CASLA | Canadian Securities Lending Association

August 12, 2013

Via Electronic Submission

British Columbia Securities Commission
Alberta Securities Commission
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
Superintendent of Securities, Yukon Territory
Superintendent of Securities, Northwest Territories
Superintendent of Securities, Nunavut

Delivered to:

Anne-Marie Beaudoin, Corporate Secretary
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The Secretary
Ontario Securities Commission
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Dear Sirs/Mesdames:

RE: Proposed Amendments to National Instrument 81-102 *Mutual Funds* Companion Policy 81-102CP *Mutual Funds* and Related Consequential Amendments and Other Matters Concerning National Instrument 81-104 *Commodity Pools* and Securities Lending, Repurchases and Reverse Repurchases by Investment Funds (collectively, the "Proposals")

We are writing to provide comments on behalf of the members of The Canadian Securities Lending Association (CASLA) with respect to the specific questions relating to securities lending, repurchases and reverse repurchases by investment funds, set out in Annex C to the Proposals.

CASLA is an industry association, the members of which are Canadian banks, trust companies, other financial institutions, securities dealers and other professionals that are

leaders in the securities lending business. CASLA's members include CIBC Mellon, RBC Investor Services, Northern Trust, State Street Bank and Trust Company, BMO Capital Markets, Scotiabank, RBC Capital Markets, Société Générale Canada, National Bank Financial, Desjardins Financial and the Canadian Pension Plan Investment Board. Part of CASLA's mission is to work with regulators and other industry associations to ensure an efficient and secure marketplace for securities lending activities. CASLA advocates for the common interests of securities lending market participants, including custodian banks, beneficial owners, asset managers and broker-dealers.

We appreciate and support the CSA's efforts to enhance investors' understanding of the benefits, costs and risks of securities lending, repurchase and reverse repurchase transactions conducted by investment funds. For ease of reference, as applicable, we will refer to repurchase and reverse repurchase transactions, collectively, as "repo" transactions. This letter is written from the perspective of members' agency role in the securities lending market, and thus, our comments are directed primarily towards custodian banks that provide agency lending services to Canadian investment funds.

We would like to reiterate the importance of securities lending as a contributor to the efficient functioning of global securities markets. Participation in securities lending programs can be a valuable portfolio management tool for investment funds[1]. A well-managed securities lending program can provide additional income, which can offset the expenses associated with managing the investment fund without the addition of undue risk or liquidity concerns. As most of our members operate global businesses, we are aware of the recent international focus on securities lending and repo transactions and we are keen to share with the CSA and other regulatory authorities our members' ideas for modernizing the current Canadian regulations to keep pace with current market practices and global risk practices.

We believe that the disclosure requirements for securities lending and repo transactions in the current regulations are sufficient and requiring more granular financial disclosure or publicly disclosing the contractual arrangements, as suggested in the Proposals, would not provide further clarity to investors regarding an investment fund's securities lending and repo activities. For the reasons outlined below, we believe that investors would be better served by receiving more general information about the investment fund's securities lending and repo activities in the fund's prospectus or AIF.

As well, while we appreciate the CSA's efforts to increase transparency to investors of investment funds' securities lending and repo activities, generally, our members are opposed to the proposed public disclosure of agency lending agreements. These agreements are commercial agreements entered into between arm's length parties which often contain confidential business and financial information. It is our strong assertion that public disclosure of these agreements, in whole or in part, will not add value or provide further clarity to investors.

Under the existing regulations, unless a specific exemption is granted, the manager of an investment fund is required under National Instrument 81-102 ("NI 81-102") to appoint the investment fund's custodian or sub-custodian as its agent to administer the fund's securities lending and repo transactions. As well, the manager may (but is not required to) appoint an agent to administer the fund's reverse repo transactions. If an agent is appointed, then it

[1] In this letter we refer to mutual funds and closed-end funds collectively, as "investment funds" in anticipation of the amendments to NI 81-102 proposed in the Proposals.

has to be the investment fund's custodian or sub-custodian. Further, NI 81-102 also requires the agent to be contractually responsible for providing the fund and the manager regular, comprehensive and timely reports summarizing the fund's securities lending, repo and reverse repo transactions, as applicable. As outlined in the Proposals, these requirements will apply to closed-end funds once the proposed amendments to NI 81-102 come into force.

The depth of CASLA membership is evidence that the Canadian securities lending market is not a monopoly and fund managers have many options in choosing an agent lender. To meet client requirements and remain competitive, agent lenders provide a great deal of transparency to managers regarding the costs, risks and benefits of securities lending and repo activities and also offer comprehensive and customized reporting beyond what is required by the regulations. As a standard practice, managers receive reports from their agent lenders, on at least a monthly basis, showing the value of investment fund's outstanding loans, collateral values, securities borrowers, borrowing fees/rebates, withholding taxes, revenues and agency fees and returns on reinvestment of cash collateral (where applicable). Additionally, agent lenders are moving towards providing greater transparency in reporting using aggregated data providers to give fund managers a better idea of how their funds' performance compares to that of similar funds in their peer group.

In respect of financial disclosure, we believe that the current provisions of Part 3 of National Instrument 81-106 provide for sufficient disclosure of the revenue and costs of securities lending transactions in an investment fund's financial statements. The interests of investors would be better served by expanding the general disclosure of the risks and returns in the investment fund's prospectus or AIF, including the relevant protections and remedies available to the investment fund under the agency lending agreement (e.g. agent's standard of care and indemnification for borrower default). For example, investors should be aware of the additional risks and exposure to the investment fund if the fund accepts cash collateral.

Regarding the conflict of interest question raised by the CSA, conflict of interest between the fund manager and the agent would be rare where the agent is the investment fund's custodian or sub-custodian, but may arise in exceptional cases where a fund manager is administering the investment fund's securities lending and/or repo activities under a regulatory exemption. Therefore, if the CSA believes that that this disclosure is necessary, then the CSA should consult with the relevant stakeholders to ensure that the disclosure obligations are limited to situations where conflict of interest is an actual concern in order to avoid overburdening market participants, generally.

We suggest that the CSA may want to consider the general approach taken by the European Securities Markets Authority ("ESMA") to address transparency concerns in the European securities lending and repo markets rather than the more detailed disclosures suggested in the in Annex C to the Proposals. ESMA recently issued guidelines (the "ESMA Guidelines") containing enhanced disclosure requirements for UCITS funds that engage in securities lending. Most notably, the ESMA Guidelines were issued in the context of increasing transparency in respect of exchange-traded funds (similar to the Proposals). However, with regards to the method and content of disclosure, the ESMA guidelines require general disclosure in the fund's prospectus and information documents, which is comparatively more general and subjective than the prescriptive disclosure proposed in Annex C to the Proposals.

As the regulatory reform process continues, CASLA would welcome further dialogue with the CSA and other regulatory authorities regarding the securities lending and repo markets in Canada so that we can work together to ensure that your objectives are met through integration within current regulatory and market practice frameworks without imposing additional material burdens on securities lending agency activities or otherwise affecting market liquidity. We have a keen interest in making securities lending and repo activities more understandable for investors and we look forward to continued engagement with the CSA to achieve this objective.

We thank you for taking our comments into consideration and would be pleased to discuss these issues further at your convenience.

Sincerely,

Rob Ferguson,
President