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June 13, 2003

DELIVERED

Alberta Securities Commission
Saskatchewan Financial Services Commission
The Manitoba Securities Commission
Ontario Securities Commission
Office of the Administrator, New Brunswick
Registrar of Securities, Prince Edward Island
Nova Scotia Securities Commission
Department of Government Services and Lands, Newfoundland and Labrador
Registrar of Securities, Northwest Territories
Registrar of Securities, Yukon
Registrar of Securities, Nunavut

c/o John Stevenson, Secretary
Ontario Securities Commission
20 Queen Street West
Suite 800, Box 55
Toronto, ON M5H 3S8

Dear Sirs/Mesdames:

Re: Response of Borden Ladner Gervais LLP to the Notice of Proposed Multilateral Instrument 55-103 and Companion Policy 55-103CP

This submission is in response to the Notice and Request for comment in respect of the proposed Multilateral Instrument 55-103 (the "Proposed Rule"), published February 28, 2003.

Our comments represent the views of some of the members of the Toronto Securities and Capital Markets Group of Borden Ladner Gervais LLP on the Proposed Rule. These comments do not necessarily reflect the opinions or feedback of all of our clients.

While we are in general agreement with the principles based approach to insider reporting put forward in the Proposed Rule, we are concerned that the tests set out in section 2.1 would require insiders of a reporting issuer to report trades of investment

funds[1] and other securities, whose economic, financial or pecuniary value is based in part, upon the pecuniary value of securities of his or her reporting issuer. In our view, public disclosure of these types of transactions falls outside the policy framework of the insider reporting obligations and should be exempt from the reporting requirements in the Proposed Rule. Additionally, insiders and their advisors could use greater guidance from the securities regulators with respect to the materiality threshold which has been incorporated into subsection 2.2(a).

Investment Funds

A trade by an insider of a reporting issuer in securities of an investment fund that holds securities of his or her reporting issuer is technically captured by subsections 2.1(a) and (b) of the Proposed Rule and would be a reportable transaction.

An investment fund's value is closely aligned with the trading price of its portfolio securities. If an insider holds securities in an investment fund, which in turn holds securities of the insider's reporting issuer, any trade by the insider in securities of this investment fund would be captured by the "economic exposure test" set out in paragraph 2.1(a)(i) of the Proposed Rule. Where an insider holding securities of an investment fund receives a pecuniary return, i.e., a distribution or dividend from the fund, which is derived in part from securities of his or her reporting issuer which are held in the fund's portfolio, trades in such funds would also be captured by the "economic interest test" set out in paragraph 2.1(a)(ii) of the Proposed Rule.

We would submit that generally insiders trading in securities of an investment fund, which holds securities of the insider's reporting issuers, should not be subject to insider reporting requirements. Presumably this is consistent with the intent of subsection 2.2(a) of the Proposed Rule and an exemption to this effect should be included.

The vast majority of investment funds are structured in such a way that an insider who holds securities in an investment fund is not able to avail himself or herself of the exemptions in section 2.2 of the Proposed Rule and, where securities of the insider's reporting issuer form part of an investment fund's portfolio, the issuer could arguably be subject to a reporting requirement in accordance with section 2.1. An investment fund that holds securities of a reporting issuer will always "involve directly or indirectly, a security of the reporting issuer" as set forth in subsection 2.2(a). Only a limited number of investment funds are likely to fall within the definition of "derivative" included in the Proposed Rule, i.e., Exchange Traded Funds, and thereby be included within the exemption. For example, if securities of the reporting issuer were not a material component of the underlying interest, benchmark or formula, an insider trading in these funds could rely on the exemption in subsection 2.2(a) of the Proposed Rule.

The Proposed Rule must balance the rights of an insider to trade in securities privately, without public disclosure, along with the rights of the public to have full disclosure of all trading activities by an insider in securities of his or her reporting issuer. Thus, another

[1] All references to investment funds should be read to include mutual funds, non-redeemable investment funds and other pooled funds.

issue to consider is whether trades by insiders in securities of investment funds should be subject to reporting requirements despite the fact that securities of the insider's reporting issuer may form a material component of the fund's securities portfolio.

If securities of an insider's reporting issuer form a material component of a passively managed investment fund, i.e. an index fund or ETF, the policy rationale for making trades by an insider in such funds reportable is clear; an insider can be reasonably certain that the underlying securities which form part of an index will remain relatively constant over a given period of time and where securities of his or her reporting issuer are a material component of the index, the insider could use the index as an indirect means of trading in securities of his or her reporting issuer. However, in the case of an actively managed fund, even one where securities of an insider's reporting issuer form a material component of the fund's portfolio, it is difficult to understand why trades in such funds by insiders should be subject to reporting requirements. There should not be any concern that an insider who invests in a fund, provided he or she has no investment control over the fund's portfolio, would be engaged in a transaction similar to insider trading that should be transparent to the market. If a fund's investments can be increased or decreased, even fully divested, without the insider's knowledge or consent, it is difficult to see how the investing public is served by knowledge that an insider has traded in securities of such a fund. Moreover, from the perspective of an insider, compliance with such a reporting requirement would be extremely difficult since the insider frequently has no knowledge until months after a trade takes place that securities of his or her reporting issuer have become or have ceased to be a material component of a fund's portfolio.

In this regard, we note that the Companion Policy to the Proposed Rule makes reference to the *Securities Exchange Act of 1934*, s. 16a-1(2) ("SEC Rules") as the inspiration for the "economic exposure test" set out in section 2 of the Proposed Rule, but the Proposed Rule does not incorporate some of the important exemptions to the SEC Rules; namely, s. 16a-1(a), the relevant portion of which provides:

> (5) the following interests are deemed not to confer beneficial ownership for the purposes of section 16 of the Act:
>
> (ii) Interests in portfolio securities held by any investment company registered under the Investment Company Act of 1940, and
>
> (iii)Interests in securities comprising part of a broad-based, publicly traded market basket or index of stocks, approved for trading by the appropriate federal governmental authority

Interestingly these exemptions exclude all trades by insiders in investment funds and do not contain the materiality component incorporated into subsection 2.2(a) of the Proposed Rule.

If a similar exemption were included in the Proposed Rule, the following exemption language could be incorporated into section 2.2:

> "a trade in a security of an investment fund"

Alternatively, if the materiality threshold were to be included in the exemption for passively managed investment funds, the definitions of an "index mutual fund" and "index participation unit" in National Instrument 81-102 – *Mutual Fund Distributions* could be incorporated into the Proposed Rule and the following might be appropriate:

> "a trade in a security of an investment fund, provided that if the fund is an index mutual fund or issues index participation units, securities of the reporting issuer do not form a material component of such investment fund's economic, financial or pecuniary value."

Other Securities – Holding Companies, Limited Partnerships, etc.

As discussed above, it is our submission that the Proposed Rule should not require insiders to report trades in securities of actively managed investment funds. Similarly, where an insider trades in securities of an issuer that holds, as part of its investment portfolio, securities of the insider's reporting issuer, then provided the insider is not a controlling shareholder of the issuer and does not have or share control of the investment portfolio, such trades should not be subject to the insider reporting requirements for the same reasons given above. The SEC Rules contain a similar exemption in s. 16a-1(a)(2)(iii) which provides:

> A shareholder shall not be deemed to have a pecuniary interest in the portfolio securities held by a corporation or similar entity in which the person owns securities if the shareholder is not a controlling shareholder of the entity and does not have or share control over the entity's investment portfolio securities.

If a similar exemption were included in the Proposed Rule, the following exemption language could be incorporated into section 2.2:

> "a trade in security of an issuer, which holds directly or indirectly securities of the reporting issuer, provided:
>
> (i) the insider is not a controlling securityholder of the issuer; and
>
> (ii) the insider does not have or share investment control over the securities of the reporting issuer."

This proposed exemption would also be broad enough to encompass investment funds, and therefore, if adopted, would make the exemptions for investment funds, above, redundant.

If the materiality threshold for passively managed investment funds were to included in the exemption, the following might be appropriate:

> "a trade in a security of an issuer, which holds directly or indirectly securities of the reporting issuer, provided:
>
> (i) the insider is not a controlling securityholder of the issuer; and

(ii) the insider does not have or share investment control over the securities of the reporting issuer; and

(iii)if the issuer is an index mutual fund or issues index participation units, securities of the reporting issuer do not form a material component of such issuer's economic, financial or pecuniary value."

Materiality

Companion Policy 55-103CP (the "Companion Policy") states that the reference to "material component" in subsection 2.2(a) of the Proposed Rule should be interpreted using similar considerations to those involved in the concepts of "material fact" and "material change". Accordingly, a "material component" should reasonably be expected to have a significant effect on the market price or value of the derivative at issue.

As mentioned previously, the inclusion of a materiality threshold does raise some concern for insiders and their advisors since the information needed to ascertain whether or not such threshold has been met is frequently unavailable on a timely basis. This is not necessarily the case with derivative transactions, which should generally be more transparent since the underlying security, formula or benchmark is fixed, but if such a test were applied to actively managed investment funds or other securities, securities of the insider's reporting issuer might comprise a small percentage of the fund's portfolio one day and a much larger percentage on another. Moreover, some funds restrict themselves to a very small universe of securities and they may place large bets on a particular security at any given time, such that one security might comprise 10% or more of the funds portfolio.

Notwithstanding the interests of securities regulators in moving towards a more principles based approach to securities regulation, some guidance with respect to the percentage of securities in a securities portfolio, benchmark index, etc. which the regulators would consider to satisfy the materiality threshold would be appreciated. In this context, one might consider paragraph (c) of definition of "distribution" in section 1.1 of the *Securities Act* (Ontario) which states that any holding of "more than 20% of the outstanding voting securities of an issuer shall, in the absence of evidence to the contrary, be deemed to affect materially the control of that issuer." If a similar threshold were used for materiality, the following language might be inserted in Part 2 of the Companion Policy at item 6 after the last sentence:

> "Generally, if securities of the reporting issuer comprise more than 20% of the economic, financial or pecuniary value of an issuer, such securities should be considered a material component of the issuer's economic, financial or pecuniary value. In the case of an agreement, arrangement or understanding that involves a derivative, if securities of the reporting issuer comprise more than 20% of the economic, financial or pecuniary value of the underlying interest, benchmark or formula, such securities should be considered a material component of the underlying interest."

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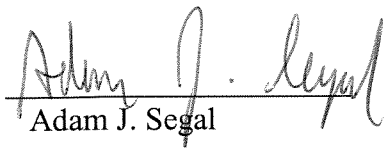
On an unrelated note, the Notice which accompanied the Proposed Rule stated that the CSA would publish examples of various types of monetization arrangements, together with examples of completed forms for such arrangements, on or before the time the Proposed Rule takes effect. In future, we would respectfully suggest that such information accompany the Notice and Proposed Rule so that users can provide comments, if any, before publication of the final rule.

Thank you for permitting us to comment on the Proposed Rule and Companion Policy. Should you wish to discuss our submissions further, please do not hesitate to contact us.

Yours very truly,

BORDEN LADNER GERVAIS LLP

Per: 
Adam J. Segal

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