Kenmar Associates
Investor protection and education

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NOTICE AND REQUEST FOR COMMENT
PROPOSED NATIONAL INSTRUMENT 55-104
***INSIDER REPORTING REQUIREMENTS AND EXEMPTIONS*, COMPANION POLICY 55-104CP**
***INSIDER REPORTING REQUIREMENTS AND EXEMPTIONS* AND RELATED CONSEQUENTIAL AMENDMENTS**

By way of introduction, Kenmar Associates is an Ontario- based organization focused on investor education via on-line papers hosted at www.canadianfundwatch.com. Kenmar also publishes ***the Fund OBSERVER*** on a monthly basis discussing investor protection issues primarily for mutual fund investors. We are responding to the request for comment from the viewpoint of the retail investor/ shareholder.

INTRODUCTION: Investors, analysts and others use insider-trading reports as part of their decision making. It is well established that there is some correlation with these trading patterns and Company health. As regards executive compensation, the timely knowledge of how many stock options (or equivalent compensation) have been granted assists in assessing the efficacy of corporate governance. Other users of course can employ such information in litigation and for other purposes such as option backdating analysis.

Timely, accurate Insider reporting serves three very important functions:

1. it provides information to investors about the trading activities of directors, senior management or significant shareholders of companies
2. it serves to deter insider trading based on confidential information, since insiders know they must disclose all of their trades to the public [assuming they also believe that regulators will enforce disclosure rules].
3. it provides early information on stock based executive compensation practices

This initiative is thus very important from an investor perspective.

OBSERVATIONS/SUGGESTIONS: In our investor advocacy work we have come across numerous best practices that may be useful to regulators.

1. Distribute Internal Memorandum. Issuers should annually distribute a memorandum to all directors, executive officers, and greater than 10% beneficial owners advising them of the prevailing SEDI provisions and the importance of prompt reporting of any transactions in the issuer's securities.
2. Send Periodic Alerts and Reminders. Issuers should send periodic alerts and reminders to directors, executive officers and greater than 10% beneficial owners regarding the importance of prompt reporting of any transactions in the issuer's securities. At least once per annum, put it on a Board meeting agenda.
3. Establish Internal Procedures. In order to ensure timely insider reporting, issuers should adopt documented internal procedures and controls to require insiders to report any transaction in the issuer's securities on the day such transaction occurs. We would go further to suggest pre-sale notification to the issuer (i.e., General Counsel or Chief Financial Officer) to provide adequate time to review the proposed transaction and consider any disclosure issues.
4. Review List of Reporting Insiders. Issuers should review the list of executive officers filing reports pursuant to CSA regulations to confirm that all persons (and only those persons) legally required to file reports are reporting their transactions in a timely and accurate manner.
5. Establish Powers of Attorney. Issuers should consider designating one or more officers to whom insiders may grant a limited power of attorney for purposes of future required Insider filings. Through such an arrangement, issuers would have greater control over filings to ensure that they are made within the 2 day time period.
6. Require Brokers to Sign Pre-Clearance Letters. In order to enlist the help of insiders' stockbrokers, issuers should ask insiders to have their stockbrokers sign a letter agreeing that the stockbroker will report securities transactions to the issuer and will not enter any order without first verifying that the trade has been pre-cleared under the issuer's policy. [A number of firms require declaration of insider status when making a trade, such as TD Waterhouse on-line brokerage, but not all.]

We note that with respect to certain transactions, it may not be practicable for insiders to meet the accelerated reporting deadline. For example, option grants are often not communicated to filing insiders on the day of the option grant, and for some issuers with a large number of recipients, a large number of individual insiders will often receive option grants on the same day. Accordingly, we agree that it may not be inappropriate for issuers to do the filing and excuse individuals from late filing fees in the event of an error.

COMMENTS:

Our comments relate to 6 main areas:

1. Filing Insiders –We agree that filing insiders should be limited to those with decision and influence powers. At least the top 5 NEO's should be filing insiders.
2. Timing –While the 5 calendar days proposed is an improvement, we hope that the end goal is 2 business days as employed by the SEC. The shorter the timeline, the better for investors and shareholders.
3. Late filing fees – It makes no sense to have non-uniform rules for late filing depending on provincial jurisdiction. We recommend that the "fee" (penalty) schedule be harmonized across Canada. As regards the amount, we conclude that the token amount will not be a deterrent for late filers if it offers them advantage. The CSA should also reveal how it will treat chronic late /incomplete or non-filers.
4. Filing Errors- It is not clear what the consequences are for incorrect or incomplete filings that could mislead those utilizing the SEDI system for investment decisions.
5. Public disclosure of filers who paid late filing fees- Humiliation may have some benefits. We presume the CSA has confirmed that doing this is not in breach of Federal or Provincial privacy laws or Human rights provisions. Additionally, if this disclosure is enacted, the CSA should establish a formal Appeal procedure as it sometimes happens there are extenuating circumstances. PC failure, Network outage, a serious family matter or even SEDI malfunctions. In any event, SEDI telephone support should be available during at least 8:00-5:00 on all calendar days. We also recommend that the SEDI system make it easy to print out any page that could be used as proof of action. Further, we recommend SEDI be modified to send an automated email confirming the receipt and posting of a filing.
6. Use of SEDAR for Issuer Grant reports for option grants- We believe ALL insider activity should be in one place, SEDI. We caution that although Issuer Grant reports may reduce administration, it may lead to problems with small issuers who are not adequately resourced to take on this obligation.

We do not understand why mutual funds are exempted from insider reporting in those cases where the fund family is a significant shareholders as a result of the cumulative ownership of shares in its many mutual funds. To a large extent, investment funds **are** the market in Canada. They certainly have *control and direction* over the shares and bonds. In the case of the fund companies that have brokerage affiliates, banking or investment banking operations, the conflict-of interest can be significant. These funds clearly have voting rights which they can and do exercise and report upon, albeit with significant delay. When they make trades, the impact can be significant to the market. Indeed the impact may be greater than any one individual insider that is required to file transactions.

We also note that in Part 10, the regulator or securities regulatory authority may grant an exemption from this Instrument, in whole or in part, subject to such conditions or restrictions as may be imposed in the exemption. As we have observed many times,

regulatory exemptions have rarely served small investors well. If this is a good rule, it should not be exempted away by regulators or anyone else. If the CSA can identify the specific types of situations where an exemption can be granted, effectively nullifying the intent of the rule, they should be enumerated a priori and exposed to public comment.

EMPTY VOTING: One area that has been of concern is that of empty voting by hedge funds and other entities. We would ask that the CSA clarify the rules surrounding securities lending and ownership/voting rights. Such votes distort the marketplace and can lead to disenfranchisement for retail investors. In particular, we would ask the CSA to consider rescinding the right for a mutual fund to engage in securities lending. This lending adds significant risk to fund unitholders while providing minimal benefit.

ENFORCEMENT: The dismal result of the Andrew Rankin tipping/insider trading court case was disturbing to us. This was followed by the wrist-slap penalty (a letter of reprimand) in the well publicized ComDev option backdating case. These outcomes detract from the credibility of regulators and the justice system to effectively deal with economic crime and financial assault.

As we have said so many times before, rules without enforcement are of little value. We therefore expect the CSA to enforce these reporting rules with vigor and to report annually on the statistics, late filing fees paid, other sanctions applied, SEDI and enforcement process improvements etc.. We assume that the monitoring process now contains the basic features such as cross checks on data entries, sanity checks on numbers, cross checks with broker /exchange databases, timeline scans vs. market activity (e.g. to detect option backdating) and the like.

SUMMATION:

Kenmar regard this rule change as moving in the right direction. We of course wish that Canada had one Securities Act and regulator but that is for another day. We hope this submission is useful to the CSA .

Given the incredible creativity of CEO's and their advisers in complicating and obscuring executive compensation, you may want to add a **General Anti-Avoidance** provision. This would require firms and individuals to report any form of arrangement that moves equity-derived or stock-based assets or cash from the Company balance sheet to them or related parties/entities. We realize that these arrangements may be captured in the Compensation Disclosure and Analysis table required by non-SEDI reporting systems.

Should you require any additional information, do not hesitate to contact us.

Permission is granted for public posting.

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