FAIRCOURT
Asset Management Inc.

Delivered By Email: comments@osc.gov.on.ca, consultation-en-cours@lautorite.qc.ca

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
Registrar of Securities, Prince Edward Island
Nova Scotia Securities Commission
Superintendent of Securities, Newfoundland and Labrador
Superintendent of Securities, Northwest Territories
Superintendent of Securities, Yukon
Superintendent of Securities, Nunavut

Attention:

The Secretary
Ontario Securities Commission
20 Queen Street West
19th Floor, Box 55
Toronto, ON M5H 3S8

Me Anne-Marie Beaudoin
Corporate Secretary
Autorité des marchés financiers
800, square Victoria, 22e étage
C.P. 246, Tour de la Bourse
Montréal (Québec) H4Z 1G3

Dear Sirs/Mesdames:

Faircourt Asset Management Inc. is pleased to respond to the Canadian Securities Administrators' (CSA's) Notice and Request for Comment, released on March 27, 2013 and titled, 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 (the Proposed Amendments) and to the additional elaboration of CSA Staff Notice 11-324, dated June 25, 2013. The following provides a summary of our recommendations and comments.

While Faircourt supports efforts to modernize regulation we would like to bring your attention to certain areas where we believe the CSA proposals need further review.

To summarize, we are concerned that the proposed amendments:

- Proceed from what we believe to an incorrect premise that closed-end funds and open ended funds should be subject to the same regulation given their fundamental differences in formation, issuance, and distribution.
- Do not take into account the current rigorous process in place for closed-end fund issuance and in particular the enormous disclosure differences between a long form prospectus filed by a closed-end fund and the simplified prospectus filed by a mutual fund.
- Do not clearly define the perceived problem that the proposals seek to address.
- Were issued with little advance notice despite being of considerable scope in terms of their effect on the marketplace.
- Will result in less choice and flexibility for Canadian investors.
- Have not given due consideration to cost benefit analysis.

SPECIFIC QUESTIONS OF THE CSA RELATING TO THE PROPOSED 81-102 AMENDMENTS

Annual Redemptions of Securities Based on NAV

1. *Securities legislation defines a "mutual fund" as, among other things, an issuer whose securities entitle the holder to receive on demand, or within a specified period after demand, an amount computed by reference to the value of a proportionate interest of the net assets of the issuer.*

The CSA have historically taken the view that "on demand, or within a specified period after demand" in the definition of "mutual fund" means that the securities of the fund entitle the holders to request that their securities be redeemed by the fund more frequently than once a year. This view has permitted investment funds to redeem their securities once a year based on their NAV and still be considered non-redeemable investment funds. We seek feedback on whether the CSA should reconsider its present view and consider an investment fund to be a mutual fund if it offers any redemptions based on NAV.

We believe that the current CSA view, which regards funds that have annual redemptions not to be investment funds to be correct and that the CSA does not need to reconsider this view. Closed-end funds (including those with annual redemptions) are formed and distributed in fundamentally different ways from traditional open end mutual funds. The CSA should provide a clear definition to provide greater certainty.

Conventional mutual funds are distributed using simplified prospectuses whereas closed-end funds file a long-form prospectus. Long-form prospectuses are far more detailed than a short form prospectus. They include extensive general business and financial information about the company; detailed terms regarding the securities offered and the intended use of proceeds; and risk factors related to the purchase of the securities. Closed-end fund prospectuses also include detailed information on investment strategy and investment restrictions.

Not only is the actual prospectus document different for closed-end funds, the process leading up to and following obtaining regulatory approval for closed-end funds is more rigorous and involved than for mutual funds.

Prior to syndication, the lead agent extensively reviews the potential fund including historical returns, volatility, worst-case drawdown, comparisons with benchmark indices, etc.; tax., structural and other risks; manager assets under management, experience in managing the proposed strategy, etc. In the syndication phase, the lead agent invites to join the syndicate of dealers. Those invited to participate in the syndicate are given the opportunity, through a formal due diligence meeting, to question all aspects of the proposed fund including use of leverage, derivatives, short-selling, currency hedging, redemption features, management fees and other terms particular to different closed-end funds before agreeing to participate. In addition, the prospectus is prepared with the assistance of external securities counsel (typically separate counsel for both the issuer and the dealers) and subject to rigorous due diligence by the dealers and their counsel.

Once in distribution, closed-end funds are subject to further scrutiny by investment dealers to ensure that they are being sold to appropriate clients. IIROC-regulated dealers offering closed-end funds, and the dealers and advisors engaged in making these closed-end funds available to clients are subject to multi-level regulatory requirements. IIROC-regulated dealers have the requisite proficiency to distribute all closed-end funds.

Investment Restrictions

Concentration Restriction

2. *Do you agree with the 10% issuer concentration restriction for non-redeemable investment funds set out in proposed amended section 2.1 of NI 81-102? If not, please provide reasons why non-redeemable investment funds should be permitted to have a higher concentration limit, and how non-redeemable investment funds would benefit from a higher limit. Please also propose a higher limit and provide reasons for the limit.*

   If NI 81-102 provides for a concentration limit that is greater than 10% for non-redeemable investment funds, should NI 81-104 provide an even higher concentration limit for non-redeemable investment funds that are alternative funds subject to NI 81-104? Or should the concentration limits be the same for non-redeemable investment funds in both NI 81-102 and NI 81-104? We invite feedback on the appropriate balance of the concentration limit in NI 81-102 for non-redeemable investment funds and the concentration limit for non-redeemable investment funds under the alternative funds framework in NI 81-104.

We do not agree that a concentration restriction is required or appropriate for non-redeemable investment funds. Investors and their advisors are provided with extensive disclosure on the investment strategy and restrictions in the long form prospectus and can make an informed judgment regarding whether the particular fund's investment strategy is appropriate for their (or their clients) needs.

As one simple example, we also point out that it is not uncommon for indices to have components with a greater than 10% weighting. Where these indices are used as benchmarks for particular funds, the benchmark performance would no longer be replicable by the fund.

Investments in Illiquid Assets

3. *As non-redeemable investment funds do not redeem their securities regularly based on NAV, the CSA propose that they be permitted to purchase and hold more illiquid assets than the levels currently permitted by subsections 2.4(1) to (3) of NI 81-102.*

However, we are concerned that a portfolio containing a significant amount of illiquid assets could lead to difficulties in valuing the NAV of the fund. It is critical that the NAV of an investment fund be accurately valued; for example, non-redeemable investment funds typically pay management and other fees based on the NAV of the fund, NAV is used to measure performance, and many non-redeemable investment funds offer annual redemptions based on NAV.

We have observed that many non-redeemable investment funds do not invest in a substantial amount of illiquid assets; in fact, the majority of non-redeemable investment funds, like mutual funds, hold minimal amounts of illiquid assets. Would the ability to purchase and hold more illiquid assets than the levels currently permitted by subsections 2.4(1) to (3) of NI 81-102 be beneficial for non-redeemable investment funds? What types of illiquid assets do non-redeemable investment funds wish to invest in, and why?

The CSA invite comment on the amount of illiquid assets that would be appropriate for non-redeemable investment funds to purchase and hold, and whether non-redeemable investment funds should be given more time than 90 days to divest illiquid assets (please refer to the mutual fund divestment requirements in subsections 2.4(2) and (3) of NI 81-102). Is there a minimum amount of liquid assets that non-redeemable investment funds should be required to hold to meet ongoing liquidity needs (e.g., to pay management fees and operational expenses)? Should the limit on illiquid asset investments be different for nonredeemable investment funds that do not offer any redemptions and non-redeemable investment funds that offer annual redemptions?

Additional rules may be of questionable benefit. As the CSA has observed "….the majority of non-redeemable investment funds, like mutual funds, hold minimal amounts of illiquid assets". We believe that this demonstrates that market discipline is working effectively – investors desire annual redemptions, and as a result, many funds limit their illiquid asset exposure. However, there are some asset classes and investment strategies that require higher levels of illiquid assets, so imposing an arbitrary limit will reduce investor choice.

Borrowing

4. *We seek comment on whether the proposed requirement for non-redeemable investment funds to borrow from a "Canadian financial institution" is appropriate. For example, if the majority of an investment fund's assets are held outside Canada because it focuses on investing in foreign securities, should there be more flexibility to borrow from lenders other than those that are "Canadian financial institutions"? If so, what conditions should the other lenders have to meet?*

We believe that closed-end funds should be free to borrow from any regulated financial entity. Many funds invest in securities outside Canada - it is difficult to see how the Canadian investor would be served by this restriction.

Organizational Costs of New Non-Redeemable Investment Funds

5. *We seek comment on the impact and the benefits and costs of proposed subsection 3.3(3) of NI 81-102. Are there other parameters that could be developed that would achieve benefits similar to the benefits from proposed subsection 3.3(3)? Please also comment on whether the capital raising model followed by non-redeemable investment funds could support the payment of some of the organizational costs out of the proceeds of the initial public offering. Are there specific components of organizational costs that are more appropriately borne by the non-redeemable investment fund and components that are more appropriately borne by the manager? Please provide information about these cost components and what fraction each component typically constitutes of the total organizational costs for launching a new fund, and explain why it is appropriate for the fund or the manager to pay the specific cost components.*

The vast majority of organizational costs of a closed-end fund consist of legal and regulatory expenses. This includes issuer counsel, agent (underwriter) counsel, securities commission filing fees, stock exchange listing fees, audit fees, prospectus printing expenses and translation fees. Although the amount of these expenses may vary from fund to fund depending on complexity, none of these fees are discretionary. While the costs of organizing a closed-end fund are significant, it is important to consider that as a result of this process, the investor is receiving a robust long form prospectus and a fund that has been through a rigorous vetting process and the fees are clearly disclosed.

We believe that these organizational costs may be passed on to investors in other ways if they cannot be recovered up front. Higher management fees and the introduction of deferred sales charges are both possibilities. An unintended consequence of this proposal is that securities commissions may end up regulating fees and pricing.

To the extent these proposals were meant to deal with conversions to open ended mutual funds, we believe rules dealing with this specific issue would be more appropriate.

Transition Period for Investment Restrictions in Proposed Amended NI 81-102 and Alternatives

6. *We are proposing that existing non-redeemable investment funds be required to comply with the investment restrictions in proposed amended sections 2.2, 2.3,1 2.4 and 2.5 of NI 81-102 18 months after the first coming-into-force date of the Proposed 81-102 Amendments pertaining to these sections. We invite feedback on whether the proposed transition period is sufficient. If not, please provide reasons for a longer transition period or provide alternatives to a transition period.*

   If you think that a grandfathering provision is warranted for existing non-redeemable investment funds, please comment on the scope of a grandfathering provision and explain why existing non-redeemable investment funds should not have to comply with specific sections in Part 2 of NI 81-102. Please also comment on the impact a grandfathering provision could have on fairness to new market participants and investor understanding.

We disagree with the changes proposed, but with respect to the transitional period, we believe that full grandfathering is vitally important, should the amendments be enacted.

Investors purchased each closed-end fund currently in the market based on the investment strategy in the prospectus. We do not believe that it is fair or appropriate for the rules to be changed retroactively such that the fund's investment strategy can no longer be implemented. It is difficult to see how this is in the best interest of investors or consistent with the investor protection objectives of securities law. If investors want to exit a fund that is grandfathered, they can so by voting with their feet – they are free to sell into the market or redeem their securities.

Dilutive Issuances of Securities

7. *The CSA propose to introduce subsection 9.3(2) to prevent issuances of securities that cause dilution to the NAV of other outstanding securities of a non-redeemable investment fund. Proposed subsection 9.3(3) recognizes that a non-redeemable investment fund that raises additional money from the public through a new issuance of securities must include the price of the securities in the prospectus. We invite comment on whether proposed subsections 9.3(2) and (3) achieve the purpose of preventing dilutive issuances while taking into account how new securities are distributed.*

Unlike open-ended mutual funds, closed-end funds have defined periods for capital raising. As many funds offer annual redemptions, over time funds will naturally lose assets. The resulting smaller fund size can impact investors through higher expenses (as the funds expenses are spread over a smaller asset base) and can also reduce liquidity in the fund's trading. We are concerned that a blanket prohibition against warrants, rights and other potentially dilutive offerings will remove one of the least costly methods of raising additional capital for closed-end funds. The costs of dilution need to be considered in relation to the benefits of a larger asset base. We believe that the matter should be left to market practice.

Anticipated Costs of the Proposed Amendments and of Implementing the Alternative Funds Framework

8. *Do you agree or disagree that the costs of the Proposed Amendments and the proposals relating to NI 81-104 are proportionate to the benefits? We seek specific data from non-redeemable investment funds and commodity pools on the anticipated costs and benefits of complying with the regulatory framework set out in the proposed amendments to NI 81-102 and the alternative funds regulatory framework being contemplated in NI 81-104.*

Based on the information available to date, we do not agree that the costs of the Proposed Amendments are proportional to the benefits and we encourage the CSA to seek additional detail on cost benefit considerations.

Sincerely,

Faircourt Asset Management Inc.