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BARRISTERS AND SOLICITORS

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July 27, 2004

BY ELECTRONIC MAIL

British Columbia Securities Commission
Alberta Securities Commission
Saskatchewan Securities Commission
Manitoba Securities Commission
Commission des valeurs mobilières du Québec
Ontario Securities Commission
Authorité des marches financiers Office of the Administrator, New Brunswick
Registrar of Securities, Prince Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
Registrar of Securities, Northwest Territories
Registrar of Securities, Yukon Territory
Registrar of Securities, Nunavut

c/o John Stevenson, Secretary
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Dear Sirs/Mesdames:

Re: Proposed National Instrument 81-106 – Investment Funds Continuous Disclosure

We are counsel to the following investment funds:

(i) GrowthWorks WV Canadian Fund Inc. (“GWCF”),

(ii) GrowthWorks WV Opportunity Fund Inc. (“GWOF”)

(iii) Working Opportunity Fund (EVCC) Ltd. (“WOF”),

(together the “Funds”) (GWCF and GWOF are the “GrowthWorks WV Funds”)

We are writing on behalf of the GrowthWorks Funds to provide comments on Proposed National Instrument 81-106 (“NI 81-106”). Our clients appreciate the opportunity to provide input on this regulatory process.

BACKGROUND

GWCF is a labour-sponsored venture capital corporation registered under the *Income Tax Act* (Canada) and the *Equity Tax Credit Act* (Nova Scotia). It is also a labour-sponsored investment fund corporation registered under the *Community Small Business Investment Funds Act* (Ontario), and an approved fund under the *Labour-sponsored Venture Capital Corporations Act* (Saskatchewan). GWCF offers its securities in all provinces and territories of Canada (except British Columbia).

GWOF is a labour-sponsored investment fund corporation registered under the *Community Small Business Investment Funds Act* (Ontario) and is a prescribed labour sponsored fund under the *Income Tax Act* (Canada). GWOF offers its securities only in Ontario.

WOF is an employee venture capital corporation ("EVCC") registered under the *Employee Investment Act* (British Columbia) and is a prescribed labour sponsored venture capital corporation under the *Income Tax Act* (Canada). WOF offers its securities only in British Columbia.

Each of the Funds is managed by an affiliate of Growth Works Ltd. (together the "GrowthWorks the "GrowthWorks group of companies"). He GrowthWorks group of companies is the second largest independent manager of labour-sponsored investment funds ("LSIFs") in Canada with approximately $750 million in assets under management.

While the distinctions between LSIFs and traditional mutual funds have been previously described in detail in submissions regarding NI 81-106 by the Association of Labour Sponsored Investment Funds ("ALSIF") and ourselves, we believe it is important to highlight the following critical differences:

- *The Goal of the LSIF Program* - In the late 1980's and early 1990's, the federal government and the governments of Ontario and British Columbia recognized that traditional capital markets were not providing sufficient venture capital for small and medium sized (mostly private) businesses in Canada. The LSIF program was created as a special public/private investment vehicle to encourage greater risk capital investment in small and medium size businesses to fill this void and foster new business formation and stimulate economic development. The program has been successful in targeting investor capital into and financing small and medium size businesses. To date, WOF alone has invested in 100 small businesses in BC and the GrowthWorks WV Funds have invested in over 215 small businesses throughout Canada. This level of activity in early stage, mostly private, businesses has not been matched by traditional mutual funds in Canada.

- *Nature of Venture Capital Investing* - Venture investing can best be described as active, value- added investing of patient capital. A typical venture investment takes 3 to 10 years to mature, during which time the fund's investment manager is actively involved in assisting the investee company to grow and develop, usually by participating at the board level and in sourcing additional financing. Typically, a venture investor will take a significant interest in

the investment, typically more than 10%. This type of investing is markedly different than typical mutual fund investing. Mutual fund investments generally can be characterized as shorter term, passive investing without a significant stake in the companies in which the mutual fund invests and without board representation. As a result of the venture capitalist's "hands on" approach and long term involvement, the costs of managing and administering LSIFs are significantly higher than those of traditional mutual funds. Long-term investing requires access to long term capital, which has been recognized by LSIF governing legislation which requires investors to repay both the federal and provincial tax credits if they sell their LSIF shares prior to eight years.

- *Type of Investee Companies* - Governing legislation requires LSIFs, like WOF and the GrowthWorks WV Funds, to invest the majority of the capital they raise in small, still developing businesses. Typically, these businesses are "emerging private companies" meaning they do not have profits or positive cashflows. As a result, they do not have listed prices and are not amenable to conventional valuation methods. For example, because they are pre-revenue, cashflows are not readily determinable with any reasonable degree of certainty. This presents valuation challenges which require special attention. This fact has been acknowledged in the valuation guidelines adopted throughout the venture capital industry such as the "Conservative Approach" under the European Venture Capital Association ("EVCA") guidelines. Recently the Canadian Venture Capital Association has recommended its members adopt valuation guidelines based on the EVCA's guidelines.

LSIFs are creatures of government economic development policy and operate in qualitatively different environment than other investment funds. This special context should be duly considered when forming securities regulatory policy applicable to these particular funds. This may mean in some instances that a "one size fits all" approach will not be appropriate.

COMMENTS ON NI 81-106 AND 81-106F1

Our comments on proposed NI 81-106 are set out below. We have separated our comments into topics and where appropriate have used sub-headings. We have also identified the relevant provisions of NI 81-106.

Separate Portfolio of Assets Considered to be a Separate Investment Fund

Summary

Where a series of shares share a large, common venture portfolio and core investment mandate with other series of shares and the only difference among the series is in the much smaller non-venture investment portfolio, treating each series as a wholly separate fund is not appropriate. In those circumstances, presenting the series a separate fund can be confusing to investors and will be more

costly. Instead, we submit that on these facts single fund reporting is more appropriate with specific disclosure on the minority of investments which differ.

Relevant Provisions of NI 81-106

Section 1.3(1) of NI 81-106 states that each class or series of a class of a fund that is referable to a separate portfolio of assets is considered to be a separate investment fund for the purposes of the instrument.

Section 7.5(1) states an investment fund with one or more class or series of securities that is referable to a single portfolio may have separate financial statements and management reports on fund performance for each class or series or the fund may have one set of financial statements provided that any distinctions between the class or series is disclosed.

Section 7.5(2) expressly contemplates that there can be differences between series while allowing the fund to prepare only one set of financial statements.

Section 7.4 of NI 81-106 restricts the binding together of financial statements and of management report of fund performance.

Application to Multiple Class and Series Funds Like WOF and the GrowthWorks WV Funds

Both WOF and the GrowthWorks WV Funds are multiple class and series funds. WOF offers Balanced Shares and Growth Shares. The GrowthWorks WV Funds offer Venture / Balanced Shares, Venture / Growth Shares, Venture / Income Shares, Venture / Financial Services Shares, Venture / Resource Shares and Venture / Diversified Shares. Currently, each fund prepares one set of financial statements that covers all of its series with the net asset value per share of each series is reported separately within those financial statements.

The fundamental investment objective of all series of WOF and the GrowthWorks WV Funds is to achieve long-term capital appreciation primarily through making venture capital investments in small and medium size businesses. Indeed, in order to have investors be eligible to receive tax credits, WOF and the GrowthWorks WV Funds are required to meet certain investment obligations. WOF invests over time 80% of the capital it raises in small and medium businesses. The GrowthWorks WV Funds invest at least 70% of the capital they raise in small and medium size businesses. Every share in each fund, regardless of the series, shares equally in that fund's venture portfolio. The essential difference among series is in how the incidental non-venture funds are invested.

Because the incidental non-venture component is invested differently, it cannot be said that the series are referable to a single portfolio. This means WOF and the GrowthWorks WV Funds seemingly cannot avail themselves of the ability to have a single set of financial statements under section 7.5(1) of NI 81-106 as it is currently drafted.

Submission

Causing WOF and the GrowthWorks WV Funds to prepare entirely separate financial statements and management reports of fund performance for each series simply because of the minority of non-venture investments differ unduly emphasizes a difference which was always intended to be minority in nature. In our view, this may confuse investors rather than assist them in understanding their investment. As a result, the significant increase in costs in preparing separate financial statements and management reports of fund performance would outweigh any perceived benefit to shareholders.

For the reasons set out above, we submit that sections 1.3, 7.4 and 7.5 of NI 81-106 be amended to allow multiple classes and series of shares of a fund having common fundamental investment objectives and a majority common portfolio, to be considered a single investment fund for the purposes of NI 81-106 and be allowed a single set of financial statements and single management report of fund performance provided that appropriate disclosure as to the differences is made. In the case of WOF and the GrowthWorks WV Funds we propose that:

(1) the statement of investment portfolio contains a listing of venture investments that will apply for all series and a separate listing of non-venture investments on a series by series basis;

(2) the financial highlights and past performance sections in the management report of fund performance be presented on a series by series basis; and

(3) the 25 top venture investment be listed for all series and then each series top 25 non-venture investments be listed for the specific series.

This disclosure is consistent with WOF's current disclosure in its simplified prospectus. Because the series structure of the GrowthWorks WV Funds is based on the WOF model, we believe this type of disclosure is also appropriate and more meaningful to investors for the GrowthWorks WV Funds. This suggestion places due emphasis on the common, majority venture portfolio and notes areas of difference in the incidental non-venture holdings. It also avoids many pages of duplication concerning the core venture portfolio.

Independent Valuations – Application of Part 8 of NI 81-106

Choice between Disclosure of Individual cost and current values versus Independent Valuations

Section 3.5 requires investment funds to provide information as to the historical cost and current value for each investment. As we have described in previous correspondence, this will often commercially harm the private companies LSIF primarily invest in as competitors and others may use publicly reported "writedowns" against them when speaking with customers, suppliers etc.

Section 8.2 permits alternative disclosure for LSIFs. LSIFs may instead disclose the individual securities in which they invest, but aggregate the changes from cost of those venture investments, showing only an aggregate adjustment from cost to fair value. (On this latter point, please see our comments above on aggregating of the adjustment cost.) Under this alternative, LSIFs must also obtain independent valuations of fair value.

It seems that the CSA views the application of section 8.2 as a choice that LSIFs can freely make. This is indicated by the CSA statement in its Appendix B to its notice where it states: "the valuation report is only required if the labour sponsored fund chooses to aggregate venture portfolio".

However, this apparent choice places LSIFs in a terrible conflict. The funds must choose between obtaining more costly valuation reports or disclosing hitherto confidential information about the carrying values of individual investee companies. Such disclosure may breach a fund's confidentiality obligations, cause the investee company commercial harm as others use this newly accessible information against the company in the marketplace, and/or adversely affect the fund's future deal flow as it becomes known in the entrepreneurial community that the fund publishes this information. We submit that for reputable funds looking to protect the fund's interests this is not a real choice. Moreover, we believe 81-106 ought not to make this choice possible for LSIFs given their specific circumstances and the injury it can bring to investee companies, the funds and fund shareholders.

Independent Valuations

Summary

81-106's proposed approach for independent valuation of LSIF investments seems to be based on the assumption that "fair value" under GAAP provides a clear, well developed set of rules that will produce a relatively narrow range of results when applied by accounting professionals to the same set of facts. However, this is currently not the case for development stage, private companies, being the kind of companies LSIFs primarily invest in.

For more senior private companies, traditional valuation methodologies exist and work reasonably well. For development stage, private companies the fair value measurement under GAAP is still at an early stage of evolution and can produce an unduly broad range of values.

We agree with the CSA that significant steps should be taken to improve comparability among investment funds in general, including LSIFs. Creating a high a degree of comparability among LSIFs would best be achieved by having all LSIFs apply a common, rules based valuation framework for LSIFs that produces a fairly narrow range of values when applied to the same set of facts. We do not think that fair value under GAAP is able to produce such a narrow range of results at this time. We propose that LSIF industry players, their accounting/valuation professionals and securities regulators work on defining and adopting a prescriptive, common valuation framework

specifically for LSIFs that will achieve a high degree of comparability, be independently verified and be cost efficient.

To enable this to occur, we suggest that the CSA defer this element pending completion of that development work. This would also be consistent with the fact that the CSA has indicated that study of investment valuation is the second phase of NI 81-106.

Evolving GAAP

Although AcG12 prescribes that investment companies carry their portfolio of investments at "fair value", in some areas there is only broad guidance in respect to what constitutes GAAP for the application of the fair value mandate. For more senior private companies, traditional valuation methodologies exist and work reasonably well to generate comparable results. However, for development stage, private companies, being the kind of companies LSIFs primarily invest in, the fair value measurement under GAAP is still at an early stage of evolution and can produce a broad range of values when applied by different professionals to the same set of facts.

For example, a common approach to valuing development stage, private companies that are "pre-revenue", would be to estimate or project future cash flows and then discount them back to generate a net present value for the company. To illustrate the point we make about the broad range of results that can be produced by such an approach, we have attached an example. In the example, two persons apply this approach, each making somewhat different assumptions and projections as to market share achieved, costs/margins and what discount rate should be applied. While this is an example only, it does illustrate the point that for these kinds of companies GAAP may currently permit too broad a range and lack a high level of comparability.

The accounting profession has begun to further develop the conceptual framework for measuring fair value. On June 23, 2004, the United States Financial Accounting Standards Board ("FASB") issued for comment an Exposure Draft, *Fair Value Measurements.* In the accompanying press release, FASB stated that the draft seeks to establish a framework for measuring fair value that would apply broadly to financial and nonfinancial assets and liabilities, improving the consistency, comparability, and reliability of the measurements. This framework would replace any current system for measuring fair value. "An important aspect of this project is to provide guidance for measuring fair value that can be generally understood and consistently applied by preparers, auditors, and valuation professionals," said Linda A. McDonald, FASB Project Manager.

FASB's exposure draft on "Fair Value Measurements" will likely influence future pronouncements on fair value measurement made by the CICA because statements issued by authorized bodies in other jurisdictions may be considered when primary sources of Canadian GAAP do not provide clear and authoritative guidance. It is also important to note that the Canadian Venture Capital Association has recently released recommended valuation guidelines for its members.

We support the CSA in taking steps to improve comparability among LSIFs. Creating a high a degree of comparability among LSIFs would best be achieved by having all LSIFs apply a common, rules based valuation framework for LSIFs that produces a fairly narrow range of values when applied to the same set of facts. We do not think that fair value under GAAP is able to produce such a narrow range of results at this time. Even with further development, this may continue to be the case. We propose that LSIF industry players, their accounting/valuation professionals and securities regulators work on defining and adopting a prescriptive, common valuation framework specifically for LSIFs that will achieve a high degree of comparability, be independently verified and be cost efficient (the "LSIF Valuation Framework").

To enable this to occur, we suggest that the CSA defer this element pending completion of that development work. This would also be consistent with the fact that the CSA has indicated that study of investment valuation is the second phase of NI 81-106.

Independent Verification

As noted above, having a common LSIF Valuation Framework so we can establish a good level of comparability is step one. Once that common, appropriate standard is ready, we suggest that step two should be independent verification by a qualified professional. This will give comfort to all stakeholders that the new common standard has indeed been applied.

We believe that an LSIF's auditor is an appropriate, independent and qualified person to provide that verification. In the companion policy, the CSA states that a report confirming compliance with stated valuation policies and practices cannot take the place of an independent valuation. The CSA explains the reasons why such compliance reports are not acceptable in Appendix B to its notice where it states "valuation policies and procedures are established by the investment fund or manager. A report of compliance with these valuation policies and procedures does not address the <u>appropriateness</u> of the policies and procedures." [*emphasis added*].

Given that the LSIF Valuation Framework will establish a common set of rules that the CSA and others will be able to assess as being appropriate prior to implementation, a verification report from an independent auditor should be acceptable. This approach would also be cost-effective, which will assist in keeping MERs down.

We are look forward to the prospect of working with other LSIFs, the CSA, and the CICA during the second phase of NI 81-106 to develop a LSIF Valuation Framework that not only results in fair values under GAAP but also results in a high degree of comparability so investors are better able to compare "apples to apples" when looking at LSIF values.

Segmented Disclosure in the Statement of Investment Portfolio

Section 3.5 requires investment funds to provide information as to the historical cost and current value for each investment. As we have described in previous correspondence, this will disadvantage the private companies in which LSIF invest. It may also breach a fund's confidentiality restrictions and adversely affect the fund's future deal flow once it becomes known in the entrepreneurial community that investee companies are indirectly providing information that they would not otherwise be required to disclose publicly but for LSIF's investment in them. Section 8.2 permits alternative disclosure for LSIFs so long as they provide detailed segmented information (including aggregate carrying value) by stage of development and industry class.

Because of the dynamics presented by LSIFs holding private companies, we suggest that any requirement for segmented disclosure by LSIFs be modified to ensure that company specific information is not required to be disclosed, directly or indirectly. To achieve comparability among funds, there must be some level of consistency in segmenting information. However, in situations where a fund has only one investment in a particular stage and class, mandating segmented disclosure by stage and industry class will effectively require the fund to disclose the carrying value of that individual investment. This directly undermines the purpose of section 8.2. In addition, this segmentation may not be suitable for all LSIFs since some focus mainly on one industry class while others focus mainly on companies at one particular stage.

As a result, we agree with ALSIF's proposal for exceptions to the requirements for segmentation by stage and sector. Specifically, we would suggest that LSIFs be entitled to simply choose the appropriate subgroups for segmented disclosure, based on their particular areas of concentration of portfolio value. If this approach is unacceptable, in the alternative we would suggest the following clarifications or changes to the regime outlined in section 8.2(b):

(a) We suggest that the reference in section 8.2(b)(i) to "a table" be changed to "two tables", one of which would show segmentation by sector and one of which would show segmentation by stage. We believe this would result in clearer disclosure to investors of an LSIF's portfolio concentration by these two different measures. It would also reduce the likelihood that any one "cell" on the table would only contain one or two companies, thereby resulting in disclosure that could permit readers to deduce the carrying value of an individual investment. To further allay this latter concern, LSIFs should also be permitted to aggregate segments where any particular segment represents less than 15% of the aggregate carrying value of all the LSIF's venture investments ("Venture NAV") or less 15% of its venture investments by number. For example, assume an LSIF is segmenting its venture investments by sector in the categories of Information Technology, Life Sciences, Manufacturing and Services. Assume further that the LSIF has 25 venture investments with a Venture NAV of $50 million. If the Manufacturing sector includes less than 4 investments or less than $7.5m of Venture NAV, the LSIF would entitled to aggregate its Manufacturing investments with those of another

sector (for example, the LSIF could provide combined disclosure for the Manufacturing and Services sectors).

(b) The requirement to provide the segmented data should not apply until an LSIF has 15 venture investments. Given the investment "pacing" rules governing Ontario LSIFs and the requirement that an LSIF put no more than 10% of its equity capital into any one investment, an LSIF that raises a stable amount of money at a stable NAV per share would normally cross this threshold within two to three years from inception.

(c) Sector-specific LSIFs should only be required to provide segmented disclosure by stage. Requiring such funds to split their portfolios into sub-sectors will probably not be useful to investors or comparable as between LSIFs.

Net Asset Value, Financial Highlights and Past Performance

Summary

In the case of LSIFs, the return an investor experiences from an investment is the difference between the subscription price the investor paid for the share purchased and the redemption price the investor receives on redemption. Accordingly, the calculations required to provide the disclosure in 81-106F and the disclosure itself must be based on the price used for issuing and redeeming shares. Otherwise, the report of management performance will not reflect the individual investors' investment experience and will confuse investors.

In British Columbia, Saskatchewan, Manitoba, Quebec and New Brunswick, LSIFs are allowed to include the unamortized balance of past and current up-front commissions in calculating their share prices for issuing and redeeming shares. This price is often referred to as "Pricing NAV". This price will differ from net asset value calculated under GAAP because the unamortized balance of commissions is no longer recognized as an asset under GAAP Therefore, in order to achieve comparability of fund performance, we respectfully request that NI 81-106 acknowledge that Pricing NAV is used by many LSIFs and that 81-106F1 expressly provide for the use of "Pricing NAV per Share" in applicable jurisdictions provided that the investment fund include relevant disclosure concerning the difference between the Pricing NAV per Share and the net asset value per share calculated under GAAP.

Pricing NAV

Historically, all LSIFs "capitalized" the commissions paid on the sale of their shares as if it were an asset and then fully amortized this cost on a straight-line basis. Until September 30, 2003, the unamortized balance of sales commissions was recognized as an asset under GAAP. On that date, GAAP changed and the amount capitalized is no longer be recognized as an asset or shown as an asset on financial statements.

The British Columbia Securities Commission has accepted the "disclosure model" whereby LSIFs (which includes venture capital corporations ("VCCs") registered under the *Small Business Venture Capital Act*) (British Columbia) continue to include the unamortized balance of up-front commissions in calculating the share price for issuing and redeeming shares provided that each fund identifies the differences between the Pricing NAV per Share and the net asset value per share calculated under GAAP in their prospectuses and in the notes to their audited financial statements. This recognizes the fact that the up-front cost of the commission is associated with raising capital that is on hand for eight years (or five in the case of VCCs). As such, it makes business sense to spread or match that cost equally over the same period. We understand that securities regulators in Saskatchewan, Manitoba, Quebec and New Brunswick also allow LSIFs in their jurisdictions to include the unamortized balance of up-front commissions in calculating their share prices for issuing and redeeming shares.

Submissions

Pursuant to section 14.2(1) of NI 81-106, values must be calculated in accordance with GAAP. 81-106F1, in its current form, refers to net asset value and net asset value per share and does not contemplate Pricing NAV.

Currently, the form of simplified prospectus under national instrument 81-101 requires disclosure that is virtually identical to the proposed disclosure in items 3, 4 and 5 of Part B and C of 81-106F1. WOF offers its shares under this form of prospectus.

Because the return from an investment in WOF that an investor actually experiences is the difference between the subscription price paid and the redemption price received on redemption, WOF uses Pricing NAV to calculate returns in its prospectus. Disclosure using any other value, such as net asset value for GAAP purposes, would simply not be accurate when the fund uses Pricing NAV for share transactions.. It would confuse investors and not reflect reality.

For the foregoing reasons, we submit that NI 81-106 acknowledge Pricing NAV and that 81-106F1 expressly provide for the use of Pricing NAV per shares in applicable jurisdictions provided that the investment fund include relevant disclosure concerning difference between the Pricing NAV per share and the net asset value per share calculated under GAAP.

Frequency of Calculating Net Asset Value

NI 81-106 now contains requirements regarding the calculation of net asset value and the frequency in which it must be calculated. Currently, these topics are contained in national instrument 81-102 ("NI 81-102").

Subsection 14.2(3) requires investment funds that use derivatives to calculate net asset value daily whereas all other funds may calculate weekly. Subsection (5) grandfathers investment funds in existence at the time NI 81-106 comes into force provided that they calculate net asset value at least monthly. Although not clearly stated, one assumes that a fund required to calculate net asset value daily would also be required to process share purchases and redemptions daily.

We note that the current provisions of NI 81-102 provide that only funds that use specified derivatives must calculate net asset value daily. "Specified derivatives" in NI 81-102 excludes the common forms of derivatives that we believe the vast majority of funds use. A specified derivative means an instrument, agreement or security, the market price, value or payment obligations of which are derived from, referenced to or based on an underlying interest, other than (a) a conventional convertible security, (b) a specified asset-backed security, (c) an index participation unit, (d) a government or corporate strip bond, (e) a capital, equity dividend or income share of a subdivided equity or fixed income security, (f) a conventional warrant or right, or (g) a special warrant.

We note that neither NI 81-102 nor NI 81-106 currently includes a definition of "derivatives".

The CSA has not stated why it has moved from "specified derivatives" to all derivatives in requiring daily net asset value calculations. We believe that this may have been unintentional. Based on this new wording, newly formed LSIFs will have to choose between incurring the higher costs of daily, year round pricing and processing share purchases and redemptions or unduly restricting their normal kinds of investments which would include warrants, rights, convertible debentures etc. This does not seem appropriate when no compelling offsetting benefit has been identified.

Accordingly, we respectfully submit that NI 81-106 be amended to follow the current requirements of NI 81-102 and require only investment funds using specified derivatives to calculate net asset value daily.

Proxy Voting

Part 10 of NI 81-106 requires investment funds to establish policies and procedures for voting proxy materials and to make their proxy voting records available to security holders.

A feature of "hands on" venture capital investing in private companies is that many decisions normally taken at the board level of public companies may also by written shareholders agreement require approval by specified large shareholders of the investee company. These decisions typically concern strategic initiatives that may affect the competitive advantage of the investee company. As a result, requiring LSIFs to disclosure their voting on these types of matters may seriously jeopardize the investee company's competitive advantage. It may also breach a fund's confidentiality restrictions and adversely affect the fund's future deal flow when it becomes known in the entrepreneurial community that investee companies are indirectly providing information that they would not otherwise be required to disclose publicly but for the LSIF's investment in them. On a

practical level, given the extensive nature of these items, a fund's stated proxy voting policies will have to be general in nature and therefore may be of limited value to investors.

For the foregoing reasons, we respectfully submit that Part 10 be amended so that it does not apply an LSIF's <u>private</u> investee companies.

Related Party Transactions

Section 4.2 of NI 81-102 defines a "related party" to include any company with less than 100 shareholders where an officer/director of the fund serves as an officer/director of the company. NI 81-102 prohibits mutual funds from purchasing securities from a related party unless the price paid for the securities is not more than the ask price on a public quotation.

As stated above, LSIFs are active investors that frequently serve on the boards of their investee companies. LSIFs invest primarily in small and medium size private companies the vast majority of which have less than 100 shareholders. As a result, <u>most</u> venture investments will now be a related party transaction. As a result, LSIFs who are subject to NI 81-102 regularly receive exemptive relief from section 4.2 for such follow-on investments.

Section 3.6 of the Instrument requires detailed note disclosure of transactions between an investment fund and a "related party". Because of the nature of follow-on investments described above, this will result in LSIFs providing detailed disclosure of the vast majority of their investment activity as opposed to what in other funds is an unusual type of investment activity. This seems inconsistent with the exemptive relief granted under NI 81-102 regarding LSIF's follow-on venture investments. We believe it will unduly clutter financial statements for limited benefit given that investors know and expect LSIFs to make a number of follow-on investments in small and medium-sized investee companies that the LSIF will have board representation on. Accordingly, we respectfully request that section 3.6 be amended to not require LSIFs to provide detailed disclosure of related party transactions that are venture investments.

MER Segmentation

Part 15 of NI 81-106 and Part 10 of the companion policy outline the calculation and presentation of the MER. In previous submissions, we and ALSIF expressed concerns about having a variable performance fee included in the management expense ratio. Without clarifying disclosure, the variable nature of the performance bonus may not be appreciated and investors may incorrectly conclude that a fund's <u>fixed</u> annual costs are higher than they really are. In response to these concerns, the CSA states in Appendix B to its notice that MER can be segmented in the notes to the financial statements and the management report of fund performance, although neither NI 81-106 nor 81-106F1 contain an express provision. We respectfully request that each of NI 81-106 and 81-106F1 be amended to contain such an express provision.

Standing Instructions for Statement Delivery

Section 5.1(3) of NI 81-106 states that an investment fund may only use the annual instructions procedure under section 5.3 if it is impracticable for the fund to send according to standing instructions. In order to satisfy the procedures for sending according to standing instructions, section 5.2(4) of NI 81-106 requires standing instructions be obtained at the time of purchase. Unfortunately it is not possible to solicit such instructions with purchases made over the FundSERV electronic order processing system. Accordingly, it would appear that on these purchases, funds will have to use the annual instructions in the first year. It appears from Part 5 that the fund will then be able to subsequently move to standing instructions. If we are incorrect in our understanding of this, please advise.

Under section 5.3(3), a request form must be sent on the earlier of the first written communication with an investor and six months after the end of the last financial year for the fund. Depending on when LSIFs hold their annual general meetings ("AGM") relative to their year-end, these timetables could have the effect of requiring an additional mailing. In our view, this results in additional costs for no compelling policy reason. Accordingly, we respectfully submit that NI 81-106 be amended so that annual request forms are required to be sent on the first regularly scheduled written communication with an investors.

Requirements on Coming into Force

Section 5.2(3) requires funds to send registered holder or beneficial holder a document explaining the choices regarding sending instructions and soliciting such instructions within 3 months of NI 81-106 coming into force. Similarly, section 18.5 states that despite Part 5, a fund must deliver to every shareholder the management discussion of fund performance for the first year together with an explanation.

Depending on when LSIFs hold their AGM relative to their year-end, these timetables could force funds to do an additional mailing than it otherwise would do. With over 55,000 shareholders at WOF and 95,000 shareholders at the GrowthWorks WV Funds, this results in substantial additional costs for no compelling policy reason. We respectfully submit that a better requirement is to have these documents sent to investors with the first regularly scheduled written communication with all investors and request that sections 5.2(3) and 18.5 be amended accordingly.

Undefined Terms/Clarification

NI 81-106 requires disclosure regarding "investment portfolio", "long portfolio" or "short portfolio". We have not been able to locate definitions for these exact terms in NI 81-106, NI 81-102, national instrument 81-105, national instrument 14-101 or the *Securities Act* (British Columbia). Accordingly, we respectfully request that NI 81-106 be amended to include definitions for these

terms. Also, in order to avoid uncertainty, one of the Funds' auditors requests hat NI 81-106 contain a statement clarifying that other than the specific additional requirements set out in NI 81-106, the financial statements required by NI 81-106 are to be prepared in accordance with GAAP and application of the CICA Handbook.

Conclusion

We appreciate the opportunity to provide our comments and welcome the opportunity to discuss them further.

Best regards,

"Jill W. McFarlane"

Jill W. McFarlane

EXAMPLE

Valuing a development stage, private, pre-revenue company
Estimating future cash flows and discounting back to calculate a net present value ("NPV")

Asumptions:

		Person A	Person B
Years		6	6
Initial outlay		$ (1,000,000)	$ (1,000,000)
Product market size	$ 50,000,000		
Market share (per annum)		5%	8%
Annual product sales revenue		$ 2,500,000	$ 4,000,000
Cost of goods sold (%)		75%	70%
Cost of goods sold on cash cost		$ (1,875,000)	$ (2,800,000)
Discount rate		30%	25%
Tax rate		0%	0%
Summary;			
Net cash flows (per annum)		$ 625,000	$ 1,200,000
After tax discount rate		30%	25%

NPV Calculation:

	Person A	Person B
Initial outlay	$ (1,000,000)	$ (1,000,000)
PV of discounted cash flows	$1,651,716	$3,541,709
NPV	$ 651,716	$ 2,541,709