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July 10, 2013

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Financial and Consumer Affairs
Authority of Saskatchewan
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
New Brunswick Securities Commission
Superintendent of Securities, Prince
Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland
and Labrador
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Dear Sirs/Mesdames:

Re: Proposed Amendments and Changes to National Instrument 62-103 *Early Warning System and Related Take-Over Bid and Insider Reporting Issues* (NI 62-103)

This letter is submitted in response to the Notice and Request for Comments ("**Notice**") made by the Canadian Securities Administrators ("**CSA**") regarding the proposed amendments to MI 62-104, NI 62-103 and NP 62-203 (the "**Proposed Amendments**"). We are submitting this letter on behalf of our client, a registered investment adviser that advises clients investing in securities worldwide, including in Canadian securities. These comments are limited to addressing the application of the Proposed Amendments to closed-end investment funds that permit the redemption of securities at a price based on net asset value ("**NAV**") not more than once a year ("**Annual Redemption Funds**"). The CSA have taken the view that these are non-redeemable investment funds.

These comments are provided in support of our client's view that there are no policy considerations warranting any amendment to the reporting thresholds provided for in Part 5 of MI 62-104 or the equivalent provisions of Canadian securities legislation for Annual Redemption Funds. In fact, for reasons described below, applying a five percent reporting threshold to Annual Redemption Funds would have an adverse impact on liquidity due to the regulatory burden and attendant costs that would be borne mainly by investors making passive material investments in these investment products. Our client also submits that the Proposed Amendments regarding "equity equivalent derivatives" ought not to apply to Annual Redemption Funds.

Consistent Treatment for Investment Funds

Annual Redemption Funds trade on public exchanges and are redeemable not more than once a year for cash at or close to NAV. Due to their redemption features, the market prices of Annual Redemption Funds typically do not materially deviate from NAV. Our client advises that as of market close on May 23, 2013, the average discount of the market price to NAV for Annual Redemption Funds listed on the TSX was 2.1% (this calculation excludes mutual funds that permit redemptions more frequently than once a year based on NAV).

Significantly for the purposes of this submission, closed-end investment funds that are redeemable quarterly or monthly at a price based on NAV are already exempt from the early warning reporting requirements of NI 62-103 pursuant to section 3.3 thereof, because they are considered by the CSA to be "mutual funds". Our client submits that Annual Redemption Funds should be similarly exempt from these requirements.

Annual Redemption Funds share many of the same characteristics as funds that the CSA classifies as mutual funds (including closed-end funds with quarterly redemptions at

NAV). Like mutual funds, Annual Redemption Funds may not invest their funds for the purpose of exercising control, or seeking to exercise control, of any investee company other than another non-redeemable investment fund or a mutual fund. In fact, under proposed amendments to NI 81-102, the CSA propose that the same control and concentration restrictions that currently apply to "mutual funds" should apply to traditional non-redeemable investment funds including Annual Redemption Funds. If these proposed amendments come into force, it will be impossible for any investor to acquire control of any issuer through the acquisition of units in an Annual Redemption Fund issuer because, like any mutual fund, subject to exemptive relief, these issuers will not be permitted to acquire more than 10% of the voting or equity securities of any issuer (other than another mutual fund or non-redeemable investment fund) and will not be able to invest more than 10% of its NAV in the securities of any issuer (other than prescribed investments in securities of another non-redeemable investment fund or mutual fund).

In this regard, it is significant that when NI 62-103 was adopted in 1999, the CSA stated that "there are no compelling policy reasons to require early warning reporting in connection with the acquisition of publicly-traded mutual funds, having regard to the investment restrictions to which those funds are subject". At that time, Annual Redemption Funds had not yet become prominent in the marketplace and the Securities Act (Ontario) had not yet been amended to provide for a definition of "non-redeemable investment funds"[1]. For this reason, the CSA likely did not have the opportunity to consider exempting Annual Redemption Funds from early warning requirements for the same or similar reasons that mutual funds were exempted. Therefore, by default, Annual Redemption Funds were grouped with reporting issuers that were not investment funds.

The case for exempting Annual Redemption Funds from early warning requirements is even more compelling now that it is proposed that these funds be subject to the same investment and concentration restrictions as mutual funds. In fact, in their request for comments respecting the proposed amendments to NI 81-102, the CSA queried whether the time had come for the definition of mutual fund to apply to Annual Redemption Funds as it does to similar investment funds that afford security holders more frequent redemption opportunities[2]. In their request for comments regarding the proposed NI 81-102 amendments, the CSA stated that the proposal "will level the playing field among non-redeemable investment funds, conventional mutual funds and ETFs, providing a more consistent framework within which trust funds can compete with each other". It is

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1 We note that OSC Rule 15-401 was amended in 1999 to provide for a definition of "non-redeemable investment funds", but that definition was not adopted until after the CSA had already received the comment letters that prompted it to exempt mutual funds from the early warning reporting requirements of NI 62-103.

2 Annex A, CSA Notice and Request for Comment Proposed Amendments to National Instrument 81-102. Companion Policy 81-102CP and Related Consequential Amendments

submitted that this policy objective of consistent treatment among these investment products should apply equally in the context of the early warning regime.

Policy Considerations Underlying Proposed Amendments to Reporting Thresholds Do Not Apply to Annual Redemption Funds

The primary purpose of the early warning regime is to alert the marketplace to accumulations of blocks of securities that "may influence control of a reporting issuer". Specifically, as the CSA have identified in the Notice, early warning disclosure is designed to signal possible take-over bids as well as to enable the marketplace to assess potential shareholder activist activities that might result in changes to the issuer's board of directors, or influence the outcome of a security holder vote respecting proposed transactions and other initiatives. The key rationale for changing the reporting threshold from 10% to 5% is to align the trigger for early warning reporting requirements with the threshold required of a security holder to requisition a meeting.

Since it can be inferred that the objective of holders of securities of Annual Redemption Funds is to seek exposure to a managed portfolio of securities and not to control, or influence the control of, the fund, these policy considerations have no application to this type of issuer. Because of the nature of an investment fund, the investment restrictions that typically apply to Annual Redemption Funds and their redemption features, no Annual Redemption Fund has ever been the target of a take-over bid as far as our client is aware. Moreover, since Annual Redemption Fund security holders have an annual opportunity to "vote with their feet" through the redemption of their investments for cash at NAV, there is no incentive for security holders to express dissatisfaction with the management of a fund or any proposed transaction through a proxy contest. Consequently, security holder meetings of Annual Redemption Funds are generally neither contentious nor economically meaningful to security holders. In fact, Annual Redemption Funds are not required to hold annual meetings except in the rare cases where the fund is a corporate entity. The constating documents of Annual Redemption Funds typically set the ownership threshold enabling security holders to requisition a security holder meeting at higher than 5%.

Precedent of SEC No-Action Letter

The benefit of consistency with reporting obligations in other jurisdictions has been identified as an argument in favour of changes to early warning reporting thresholds in Canada. Accordingly, it is worth noting that in a 1998 No-Action Letter regarding the waiver of 13(g) filings (the U.S. equivalent to early warning reports) for holders of ETF securities, the United States Securities Exchange Commission ("**SEC**") considered the issues raised in this submission in analogous circumstances.

Annual Redemption Funds were not addressed in the 1998 No-Action Letter because they do not exist in the United States. However, the SEC's reasoning is relevant to them. In the No-Action Letter, the SEC observed that ETFs are subject to strict investment restrictions because managers generally are not permitted to deviate from the investment mandate described in the ETF's prospectus. The SEC's No-Action Letter also noted that there is little incentive for security holders to pursue a take-over bid for ETFs. The same is true for Annual Redemption Funds which, like ETFs, trade in the public market at a price very close to their NAV.

Policy Considerations Underlying Proposed Amendments Regarding Equity Equivalent Derivatives Do Not Apply to Annual Redemption Funds

It is submitted that the Proposed Amendments respecting "equity equivalent derivatives" should not apply to derivatives referencing securities of Annual Redemption Funds. Counterparties to derivative contracts respecting Annual Redemption Fund securities generally do not have the intention of "acquiring the referenced securities at a future date" (as noted in question 14 of the Notice) but would still be required to report monthly under the alternative monthly reporting regime under NI 62-103. From a legal and economic perspective, these equity derivative contracts are wholly synthetic, each being merely a cash "bet" between two parties; they are not backed by, or secured by, the underlying security, and there is no right for a party ever to obtain the underlying security. Equity derivative contracts allow parties to achieve economic benefits without affecting voting or ownership of the underlying securities, and reporting of these transactions is not in line with the purpose of the disclosure regime.

Moreover, in the experience of our client, it is extremely rare that equity derivative contracts result in the acquisition of beneficial ownership of the underlying security at any point during or upon the termination of the contract. Our client advises that, in their experience all of the major banks and brokers that provide such contracts on Canadian securities require that the contracts be settled only in cash; they do not allow swaps to be "crossed off."

Consequently, for the reasons set-out above, concerns about hidden ownership and empty voting do not apply to Annual Redemption Funds.

Disadvantages of Applying Proposed Amendments to Annual Redemption Funds

The application of the Proposed Amendments to Annual Redemption Funds will impose a regulatory burden on investors in these products that is not warranted due to the absence of any regulatory objective that would be achieved by the extension of these requirements to holders of the securities to these issuers. Maintaining consistent market liquidity is essential to the viability of the market for Annual Redemption Fund securities. If value investors such as those our client advises were deterred from investing in securities of Annual Redemption Funds by virtue of onerous reporting requirements, liquidity would be reduced and the spread between the trading price and NAV for these securities would be expected to widen. Since the Proposed Amendments do not apply to mutual funds including closed-end mutual funds, it can be expected that liquidity would be diverted to these securities resulting in disparities in trading prices that are not reflective of the respective performance of the underlying assets. Annual Redemption Funds are retail investment products that serve a beneficial purpose in that they allow retail investors to have access to less liquid securities and markets that may not be appropriate for a mutual fund. New rules that penalize Annual Redemption Funds will ultimately penalize ordinary investors by essentially making them bear the costs of the resulting loss of liquidity and lower trading value.

If the equity equivalent derivative provisions of the Proposed Amendments were applied to Annual Redemption Fund securities, the result would be an additional regulatory burden on Canadian banks and investment dealers who act as counterparties to cash settled TRS and CFD swaps and other derivatives contracts with investors seeking to leverage their positions. For reasons described above, the concerns identified in the Notice relating to these derivative instruments generally do not apply to Annual Redemption Funds. If unforeseen instances of abuse were ever to arise in the context of equity equivalent derivative transactions related to Annual Redemption Funds, the Commission could and should address those specific issues through the exercise of its public interest powers either through the issuance a cease trade order or by other means[3].

If you have any questions regarding the foregoing or would like to discuss the issues raised in this submission further, please feel free to call me.

Yours truly,

FASKEN MARTINEAU DuMOULIN LLP

David A. Hausman

DAH/mk

[3] *Re ARC Equity Management (Fund 4) Ltd.*, , 2009 ABASC 390