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August 23, 2013

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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, Department of Justice and Public Safety,
Prince Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
Superintendent of Securities, Northwest Territories
Superintendent of Securities, Yukon
Superintendent of Securities, Nunavut

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SENT VIA EMAIL

Re: Staff Notice and Request for Comment 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 ("the Notice")

Morgan Meighen & Associates Limited ("MMA" or "we"), appreciates the opportunity to submit comments with respect to the Notice. Our comments are generally restricted to the reduced scope provided for in CSA Staff Notice 11-324, which also extended the comment period.

By way of background, MMA is registered as portfolio manager and exempt market dealer in the provinces of Ontario, Alberta, British Columbia and Manitoba. We are also registered as an investment fund manager in the province of Ontario. MMA has approximately $1.2 billion in assets under management. We have a broad base of clients, including individual and institutional private clients, as well as pooled funds, for which we carry out activities under our portfolio manager, exempt market dealer and investment fund manager registrations, as applicable.

Of particular relevance to the Notice is the fact that we currently manage two TSX-listed closed-end investment funds. To provide some additional context to our responses, these funds are "traditional" closed-end funds, which do not offer redemption privileges, at any time, to shareholders, or have a future "wind-up" date. One of these funds, Canadian General Investments, Limited ("CGI"), has been in existence for over eighty years, also carries a listing on the London Stock Exchange and has two series of TSX-listed preferred shares outstanding. Preferred shares have been used by CGI since 1998 as part of a leveraging strategy in an effort to enhance returns to common shareholders.

We would like to acknowledge that we are supportive of the proposed amendments related to:

- Conflict of interest provisions (Part 4 of NI 81-102);
- Securityholder and regulatory approval requirements for fundamental changes to non-redeemable investment funds and their management (Part 5 of NI 81-102);
- Custodianship requirements (Part 6 of NI 81-102).

These would all seem to be fundamental protections that should be available to investors in all investment funds. We suspect that most, if not all, non-redeemable investment funds are substantially in compliance of the proposed amendments to these sections already, but they should be codified for consistency.

The response letter from the Investment Industry Association of Canada dated August 2, 2013 provides a very good description of the background of closed-end funds and their differences from conventional mutual funds, particularly with respect to their organization and method of distribution that should support some differences in certain regulations from conventional mutual funds.

With respect to the specific questions of the CSA, we have comments on the following issues:

Annex A – Specific Questions of the CSA Relating to the Proposed 81-102 Amendments

Investment Restrictions

Investments in Illiquid Assets

Historically, the ability to invest in less liquid investments has been one of the primary benefits of the closed-end fund structure over that of a mutual fund. Illiquid investments, whether unlisted or thinly traded, can be undervalued by the market as a result of their illiquid nature, providing an opportunity for the fund to earn a higher return, particularly over the longer term. Specific examples would be a private company eventually going public, a closely-held company buying in shares held by outside shareholders, or similar special situation.

Liquidity needs of closed-end fund shareholders, each of whom has different requirements or expectations, are handled directly by the shareholders themselves, selling or buying their shares of the fund through a broker or dealer. With infrequent redemptions to worry about, or in our case where there are no redemptions, cash flows are limited primarily to dividend payments, management fees, operating expenses, and tax instalments, which are relatively easy to forecast.

As every investment fund is unique, in our view, with respect to illiquid investments no single specific limit (or limits – one for redeemable funds and one for non-redeemable funds) should be mandated. Whether a fund is redeemable or non-redeemable, the manager of the fund, acting under the oversight of the fund's board of directors or trustees, is in the best position to evaluate a fund's own liquidity needs and, in the normal course of conducting prudent portfolio management practices, determine the appropriate level of illiquid assets that may be held. This determination will be driven by such factors as the frequency of redemptions, other cash flow needs, investment mandate, market conditions, outlook for different asset classes and so on. Shareholders and other interested parties are already provided information enabling them to evaluate a fund's liquidity risk and what is being done to manage that risk by reading through the notes to a fund's financial statements as this is required disclosure under current accounting guidelines.

Fund-of-Fund Structures

The proposed amendments would prevent non-redeemable investment funds from investing in other non-redeemable investment funds. The rationale provided for this restriction is to avoid the fund achieving a greater amount of leverage than deemed desirable by the CSA. Since CSA Staff Notice 11-324 contemplates that investment restrictions and parameters related to borrowing cash will be considered later given the interrelationship with the alternative funds proposals, we suggest that it would be most appropriate to defer this particular restriction and consider it in conjunction with decisions on bank borrowings and leverage.

However, we would like to point out that there are other legitimate reasons for a non-redeemable investment fund to choose to invest in a non-redeemable investment fund other than to circumvent leverage limits. For example, closed-end investment funds frequently trade at a substantial discount to their underlying net asset value. Investing in a closed-end fund when the discount is high and subsequently selling when the discount is lower will result in a greater return than the underlying net asset value return of that fund and its security holders. If the CSA's concern is specific to leverage, we do not believe that an outright restriction on investments in non-redeemable investment funds is the best method to address that concern. Such a restriction would, for example, prevent a non-redeemable investment fund employing no leverage at the fund level, from holding a position in another non-redeemable investment fund thus limiting the investment options for the security holders.

Naming Convention for Investment Funds

We do not feel that requiring specific identifiers, such as "Alternative Fund" or "Conventional Fund" in the name of an investment fund would be a useful exercise. There will undoubtedly be a broad range of funds governed by either NI 81-102 or proposed NI 81-104. In our view, it is likely that an identifier of "Alternative Fund" would carry negative connotations, implying a higher level of risk for an investment fund relative to a fund that does not, when this is not necessarily the case.

Securities Lending

While we are in support of enhanced disclosure with respect to securities lending, we do not believe that requiring presentation of the gross revenues in the financial statements, together with the fee paid to the agent as an expense and, therefore, included in the management expense ratio or trading expense ratio serves a useful purpose or will result in a desirable effect. With securities lending, collateral, generally comprising Canadian or provincial government-guaranteed securities, that exceeds the amount of the securities lent out is held by the agent. Further, in the event any loaned securities are not returned to the fund and the value of the collateral held is less than the value of the securities not returned, the agent indemnifies the fund for any shortfall. Despite the fund, and its shareholders, benefitting from securities lending with little risk, required inclusion of the agent expenses in the management expense ratio, a number scrutinized by many investors, could have the effect of prompting some investment funds from discontinuing this practice, a result that is not in the fund's investors' best interests. We believe that the net proceeds of securities lending activities is more valuable information for security holders.

Borrowing and Leverage

Although CSA Staff Notice 11-324 issued on June 25, 2013 reduces the scope somewhat from the initial Notice issued on March 27, 2013, excluding a request for comments for investment restrictions related to "borrowing cash", we felt it was important to bring issues related to borrowing and leverage to the fore, so they are considered by the CSA prior to the issuance of further proposals in these areas.

It is difficult to tell exactly what constitutes "borrowing cash" with respect to the proposed amendments. For example, in the case of CGI, the preferred shares it has outstanding, both with ten year terms, constitute leverage, but it is not clear why or if they should be caught in the proposed regulations. There are many split-share corporations that may also be affected by the proposals as written.

Judging from the commentary in the Notice, the proposals seem to be designed primarily to steer investment funds creating leverage through traditional loans towards an acceptable Canadian financial institution, or investment funds creating leverage through specified derivatives or short selling towards the new "alternative funds" framework. Any concerns over the use of other forms of leverage, primarily bonds or preferred shares, if there are any, are not explicitly expressed.

However, in the discussion on related consequential amendments to NI 41-101 and Form 41-

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101F2 it states that "...non-redeemable investment funds would not be permitted to issue debt securities to the public". The CSA offers little support as to its reasons for requiring "bank borrowings" to take on a specific form only (i.e., a traditional bank loan), as opposed to issuing bonds or preferred shares. Issuers who are investment funds should be able to consider all forms of leverage that are available to them and select the form that is most beneficial to its structure and its shareholders. In making this determination, considerations include such factors as cost, collateral, term and taxation.

We hope that the CSA's views in the areas of borrowing and leverage will be clarified.

If you should have any questions, or require further information, please do not hesitate to contact me.

Yours truly,

Frank Fuernkranz
Vice-President Finance & Secretary