this way, the investment in a fund by another fund should be treated like any other investment by an institutional investor. This proposal creates an unnecessary barrier to a manager's and portfolio manager's discharge of the standard of care they owe to their mutual funds.

Having an insignificant percentage of a fund's assets invested in another fund is not an investment objective of the fund; it is merely an investment strategy that the fund may use from time to time. Requiring the minor strategy of investing an insignificant percentage of a fund's assets in another fund to be disclosed in the fund's SP as a fundamental investment objective artificially elevates the status of an investment strategy to a fundamental investment objective. With these requirements, the proposed amendments demand a level of transparency that is not required of investments in other types of securities.

If a fund's investment in other funds is truly its investment objective, then that fact belongs in the fundamental investment objective. However, a fund manager should have the discretion to decide whether or not the fund's reliance on investments in other funds should be considered to be the fundamental investment objectives of the fund, or whether the investments in other funds can more appropriately be described as one of the fund's strategies that achieves its investment objective, in which case it should not be restricted in exercising this discretion by arbitrary limits.

If the CSA are unwilling to rely upon this distinction between fundamental investment objectives and less fundamental strategies, we submit that retaining a 10% threshold may be appropriate; a fund that wishes to invest less than 10% of its net assets in other funds from time to time as a minor strategy would be allowed to do without having to disclose this in its fundamental investment objectives.

Given the widespread use by mutual funds of small investments in other funds, the proposed amendments will have the effect of requiring a very large number of existing mutual funds to become "top funds" and to include the appropriate disclosure in the "Investment Objectives" sections of their SPs. We believe that this would be inappropriate and misleading disclosure and would diminish the value of the disclosure with respect to "true" fund of funds.

Multi-tiered Funds

We believe that multi-tiered funds should be permitted for all funds and not just for clone funds. We are aware of at least one mutual fund company that has been granted permission to offer a multi-tiered fund of funds. There are valid commercial reasons for offering multi-tiered funds. We believe that these types of structures should be permitted if the portfolio adviser decides that investing in these types of structures is in the best interests of the fund.

Again, provided one guards against the potential for abuse in the structure, we see no sound basis on which to preclude this practice, and thereby lessen the investment flexibility of portfolio managers. We fail to see why fund structures should not be permitted to evolve in a similar fashion to companies such as Power Corporation and Brascan, which are multi-tiered corporate structures, where it is appropriate to do so. Mutual funds will have the added benefit of liquidity because their securities are redeemable on demand at the option of the unitholder. Given the other safeguards, which are built into NI 81-102, we do not believe that this provides a sufficient point of distinction to warrant the prohibition of multi-tiered structures.

We believe that the CSA must define what constitutes a multi-tier fund of funds structure. We agree that it may be reasonable for the CSA to prevent a top fund (other than a RSP clone fund) from investing in a bottom fund whose <u>investment objective</u> is to invest in another mutual fund. However, we believe that there may be circumstances where a bottom fund may use fund of funds investments as part of its investment strategy to achieve its investment objective and that a broad, sweeping prohibition against multi-tiered structures eliminates potential investment opportunities to the detriment of the very investors the CSA seeks to protect. We understand that the CSA has considered this matter in the context of exemptive applications in the past and has supported such relief.

By clarifying what is meant by multi-tier structures and clarifying that this is not intended to include mutual funds that either wish to (i) use fund of funds to achieve a component of its investment strategy or (ii) preserve flexibility for potential future use of active fund of funds the CSA may be able to minimize the number of applications of this kind, which we understand is one of the CSA's objectives going forward.

4. <u>Control of bottom fund by the top fund</u>

i) <u>Removal of the concentration and control restrictions</u>

We are supportive of the proposal to remove the concentration and control restrictions and do not believe that there should be a limit on the percentage of the net assets invested in one bottom fund. The CSA's approach of using disclosure to give investors an adequate sense of their investment is the appropriate one.

ii) <u>Massive redemptions</u>

We are concerned about the recommendation of requiring "large redemption risk" disclosure to be included in the SP of each bottom fund. We believe that a top fund or clone fund that invests in assets of a bottom fund is like any other large investor investing assets in a fund. Accordingly, we do not believe that the risk of large redemptions is inherently greater in a fund of fund structure than in any other mutual fund that has a large investor.

Redemption risk is a fact of life for all mutual fund investors. Assessing risk and mandating disclosure requirements on the basis of the "type" of securityholder in a mutual fund has no merit. Mutual funds are not obligated to disclose "massive redemption risk" when institutional or high net worth investors invest in a fund. We believe a fund of funds investment, from a bottom fund's perspective, should be looked at in the same way as any other institutional holding. Furthermore the fact that a fund of funds relationship exists may not be material in the context of the fund's overall securityholder base; in other words, the fund of funds' holding may be small in relation to other holdings. Finally, a bottom fund may not be aware, in advance of its SP's release, who its investors are or will be during the year and we believe that mandating such disclosure may be misleading.

Furthermore, to the extent that fund managers would not want to exclude any of their funds from becoming a bottom fund, we believe that the proposed "large redemption risk" disclosure would become boilerplate language in virtually every mutual fund's SP, thereby significantly diminishing any potential value of the disclosure to investors.

5. <u>Prohibition against sales and redemption charges</u>

Disclosure is the cornerstone of the Canadian securities regulatory regime. We believe that it is reasonable to prohibit top funds from paying sales charges in connection with a purchase of securities of a bottom fund, and similarly reasonable to prohibit redemption fees from being charged for redemptions made by a top fund, where the funds and their respective managers are related. In an arm's length transaction, however, fund managers should be free to negotiate all charges and fees, including trail fees. This is, in effect, a commercial negotiation that should be permitted, provided the top fund meets the requisite disclosure requirements.

We believe that it would be a mistake for the CSA to take away a mutual fund manager's right to levy a short-term trading fee in circumstances where there is heavy switch activity or where a significant amount of units are redeemed within 90 days of purchase. This fee is payable to the respective fund as compensation for costs incurred including regulatory fees, processing costs, portfolio trading costs and other such costs to the fund and represents a tool that a fund manager may use to discourage short term trading in a bottom fund. This fee is applied for the benefit of the fund's remaining unitholders and it would be detrimental to the public interest to take away a fund manager's discretion to impose such a fee where circumstances warrant it. Fund managers have the ability to do this now and we fail to see why the CSA would consider restricting a manager's ability to protect a fund in a way that could ultimately hurt the investors in that fund.

6. <u>Voting rights of top fund securityholders in bottom fund matters</u>

In general, we support the proposal to remove the requirement to pass through bottom fund voting rights to top fund investors. In our experience, fund investors are passive investors who have not been active in exercising their voting rights and so there is little benefit in spending the time and expense that goes into holding a unitholder meeting.

7. Active management and prospectus disclosure

We believe that the CSA has adopted an appropriate approach to disclosure of a top fund's investments. Not requiring disclosure of a top fund's underlying investments (other than in the "Top Ten Holdings" section of a fund's SP) is consistent with the principle that a mutual fund is one of many potential investments that a portfolio adviser may make with a top fund's assets. We believe that it should be left to fund managers to determine whether a particular top fund's intention to invest in a particular bottom fund is a "material fact" requiring disclosure. For example, it may well be a material fact requiring prospectus disclosure if a top fund intends to invest 80% of its assets in one bottom fund. However, an investment in any one bottom fund is less likely to be a material fact if a portfolio adviser takes full advantage of the ability to actively manage bottom funds and each bottom fund represents a relatively small portion of the top fund's assets.

With respect to a requirement to notify investors of the replacement of one "important" bottom fund, we submit that the existing definition of "significant change" and the requirement under section 5.10 of NI 81-102 to file a material change report, press release and prospectus amendment in the event of a significant change are adequate tools to address this issue.

B. Other Issues Relating to the Fund of Funds Amendments

1. Requirement that any fund of funds investment be disclosed as a fundamental investment objective in the top fund's SP

Currently, a fund's investment in another fund may be disclosed as an investment strategy in the fund's SP. We believe that the proposed requirement that any investment in another fund must be disclosed as an investment objective in a top fund's SP is problematic from a fund administration perspective. This proposed requirement is likely to oblige the vast majority of funds currently using a fund of funds investment strategy to hold securityholder meetings to obtain approval for a change in the fund's fundamental investment objective and to amend the constating documents of the fund. We believe this artificial elevation of the fund of funds investment strategy does not warrant the cost associated with holding these meetings and the amending of the fund's documentation. These costs, which will be borne by the funds and indirectly by the unitholders, is an unavoidable consequence of this new disclosure obligation and is inconsistent with current disclosure requirements and industry practices. Accordingly, we would strongly urge the CSA to reconsider this disclosure requirement.

2. Financial arrangements

There are several issues relating to the financial arrangements contemplated by proposed section 2.5 of NI 81-102 on which we would like to comment.

Firstly, we believe there is an inconsistency between permitting top funds to actively manage their bottom fund holdings and the prohibition under proposed paragraph 2.5(1)(d) against the "duplication" of management fees. Under existing discretionary orders permitting the operation of "passive" fund of funds, the prohibition against duplication of management fees was appropriate given the limited role for the portfolio adviser at the top fund level. However, to the extent that a top fund's manager and portfolio adviser will now have a far greater role in actively managing the top fund's investments, we question whether it could ever be argued that there is truly a "duplication" of management fees.

In an actively managed fund of fund structure, there will now be two layers of management taking place. Particularly in respect of arm's length fund of fund structures, both layers of management add value to unitholders and, therefore, both layers of management should be compensated. In our view, it should be permissible for management fees to be charged at both the top fund and bottom fund levels, provided that top fund investors are given full disclosure of their total management costs. Given the highly competitive nature of the Canadian mutual fund industry, there will be significant commercial incentive for managers of a top fund to ensure that the total management costs of the top fund are not significantly higher than other mutual funds and to attempt to negotiate management fee rebates or reduced management fees from the managers of bottom funds.

Secondly, we would like to comment on proposed paragraphs 2.5(1)(g) and (h) of NI 81-102. As written, these paragraphs would prohibit certain existing, negotiated arrangements between top funds and their managers and bottom funds and their managers. Some top fund managers have negotiated both management fee rebates (which are typically payable by the bottom fund manager directly to the top fund and would, therefore, be permitted under proposed paragraph 2.5(1)(h)) and a form of "trailer" fee (which are typically payable by the bottom fund manager to the top fund manager and would be prohibited by both proposed paragraphs 2.5(1)(g) and (h)). The payment of trailer fees by a bottom fund manager to a top fund manager is, in effect, a mechanism to ensure that there is no duplication of management fees, as is required under existing exemptive relief and would be continued under subsection 2.5(1)(d).

A very significant proportion of management fees of any mutual fund are used to fund distribution costs, specifically trailer fees payable to mutual fund dealers and investment dealers. A bottom fund and its manager have no such distribution costs in respect of those securities of the bottom fund owned by a top fund, but the top fund manager does have such costs. Accordingly, the payment of trailer fees from the bottom fund manager to the top fund manager is an efficient way to redistribute this income and appropriately recognize the cost realities in the marketplace. Proposed paragraph 2.5(1)(g) would prohibit the payment of trailer fees to either the top fund or its manager and, even if these fees were recharacterized as a rebate of a portion of the bottom fund's management fees, proposed paragraph 2.5(1)(h) would prohibit these fees from being paid to the top fund manager. Accordingly, in order to fund its obligations to pay trailer fees, a top fund manager's management fee would need to be higher and, in some cases, would require the manager to seek unitholder approval for an increase. In the case of a bottom fund that does not offer I series or O series of its securities (which typically have a lower, negotiated management fee), proposed paragraph 2.5(1)(g) could result in a duplication of a portion of the management fees, the benefit of which would accrue to the bottom fund manager. We do not believe that the CSA intended this result.

On the basis of the foregoing, we would encourage the CSA to consider replacing proposed paragraphs 2.5(1)(d), (g) and (h) with provisions that would allow top fund managers and bottom fund managers maximum flexibility to negotiate their financial arrangements, provided that investors are always able to determine from the top fund's SP their total cost of investing.

3. Index participation units

We believe there are significant issues raised by the way in which index participation units (IPUs), which are securities of a mutual fund, would be treated under the proposed amendments. One IFIC member, Barclays Global Investors Canada Limited, has submitted to you a comment letter dated September 3, 2002, which includes a comprehensive discussion of those issues. We are similarly concerned that in drafting the proposed amendments, the CSA may have misunderstood both how portfolio advisers typically use IPUs and certain unique features of IPUs that suggest that they should not generally be dealt with as bottom funds for the purposes of NI 81-102. We fully support, but do not propose to reiterate, the discussion set out in the Barclays letter.

4. Future discretionary relief

As indicated at the outset of this letter, we believe the CSA does not truly treat mutual funds as simply one of a number of potential investments that could be made by a top fund and many of our above comments have been formulated in contemplation of that principle. While we recognize that the CSA may ultimately choose not to accept some of our recommendations, we expect that CSA staff will continue to accept applications for and, in appropriate circumstances, recommend applications for discretionary relief respecting these matters in the future.

5. Impact of the sunset provision

Similarly, while we appreciate the CSA's desire to have a common set of rules apply to all existing fund of fund arrangements, we submit that the result may not be appropriate. Certain funds have been structured based upon relief that they have received in the past.

Investors have acquired the securities of those funds on the strength of the features of the funds disclosed in their respective SPs and annual information forms. Accordingly, it would be prejudicial to the investors in those funds to simply eliminate the ability of those funds to invest in this manner going forward. We strongly recommend that for these instances, a grandfathering clause be written into the amended version of NI 81-102. Indeed, it may be appropriate to allow all funds to elect whether to continue to carry on its reliance upon their current relief or to rely upon the new amendments.

Not only do we believe that forcing sunset provisions has the potential to be prejudicial to a fund's existing unitholders, but in certain circumstances a fund's units may have been purchased as financed units under financing agreements with limited partnerships and other financing sources. Under these arrangements, fund companies may not have the legal right to change the way those units have been structured. The impact on the fund of funds relationship by not grandfathering could impact on a number of third party financing arrangements. We strongly recommend that for these instances, a grandfathering clause be written into the amended version of NI 81-102.

In any event, if the CSA decides to proceed with a general rule of having a sunset on the reliance upon the current relief, it should adopt a streamlined application process under which managers may apply to be exempted from the sunset provision in order to continue to rely upon some or all of the elements of the relief currently relied upon by the funds they manage. We suspect that, provided the other issues in this letter are addressed, the number of applications made on this basis would be fairly limited. Guidance could be given by the CSA on the general circumstances in which this relief would be granted in order to avoid an unnecessary number of applications.

C. <u>Other Matters</u>

We have the following comments on the other non-fund of funds related proposed amendments.

1. <u>Definition of RSP Clone Fund in Section 1.1 NI 81-102</u>

The "RSP Clone Fund" definition in the proposed amendments requires the fund to be "linked" to an underlying fund. There are several fund companies that have RSP clone funds that are either index funds or RSP clone funds that are based on the performance of a group of securities which may reflect the investments of the underlying fund, but it is not directly linked to the underlying fund in the same way. We would like to see the definition of "RSP Clone Funds" reflect this reality. We propose the following definition:

"RSP Clone Funds" means a top fund that has adopted a fundamental investment objectives to link its performance to the performance of a specified bottom fund or to the performance of a basket of securities which may reflect the investment of the bottom fund whose securities constitute foreign property for registered plans by using specified derivatives to ensure that the securities of the top fund will not constitute foreign property under the ITA"

2. <u>Subsection 5.1(a) NI 81-102</u>

We are concerned about the addition of the words "or directly to its securityholders" in this subsection. While we are uncertain what types of direct securityholder fees the CSA contemplated when drafting this proposed amendment, as written, this subsection is problematic for the following six reasons:

i) The mutual fund manager is not necessarily aware of all the fees paid by unitholders related to investing in the manager's funds. For example, the manager will not necessarily be aware of the fees that are negotiated directly between the broker/dealer and the investor hence the need for subsection 16.1(5) of NI 81-102, which includes the maximum non optional fees in MERs, when the actual fees are not known. By extension, even if the manager is aware of certain fees, they can not necessarily control fee changes. Fee changes could be initiated without the manager's knowledge, or even if a fee change is made with the manager's knowledge, it may be changed without the manager's approval. If early redemption fees, which are clearly disclosed in the fund's SP and not applicable to all unitholders, are increased on a prospective basis, then this increase should not be captured by this proposed provision;

ii) If an advisory fee is paid by some, but not all unitholders, do all unitholders have to vote on changing the fee? Likewise, if the fee is adjusted upwards for some, but not all unitholders that are subject to the fee, do all of unitholders have the right to vote on the fee change?;

iii) New fees may result from changes to NI 81-102 or other securities legislation, such as the requirement to hire a securities lending or repurchase agreement agent. In the case of securities lending, a manager may be reluctant to establish a program, even though it would prove to be beneficial to investors, because of the burden of an investor vote which is a result that is clearly not in the best interests of investors.

iv) If the manager waives a fee, or voluntarily charges less than the "up to" maximum as indicated in the SP, does a decision to discontinue waiving the fee constitute a "change in the calculation of the fee or expense" which results in more fees being paid by the unitholder?;

v) Who should pay for the high costs of holding meetings if unitholders were required to vote on all fee changes?; and

vi) Unlike part (i) of the subsection, part (ii) does not mention that the new fee "could result in an increase in charges". Perhaps the CSA thought it was implicit that a new fee would automatically result in an increase in charges payable by the securityholder. However, this is not necessarily the case. For example, a manager may decide to restructure its fees by reducing the management fees paid by each fund by 1% and charge all investors a 1% "advisory fee" at the client's account level. In this way the "advisory fee" gives the client a benefit because the advisory fee is tax deductible to the client and does not actually cost the client more than he/she would pay had the fees not been restructured. However, as worded, part (ii) would be deemed to be the "introduction" of a new fee.

3. Subsection 5.8(1.1) NI 81-102

We suggest clarifying this subsection by replacing "upon the occurrence of an offer" with "upon the occurrence of a bona fide offer" because an unscrupulous individual or company can potentially abuse the intention of this section if it remains as is. Requiring a mutual fund manager to provide the person or company who has simply made an offer with the records of the mutual fund may result in unitholders receiving several notices of offers and counteroffers making the public aware of what may be a ludicrous offer, which negatively effects the bargaining process.

4. Subsection 13.1(1.1) NI 81-102

We believe that the intent of this section is that valuation dates have to be on a consistent frequency and not that each valuation date has to be compatible. This becomes an issue because different jurisdictions have different holidays where markets and/or businesses are closed. We request clarification on this matter.

Conclusion

We applaud the CSA's efforts in opening up fund of fund rules to permit active fund management and eliminate yet another of the prescriptive rules that have unduly restricted the flexibility of portfolio managers. While we appreciate the effort and challenge in getting all CSA members to agree on a common set of rules, we are very concerned, as stated above, that certain aspects of the proposed amendments cause serious impediment to the use of fund of fund investments on either an "active" or "passive" basis, and therefore, need to be reconsidered.

We believe that the proposed amendments do not adhere to their stated principle that a mutual fund is one of many potential investments that a portfolio adviser may make with the assets of a top fund and so, as is written above, we recommend, among other things, that the following changes be made:

i) Allow a top fund to invest in mutual funds that are not qualified in all the same jurisdictions, or in any jurisdiction provided they are pooled funds which are managed subject to specified conditions which make them "NI 81-102 like", if the fund manager decides that that investment is in the best interests of the fund;

ii) Allow a top fund to invest in investments such as IPUs that are not subject to NI 81-101 and NI 81-102;

iii) Delineate between using fund of funds on an investment objective versus the more limited use as a strategy and allow funds to use fund of fund investing as a limited strategy (rather than as an investment objective) without deeming this fund to be a top fund;
iv) Allow multi-tiered fund of funds structures;
v) Allow a bottom to charge a top fund an early redemption fee if it is appropriate;
vi) Allow the flow of trails and other charges negotiated in an arm's length agreement where such payments are duly disclosed to investors; and
vii) Allow for the "duplication" of management fees where the duplication is in reality superficial because the unitholders of the top fund are receiving a service that would not otherwise be available to them without their investment in the top fund.

We thank you for this opportunity to comment on the proposed amendments. We would welcome and look forward to the opportunity to discuss these matters with you further. Please feel free to contact me by email at jmountain@ific.ca or by telephone at (416) 363-2150 x271 or Stacey Shein, Legal Counsel by email at sshein@ific.ca or by telephone at (416) 363-2150 x238 should you have any questions or if you require clarification about any of our comments.

Yours truly,

John Mountain
Vice President
Regulation