Mackenzie
MUTUAL FUNDS

BY ELECTRONIC MAIL

May 2, 2004

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Re: Proposed National Instrument 81-107 – Independent Review Committee for Mutual Funds

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Mackenzie Financial Corporation ("Mackenzie") appreciates the opportunity to submit its comments to the Request for Comment on Proposed National Instrument 81-107 – Independent Review Committee for Mutual Funds ("NI 81-107"). Mackenzie fully supports the proposal of the Canadian Securities Administrators ("CSA") to require the appointment of an independent review committee ("IRC") for mutual funds.

We believe that the proposal for an IRC, which would focus on conflicts of interest, is a welcome step forward for mutual fund investors. We believe that allowing a group of independent individuals to focus solely on conflicts of interest will increase the scrutiny in and around conflicts of interest in the industry and result in tangible improvements in the oversight of mutual funds in Canada.

A. Introduction

Mackenzie currently offers 143 mutual funds (the "Funds") to the public. Mackenzie manages approximately $40 billion in assets for more than 1 million Canadian investors. The Funds are sold through more than 37,000 independent financial advisors across Canada. Mackenzie is a wholly-owned subsidiary of Investors Group Inc. and is part of the Power Corporation group of companies.

Mackenzie has had extensive experience with boards of directors within the Mackenzie group of companies. Prior to 2001, Mackenzie was a public company with a board of directors comprised of a majority of independent directors. Subsequent to the takeover bid for Mackenzie by Investors Group Inc., Mackenzie retained an independent board of directors. Currently, Mackenzie's board of directors consists of 6 independent directors and 2 members of management. Mackenzie's wholly-owned trust company, M.R.S. Trust Company, also has a board comprised of a majority of independent directors. Prior to its sale, Mackenzie owned a U.S. investment management company, Mackenzie Investment Management Inc. ("MIMI"). It was a public company with a board comprised of a majority of independent directors.

In addition to independent corporate boards, Mackenzie has had experience with mutual fund boards of directors in Canada and in the United States. In the United States, the Ivy Funds managed by MIMI and offered to the public were governed by a fund board of directors which was comprised of a majority of independent directors in accordance with the rules of the Securities and Exchange Commission. In Canada, when Mackenzie acquired the Cundill Funds in 1998, the Cundill Funds were governed by a board of governors. The board of governors for the Cundill Funds still exists today.

Lastly, Mackenzie created an Independent Review Committee relating to holdings in its Funds of related companies within the Power Corporation group of companies. This Committee is comprised entirely of independent members. This Committee was created pursuant to relief granted by the CSA on July 26, 2002 (and subsequently amended) to address the conflicts of interest inherent in the Funds continuing to own, purchase and sell securities of companies within the Power Corporation group of companies (excluding Investors Group Inc.).

Our experience in working with three independent fund boards and several corporate boards within the Mackenzie group of companies has shaped our views as set out in this letter.

B. Current Structure

Currently, the independent board of directors of Mackenzie oversees and reviews all aspects of the management of the Funds. The Mackenzie board of directors reviews all prospectuses for new and existing Funds, the financial statements for all Funds, information circulars for any changes to the Funds including fund mergers, changes in structure, fund performance, sales and marketing issues, in addition to matters relating to Mackenzie as a corporation.

The Mackenzie board of directors has a Regulatory, Compliance and Ethics Committee ("RCE Committee") comprised of six independent directors. The RCE Committee reviews and approves all compliance policies and any matters having a regulatory or legal impact. It also reviews matters that could involve conflicts of interest issues such as related party transactions and personal trading policies relating to access persons.

The Mackenzie board and the RCE Committee meet frequently in order to address Mackenzie Fund issues. The meetings are lengthy and detailed. The Mackenzie board asks in-depth questions about the Funds, management of the Funds and conflicts of interest. It is asked to review a high volume of printed materials which are required to be approved in accordance with laws, regulations and policies which govern mutual funds. These materials include simplified prospectuses for each family of Funds, fund financial statements for all 143 Funds, approval of all changes to any Fund, etc. This workload is extensive and time consuming.

In contrast, the mandate of the Independent Review Committee created to oversee the Fund holdings in related companies focuses solely on purchases, sales and holdings of related party securities and conflicts of interest related to those holdings.

In our experience, even a highly skilled and highly technical board of directors, such as Mackenzie's current board, does not have sufficient time to devote to the numerous conflicts of interest inherent in the management of mutual funds. Based on the number of meetings that Mackenzie's current board and committees have and the workload that they experience, we strongly believe that a separate and independent fund board (known as

an IRC in NI 81-107) to address conflicts of interest alone would well serve mutual fund investors in Canada.

We believe that our experience applies whether a board of directors is dealing with a large fund complex such as Mackenzie or a smaller complex. There are just too many distractions, in terms of workload and issues, for a board that has a broad mandate. A fund board or IRC with conflicts of interest as its paramount mandate will by its very nature have the ability to focus in on the very issues that are most important to investors.

We urge the CSA to consider the practical realities of the mutual fund world and not to bow to pressure and comments that a broader mandate would serve investors better. A fund board of directors with a very broad mandate is not a panacea. While it may seem intuitive that a group of independent individuals with a very broad mandate may be more effective in protecting investor interests, we do not believe that is true based on our own extensive experience with boards and managing the Funds. It is trite to point out that the U.S. experience relating to late trading and market timing was not prevented by fund boards with very broad mandates. Our own experience with a U.S. fund board simply highlights that U.S. fund boards receive standard agendas and review mounds of written materials required to be approved by fund boards by regulation.

C. Comments on NI 81-107

We have some general and specific comments on various aspects of NI 81-107. Our comments are set out below.

Section 1.3 – Multiple Class Mutual Funds

This section says that separate classes or series of multiple class mutual funds should be considered to be a separate mutual fund. It references the separate mutual funds by reference to their respective fundamental investment objectives. While this may work in a corporate context, it is not correct in the context of different classes of the same fund that is a trust.

Section 1.3 of National Instrument 81-102 (“NI 81-102”) looks to the underlying portfolio of assets as the source for determining each separate mutual fund in a multiple class context. This is consistent with the standard approach that has always been followed in determining what constitutes a mutual fund. As a result, NI 81-107 differs from NI 81-102 in this regard and we would suggest that the regulators look to adopting the approach set out in NI 81-102.

Section 2.2 – Initial Appointment

NI 81-107 proposes that a fund manager appoint the first members of the IRC. We believe that this is a practical approach. NI 81-107 further proposes that subsequent members be appointed by the other members of the IRC. We believe that the manager should be involved in the appointment and replacement of members the IRC. Mackenzie's experience with Canadian and U.S. fund boards is consistent. Fund board members tend to appoint friends and other like-minded individuals. They tend to have similar views and come from similar backgrounds. Over time, this can lead to an entrenchment mentality and a confrontational relationship with the manager.

We strongly believe that there should be a balance of different types of skills in persons on the IRC. In order to accomplish this, we believe that there should be a balance between the IRC and the manager as to replacement members. New members should be appointed jointly by the IRC and the manager. A new member that is not acceptable to one party or the other should not be appointed. It is critical to the reputation and integrity of the manager that effective IRC members be appointed. In addition, we believe that fund manager involvement in recruiting along with the participation of the IRC will ensure higher quality directors and oversight for mutual funds in Canada.

Further, we do not believe that a member of an IRC should be able to sit as a member of an IRC of another fund complex. This raises disturbing confidentiality and privacy issues as well as conflict of interest issues. At Mackenzie, we feel particularly strong about this issue due to the innovative nature of the products that we often bring to market.

Section 2.3 – Composition, Term of Office and Vacancies

This section permits the term of office for a member of the IRC to be not less than 2 years and not more than 5 years. However, in the commentary, the CSA states that the IRC can re-appoint members or limit the number of terms that a member may serve. We would suggest that a different approach be taken. We would suggest that a maximum number of years for service be set – NI 81-107 should state that the term should be between 2 and 5 years but that the maximum number of years that can be served by any one director should not exceed 10 years.

Our experience with both U.S. and Canadian fund boards are that board members, if left to their own devices, will sit for as long as they possibly

can. After a certain amount of time board members who have worked together can become entrenched both in their viewpoints and their desire to stay on as fund directors. In the U.S., Mackenzie inherited Fund directors on acquisitions who had been on Fund boards since the 1940s and in Canada for more than 25 years. This is clearly contrary to governance best practices.

Section 2.4 - Independence

NI 81-107 suggests that all IRC members be independent of the manager. We urge the CSA to allow for the inclusion of a minority of IRC members who are not independent of management. In the case of the Board of Directors of Mackenzie, 2 of 8 directors are members of management. On the board of directors of M.R.S. Trust Company 4 of 10 are members of management.

We believe that the interests of the manager should be represented on these boards. We believe that more effective decisions will be made with a management representative as a full participating member of the IRC. Discussions that are held in camera without management will not allow the manager to bring its views to the discussion at the time that they are relevant.

We do not believe that the IRC will be precluded from coming to an impartial view on conflicts of interest where a majority of members of the IRC are independent and a minority of members are not. The manager has a deep and abiding interest in the funds. It created the funds, it provided the investment to start the funds, it manages the funds, and has many obligations to the funds. It is unfair to disenfranchise the manager completely. Moreover, it deprives the funds of the benefit of manager experience as decisions affecting the funds are being made. Also, by heightening the liability of some members of management to consider conflicts of interest, those members will have an innate interest in ensuring that conflict issues are raised to the IRC and are considered first by the manager.

We refer you to the ICI Advisory Group for Fund Directors in their 1999 publication, *Best Practices for Fund Directors*. On page 11 of that report under the discussion of best practices, the following quote is relevant:

> Suggestions have been made that Fund Boards should be composed exclusively of independent directors. While the Advisory Group recognizes that some funds may find a Board consisting of only independent directors to be most suitable under their particular

> circumstances, as a general matter, the Advisory Group believes that Fund Boards can benefit from having affiliated directors on the Board. Board membership by representatives of the adviser allows for more direct accountability on the adviser's part and a better exchange of information with the adviser. In addition, representatives of the adviser may have greater expertise in many aspects of the operations of the fund. Thus, their participation may enhance the Board's effectiveness. Finally, as noted above, affiliated directors are subject to the same fiduciary standards as independent directors.

Further, we do not believe that the inclusion of members of management on the IRC is any different from the corporate world where best practices permit non-independent persons to sit on boards of directors. We refer you to the Corporate Governance Guidelines for Building High Performance Boards published by the Canadian Coalition for Good Governance (the "CCGG"). Guideline 3 states that, at a minimum, a board of directors should have a majority of directors, which are independent of management and have no material relationship with the company. However, even under the best practices guideline the CCGG recommends that the board membership be comprised of two-thirds of independent directors. In other words, even best practices in Canadian corporate governance circles would allow one-third of the directors on a corporate board to be non-independent.

The CSA has chosen to use a high level definition of independence which is generally accepted in corporate governance theory. However, we have found that boards of directors which use this definition tend to make a judgment that certain types of relationships might not interfere with the exercise of their independent judgment. As a result, in more recent years Mackenzie has tended to adopt more specific independence guidelines and would urge the CSA to consider them in addition to the broad standard of independence. We enclose our definition of independence plus suggested guidelines relating to independence as Schedule "A" to this letter.

In addition, we would point out that the definition of independence set out in NI 81-107 does not appear to preclude a direct or indirect material relationship with an investment advisor to funds or any other significant supplier to funds. We urge the CSA to include this in its definition of independence.

The definition of "independence" would also not allow independent directors who were previously independent directors of a manager to sit on

the IRC. The result of this would be to preclude very effective independent directors who understand and know the mutual fund business from sitting on the IRC. Mackenzie specifically recruited new independent directors to its Board within the last two years in order to give them Fund experience in anticipation of Mackenzie creating a fund board of directors across all of its Funds when the CSA published its fund governance concept proposal.

As a result, under NI 81-107 as it currently stands, all of the initial members of an IRC will, in all likelihood, not have had any direct mutual fund experience. We believe that IRCs would benefit from previous experience at their inception. We believe that an IRC comprised of members with no prior experience will take a significant amount of time to become effective and to appreciate the more complex conflicts of interest issues that fund companies face. We believe that more experienced IRC members would be able to provide leadership and guidance to less experienced members until such time as the less experienced members have developed the experience necessary to be as effective as possible.

Section 2.7 – Authority

This section allows the IRC to set its own compensation. This ability creates a conflict of interest between the personal interests of the members of the IRC and the funds that they are appointed to oversee and protect. We believe that the compensation of IRC members should be set jointly by the manager and the IRC. Both have a conflict of interest, but in this case, the manager actually has less of a conflict.

Mackenzie has had experience with independent fund board members who point to U.S.-style fund board compensation as the direction that a Canadian fund board's compensation should travel, with little regard to the differences in the Canadian compensation system for corporate directors. In a recent Wall Street Journal article "Directors Take, Don't Always Invest" by Ian MacDonald, a statement is made that the median salary of fund directors at the U.S.'s 50 largest fund boards is U.S. $128,000 plus expenses for travel, accommodation, meals etc. This salary is greater than most mutual fund executives are paid in Canada for doing a full-time job. By contrast, at the largest public companies in Canada (including the banks), the median compensation is far less than for U.S. fund boards or corporate boards. According to a report by Patrick O'Callaghan & Associates entitled "Corporate Board Governance and Directors Compensation in Canada – A Review of 2002", the average annual retainer for a corporate director in Canada in 2002 was $17,044 plus an average per meeting fee of $1,738. Again, a balance of interests relating

to compensation of IRC members is crucial for fairness to the fund investors that the IRC serves.

We would also suggest that the CSA consider giving specific relief in NI 81-107 relating to charging mutual funds for the costs of an IRC. As it stands now, fund managers would be obliged to call investor meetings to approve the increase in fees to mutual funds associated with creating the IRC and charging IRC-related expenses to the funds.

Section 2.8 – Liability

Mackenzie believes that liability for IRC members should be limited as long as the meet their standard of care. Unlimited liability in a fund complex such as Mackenzie's (with $40 billion in assets) is unfair and unwarranted.

Further, we have had recent experience with obtaining insurance for fund board members and would agree that it is becoming more and more difficult in the current environment to find insurance and appropriate coverage. However, we would expect insurance companies to understand the potential for business in this area and to find a way to service mutual fund companies who often have many other needs for insurance within their complex.

Section 2.10 – Ceasing to be a Member

We would suggest that IRC members should also cease to be a member if they are subject to regulatory or criminal sanctions. This is crucial to the integrity of the IRC and the manager.

Section 2.11 – Disclosure

We do not object to the disclosure required under this section. However, we would appreciate it if you could make it clear that when IRC members change, it would not trigger an amendment to all Fund prospectuses. Fees charged for changes to Part A of the simplified prospectus appear to be charged in many jurisdictions as if it is a change to every fund in the prospectus which can be prohibitively expensive. We would suggest that an updated list of members be included on the websites of the managers instead and that in the annual renewal, the names be republished.

Section 3.1 – Conflicts of Interest

As stated earlier, Mackenzie supports the referral of conflicts of interest to the IRC. However, we would suggest that more guidance be given in

NI 81-107 on the conflicts of interest to be referred to the IRC. In particular, we suggest that NI 81-107 refer to "material" conflicts of interest. A definition of "material" could also be incorporated. This would allow for sufficient focus and discussions of conflict issues of importance to the Funds and would assist in avoiding lengthy checklists and standard reports which seem to hamper existing fund boards.

In addition, we suggest that NI 81-107 make greater reference to the manager having policies in place which are approved by the IRC in order to address conflicts of interest. We would envision the IRC approving such policies and receiving regular reporting on compliance with those policies, including material exceptions to those policies (or an ongoing pattern of immaterial exceptions that could point to internal control issues). We also see managers referring non-standard conflicts of interest that often cannot be addressed simply by policies because they might occur infrequently or just once.

Section 3.2 – Changes to the Mutual Fund

We are struggling with the concept that all changes to investment objectives of a fund or fund mergers are inherently conflicts of interest. Very often these changes are of a routine nature. Under the proposed regime, these changes would have to be brought both to the manager's board and the IRC for approval. We think it should be clear that these NI 81-107 provisions should only apply where the changes constitute a conflict of interest. Simple examples of changes that would not be conflicts include the addition of a new type of security to a fund mandate (such as income trusts more recently), and a change in the economic environment which necessitates a change in the fund – i.e. the recent impact of the markets on technology funds. These are simply prudent changes to make and as long as the manager and its board of directors determines that they are in the best interests of the funds and calls meetings to approve the changes, we do not see the value in referring these matters to the IRC.

Section 3.3 – Inter-Fund Trades

Rather than reviewing specific inter-fund trades, we would suggest that the IRC adopt policies and that the IRC receive regular reports on inter-fund trading including material exceptions to the policies. Obtaining approval for each inter-fund trade would be impractical and make this relief ineffective.

In addition, we do not understand why inter-fund trades should be restricted to a particular fund family. In the Mackenzie complex, we have

six Fund families. It is not clear why trades cannot take place amongst fund families considering that they are usually only created with branding and investment style in mind and with no other functional distinction.

Section 3.4 – Supporting Information

This section allows the IRC to direct the manager to convene a special meeting of investors in certain situations. We believe that this section should give greater guidance to the IRC. For example, the IRC should only refer material issues to investor meetings and before making such a decision should take into account the absolute costs of calling and holding those meetings, either where the costs are to be borne by the funds or the manager. It is easy to envisage an IRC that is nervous about its own liability and feels that it can take greater comfort where a meeting of investors has been called to approve an issue. There should be checks and balances in place to address this concern.

D. CONCLUSION

Again, we thank you for the opportunity to submit Mackenzie's comments on NI 81-107. We would be pleased to meet with representatives of the CSA at any time to discuss further Mackenzie's own experience with fund and corporate boards and why we feel strongly that the proposed model will work well for investors in Canadian mutual funds.

Yours very truly,

MACKENZIE FINANCIAL CORPORATION

"W. Sian B. Brown"

W. Sian B. Brown
Senior Vice-President, General Counsel and Secretary

c.c. James Hunter, President and Chief Executive Officer
Mackenzie Financial Corporation

SCHEDULE "A"

INDEPENDENCE GUIDELINES

> "An independent director is independent of management and is free from any interest and any business or other relationship which could, or could reasonably be perceived to, materially interfere with the director's ability to act in the best interests of the corporation, other than the director's interests and relationships arising from being a shareholder."

Using that definition as a starting point, guidelines are required to indicate which relationships would disqualify a director from being independent. We have reviewed current corporate governance practices in this regard and have written them to apply to mutual fund governance structures. The Independent Review Committee proposes the following tests:

1. An Independent Director is a director who is not currently employed by Mackenzie Financial Corporation or any of its affiliate or subsidiary companies or by any investment advisors or their affiliate or subsidiary companies;

2. An Independent Director is a director who, in the past three years, has not been employed by Mackenzie Financial Corporation or any of its affiliate or subsidiary companies or by any investment advisors or their affiliate or subsidiary companies;

3. An Independent Director is a director who does not have a material business relationship or is affiliated with:
    - Mackenzie or any of its affiliated or subsidiary companies;
    - Any of the Funds managed by Mackenzie
    - Any investment advisors to the Funds
    - An employee of any of the above-mentioned entities
    - Any other significant supplier to the Funds

4. An Independent Director is a director who, in the past three years, has not had a material business relationship with:
    - Mackenzie or any of its affiliate or subsidiary companies;
    - Any of the Funds managed by Mackenzie
    - Any investment advisors to the Funds
    - An employee of any of the above-mentioned entities
    - Any other significant supplier to the Funds

5. An Independent Director is a director who has no personal or material financial ties to:
    - Mackenzie or any of its affiliate or subsidiary companies;
    - The Cundill Funds (other than ownership of units of the Funds)
    - Any investment advisors to the Funds
    - An employee of any of the above-mentioned entities
    - Any other significant supplier to the Funds

6. An Independent Director is a director who has no close family ties to:
    - Mackenzie or any of its affiliate or subsidiary companies;
    - The Cundill Funds (other than ownership of units of the Funds)
    - Any investment advisors to the Funds
    - An employee of any of the above-mentioned entities
    - Any other significant supplier to the Funds

7. An Independent Director is a director who has not served on the board continuously for a period of ten years.