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December 21, 2016

British Columbia Securities Commission
Alberta Securities Commission
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
Financial and Consumers Services Commission, New Brunswick
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
Registrar of Securities, Northwest Territories
Registrar of Securities, Yukon Territory
Superintendent of Securities, Nunavut

The Secretary
Ontario Securities Commission
20 Queen Street West
22nd Floor
Toronto, Ontario M5H 3S8
Fax: 416-593-2318
Email: comments@osc.gov.on.ca

Dear Sirs/Mesdames:

RE: Canadian Securities Administrators ("CSA") Request for Comment – Modernization of Investment Fund Product Regulation – Alternative Funds (the "Proposed Amendments")

RP Investment Advisors ("RPIA") is a specialized, credit focused, alternative fixed income investment management firm that is registered as an Investment Fund Manager, Portfolio Manager and Exempt Market Dealer in multiple Canadian jurisdictions. RPIA is located in Toronto, Ontario and our principle regulator is the Ontario Securities Commission. We actively participate in the global fixed income market and currently manage over C$3.0 billion in assets, primarily on behalf of Canadian investors.

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RPIA is strong supporter of the CSA's endeavor to modernize the Canadian investment fund landscape, and particularly with regards to the role of alternative funds. Institutional and other sophisticated investors have, for some time now, been utilizing alternative investment strategies within their overall portfolios to help provide diversification, and to gain exposure to certain risk and return profiles that generically are not achievable through more traditional investments. We congratulate the CSA's efforts to ensure that the opportunities presented by alternative investments is made available to a broader range of Canadian investors. We truly believe in the value alternative strategies can provide as part of well diversified investor portfolios.

Notwithstanding our overwhelming support for the direction of the Proposed Amendments, we are of the view that certain aspects of the proposals should be reviewed and possibly reconsidered. We believe that these would positively contribute to the goal of providing Canadian investors with access to innovative alternative strategies, that if implemented appropriately, would complement their existing investment portfolios, and assist them in reaching their own investment objectives. Both from a performance and risk management perspective. We appreciate the opportunity to provide our thoughts and comments on this important regulatory initiative and will be pleased to provide additional information or participate in industry discussions as deemed appropriate by the CSA.

The purpose of this letter is to provide the CSA with comments regarding certain aspects of the Proposed Amendments. RPIA is a member of the Canadian section of the Alternative Investment Management Association ("AIMA Canada") and we would like to convey that we are generally in support of the views and comments of AIMA Canada, as they relate to the Proposed Amendments. As such, RPIA's comments may, where appropriate, directly or indirectly reference those expressed by AIMA Canada in their own comment letter. We note that where appropriate, we may also provide additional thoughts and comments of our own, that may not necessarily be reflected by those of AIMA Canada.

For the purpose of this letter, RPIA will directly address select questions posed by the CSA, followed by relevant supplementary comments.

Part 1 - CSA Questions

Question 5

Should we consider how frequently an alternative fund accepts redemptions in considering an appropriate illiquid asset limit? If so, please be specific. We also seek feedback regarding whether any specific measures to mitigate the liquidity risk should be considered in those cases.

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Response

In the absence of specific redemption frequency requirements in the Proposed Amendments, RPIA would like to echo the views expressed by AIMA Canada, as detailed in their comment letter. We request that the CSA therefore consider the operational complexities and additional costs that could exist under a regime where the required frequency of NAV calculation, required purchase/redemption NAV (i.e. next NAV, or first or second business day following the purchase/redemption request) does not align with the purchase/redemption frequency set by the fund. As noted by AIMA Canada, an alternative fund that offers monthly purchases/redemptions, may need to execute these at up to 30 different NAVs on a single transactional day. This could result in severe operational difficulties, especially for smaller firms.

Question 8

Should alternative funds and non-redeemable investment funds be permitted to borrow from entities other than those that meet the definition of a custodian for investment fund assets in Canada? Will this requirement unduly limit the access to borrowing for investment funds? If so, please explain why.

Response

Under the Proposed Amendments, alternative funds would only be permitted to borrow cash from entities that qualify as investment fund custodians under Section 6.2 of NI 81-102, and it is RPIA's belief that this requirement would restrict borrowing for many alternative funds. We align our views with that of AIMA Canada and would like to highlight the following comments.

RPIA acknowledges that the Proposed Amendments are intended to permit an alternative fund to borrow from entities acting as prime brokers in Canada. However, we would like to highlight a specific concern with the requirement that all such lenders must qualify as a custodian under Section 6.2 of NI 81-102. As per the requirement, the equity of most bank affiliated dealers that provide prime brokerage services exceed the minimum $10,000,000. However, they generally do not prepare separate audited financial statements that are made public, as required by subsection 3(a). For the purpose of permitting an alternative fund to borrow from prime brokers in Canada, we agree with the comments of AIMA Canada, in that the CSA consider removing the requirement under Section 6.2(3)(a) that requires that a dealer's financial statements be made public. We would like to note that this would be in line with the definition of "Canadian Custodian" in the recently proposes amendments to NI 31-103.

The ability to borrow funds is crucial to many alternative fund strategies, and based on the circumstance, the efficiency and terms of loans could potentially be improved by borrowing from foreign lenders. For example, borrowing U.S. dollars from a U.S. domiciled lender in order to finance the purchase of U.S. dollar denominated securities. RPIA believes that it would be in the interest of alternative funds and investors alike

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to permit borrowing from certain foreign entities. We note that NI 81-102 currently permits qualified foreign entities to act as sub-custodians for investment fund assets held outside of Canada. To facilitate a practice whereby an alternative fund can obtain efficient and effective sources of funding, we propose that the CSA expand the scope of the current rule proposal to permit borrowing from foreign entities that are permitted to act as sub-custodians under Section 6.3 of NI 81-102.

Lastly, RPIA also agrees with the comments provided by AIMA Canada that the proposed borrowing limit of 50% of NAV should be calculated net of cash and cash equivalents that are held in the same account with the lender.

Question 10

The method for calculating total leverage proposed under the Proposed Amendments contemplates measuring the aggregate notional amount under a fund's use of specified derivatives. Should we consider allowing a fund to include offsetting or hedging transactions to reduce its calculated leveraged exposure? Should we exclude certain types of specified derivatives that generally are not expected to help create leverage? If so, does the current definition of "hedging" adequately describe the types of transactions that can reasonably be seen as reducing a fund's net exposure to leverage?

Response

RPIA strongly believes that specified derivatives that are used for hedging purposes should be excluded from the proposed leverage calculation. We agree that the current NI 81-102 definition of "hedging" adequately described transactions that are considered to be for hedging purposes, and are not proposing that the definition be amended.

Implementing hedging strategies forms part of the foundation of many alternative investment strategies and do not, in our view, contribute to the leverage or magnify the risk of a portfolio. In this sense, hedging is viewed and used as a risk-mitigating tool, and including the notional value of derivatives used for this purpose in the leverage calculation, will not provide investors with an accurate and transparent understanding of the risks that might be associated with an alternative fund.

We acknowledge previous CSA comments that note that hedging transactions do not necessarily fully offset the risk of any particular position and disregarding the notional value of all hedging transactions from the calculation of aggregate gross exposure may misstate a fund's true leverage position. We do however, want to respectfully emphasize the crucial role that hedging could play in mitigating certain risks within an alternative fund.

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As an alternative fixed-income manager focused on global credit securities, we are of the view that hedging against interest rate risk and foreign currency exposure is a valuable and necessary tool. A tool that can be effectively implemented to reduce risk within a credit focused portfolio, protect investor capital and ultimately allow a fund to pursue its stated investment objectives and deliver value to investors. Fixed-income securities are inherently exposed to interest rate risk. Using derivatives for hedging purposes allows managers like us to effectively minimize volatility associated with interest rate fluctuations, while focusing on building, what we feel, are optimal credit-focused portfolios for our investors. In our opinion, this results in a truly alternative asset class that compliments investment portfolios and we strongly feel that this supports the consensus views on the value of alternative funds as part of well diversified investor portfolios.

As noted, the importance of hedging is strongly echoed as it pertains to foreign currency investments. Many alternative funds hold securities denominated in foreign currencies, but maintain an objective to deliver optimal risk-adjusted returns to investors in the fund's local currency. Currency fluctuations can have a severely detrimental impact on investor returns, especially those invested in fixed-income securities, and many alternative managers disclose that they will employ currency hedging to help offset this risk. This could be an important consideration for certain investors and could impact their investment decision to invest in a particular fund, based on their own investment objectives.

In addition to the use of specified derivatives for hedging purposes, RPIA would like to highlight, the crucial importance of using short selling strategies for hedging. Interest rate risk, as discussed above, is a fundamental risk faced by fixed-income funds and alternative managers who provide investors with credit focused alternatives, and who commonly utilize short selling as an effective and efficient approach to hedging against interest rate risk. A primary example of this is a strategy whereby a manager invests in an investment grade corporate fixed-income security while simultaneously entering into a short sale of a corresponding and highly liquid government security, such as Canadian or U.S. government issues. A negative change in market value of the long position due to rising interest rates, for example, would be offset by a positive change in market value of the short position. This strategy makes it possible for a credit focused manager to effectively hedge against interest rate risk across a fixed-income portfolio and often without the need to make large scale use of the derivatives market. We note that the government securities sold short under such a strategy represent, what is widely considered to be some of the most liquid and least volatile investments available. Of note is that the use of this type of short selling strategy for hedging purposes supports our comments later in this letter pertaining to the issuer concentration restrictions related to short sales.

By aggregating the notional value of all short sales and derivative instruments for the purpose the leverage calculation, we feel that it not only provides the investor with an inaccurate view of the fund's use of leverage, and therefore the perceived risk, but restricts the fund from utilizing other true forms of leverage, such as borrowing and short selling for non-hedging purposes. This would curb the fund's ability to pursue optimal risk-adjusted returns for its investors.

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Based on our understanding of the Proposed Amendments, we would like to highlight that an alternative fund that intends to leverage its portfolio by borrowing up to a maximum permitted 50% of NAV, would not be able to employ short selling strategies or derivative instruments to effectively hedge its overall economic exposure against interest rate risk and foreign currency risk. If, for example, the fund fully invests the borrowed funds, along with the rest of its assets, in U.S. dollar denominated investment grade fixed-income securities, the nominal value of its economic exposure to interest rate risk and currency risk that would need to be hedged is magnified as a result of the leverage created by the borrowing. Aggregating the notional value of the required hedging instruments with the borrowing, will exceed the proposed permitted limit of 300% of NAV. In this scenario, a fund manager may need to prioritize the relative importance of interest rate risk vs. foreign currency risk and apply selective hedging. This approach could possibly be at odds with the fundamental investment objectives of a fund that states that it pursues a credit focused strategy that aims to fully hedge both interest rate risk and foreign currency risk. As an alternative, such a fund would have to largely abstain from borrowing, thereby restricting its ability to leverage the fund in order to pursue a certain risk adjusted return objective.

Given the myriad of alternative strategies and accompanying risk mitigation practices, we urge the CSA to consider, for the purpose of calculating the total leverage exposure of an alternative fund, excluding the value of those specified derivatives and short sales that are used for hedging purposes.

Question 11

We note that the proposed leverage calculation method has its limits and its applicability through different type of derivatives transactions may vary. We also acknowledge that the notional amount doesn't necessarily act as a measure of the potential risk exposure (e.g. interest rate swaps, credit default swaps) or is not a representative metric of the potential losses (e.g. short position on a futures), from leverage transactions. Are there leverage measurement methods that we should consider, that may better reflect the amount of and potential risk to a fund from leverage? If so, please explain and please consider how such methods would provide investors with a better understanding of the amount of leverage used.

Response

RPIA is of the view that an aggregate notional leverage limit does not provide investors with a fair and transparent view of the risks associated with leverage. We respectfully state that a risk based approach would result in a more relevant view and appropriate understanding of the risks facing alternative fund investors. A "one-size-fits-all" notional limit implies that the use of leverage results in the same level of risk to an investor, regardless of important contributing factors such as asset class risk and security specific risk. Investors are likely to view these risks in terms of the potential for capital losses related to a fund's use of leverage. The notion of leverage might be relatively unknown to many retail investors and can easily be misinterpreted and

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misunderstood in the absence of expert clarification. RPIA feels that it is vitally important to educate investors on the concept of leverage, and how risks associated with leveraged strategies can impact their overall investment risk profile, investment objectives and performance.

We note that risk can vary greatly between asset classes and between securities with differentiating characteristics. Applying leverage to these only magnifies this important distinction. In its simplified form, risk associated with leverage varies drastically, not only between asset classes such as equity and fixed-income, but between securities with varying characteristics. Examples of these could include fixed-income securities with different maturities and credit risk profiles. Leverage applied to investment grade fixed-income securities by nature would have a lower risk profile and potential for capital loss, than the same level of leverage applied to equities.

Other parts of the Canadian securities industry successfully apply risk based approaches to regulation and requirements. One prominent example of where a risk based approach is reflected, is in the investment dealer margin requirements prescribed by the Investment Industry Regulatory Organization of Canada ("IIROC"), in Rule 100 of the IIROC Dealer Member Rulebook. Although a discussion of these requirements go well beyond the scope of this letter, we would like to draw specific attention to the varying margin requirements that are based on the risks attributed to asset classes, security types and other security characteristics. For example, generally speaking, equities listed on an exchange in Canada or the U.S. for which margin is available (i.e. selling at $1.50 or more) require margin of between 50% and 80% of market value (excluding securities eligible for reduced margin). This can increase dramatically for securities listed in other countries, or for unlisted securities, and the margin requirement could represent multiples of the security's market value. This contrasts with fixed-income securities issued by the Canadian or U.S. governments that generally require margin of between 1% and 4% of market value. Additionally, prescribed margin requirements applicable to investment grade corporate fixed-income securities generically range between 3% and 10% of market value. We note that this example provides a very limited scope of the margin requirements under IIROC Rule 100. These requirements are subject to various conditions and can change or vary drastically depending on the nature of a security or the situation under which the margin requirements apply.

The rationale for referencing the IIROC margin requirements is to highlight the key importance of risk assessment in setting guidelines and restrictions. We realize that margin requirements do not, and should not necessarily form the basis of leverage restrictions for the purpose of the Proposed Amendments to NI 81-102, but we strongly and respectfully make the case that a "one-size-fits-all" notional limit is not appropriate and may not be in the best interest of investors. We urge the CSA to take these comments into consideration and to continue exploring risk based alternatives to setting leverage guidelines for alternative funds. RPIA will be pleased to contribute to any industry discussion that the CSA might see helpful in reviewing and assessing this material subject.

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RPIA would also like to draw attention to the view expressed by AIMA Canada that applying a nominal leverage limit is not appropriate, and that removing this limit would permit certain existing commodity pool funds to continue to operate, and very importantly, broaden the types of alternatives strategies available to retail investors. We would also support their recommendation that alternative funds be required, in the absence of an upper limit, to disclose their leverage and calculation methodology. An addition, RPIA agrees with AIMA Canada that there are multiple appropriate measure of leverage that can and should be used to address the variability of strategies across the alternative investment landscape.

Question 13

Are there any other changes to the form requirements for Fund Facts, in addition to or instead of those proposed under the Proposed Amendments that should be incorporated for alternative funds in order to more clearly distinguish them from conventional mutual funds? We encourage commenters to consider this question in conjunction with proposals to mandate a summary disclosure document for exchange-traded mutual funds outlined in the CSA Notice and Request for Comment published on June 18, 2015.

Response

RPIA appreciates the importance of appropriate and relevant disclosure in Fund Facts documents and generally support the views expressed by AIMA Canada regarding this matter.

Part 2 - Additional Comments

1. Short Selling

a. Overall Limit

The Proposed Amendments will permit an alternative fund to enter into short positions with an aggregate value of not more than 50% of the fund's NAV. RPIA feels that although the limit is a very positive increase from the 20% applicable to existing funds under NI 81-102, it falls short of permitting several alternative investment managers from implementing specific investment strategies. Many alternative fund strategies rely on short selling as hedging to reduce certain risks. A notable example, and one that is detailed in the AIMA Canada comment letter, applies to funds that employ a market-neutral strategy, whereby long and short positions are balanced with the aim to negate market risks, so to allow the fund to pursue absolute returns, regardless of general market fluctuations. These strategies are used by

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sophisticated and institutional investors alike and present certain valuable risk and return opportunities. In order to successfully employ such a strategy, funds must have the ability to have short positions of up to 100% of NAV.

A second example builds on our earlier comments in Question 10 as it pertains to the short selling of government issued fixed-income securities for hedging purposes. As noted, this practice can be employed as an efficient way to hedge a portfolio holding investment grade corporate fixed-income securities, from the risks associated with general interest rate fluctuations. As a result, we request that the CSA consider increasing the overall permitted limit of these types of short sales. RPIA views this approach to be appropriately aligned with alternative funds that follow market-neutral approach.

Lastly, a focus of some alternative funds is to exclusively employ short selling strategies to generate leverage, and thereby largely refrain from using derivatives for this purpose. We note that permitting an alternative fund to employ leverage of up to 300% of NAV, while restricting its ability to engage in short selling to a lower limit, would likely compel those managers to change their investment strategies by engaging in derivatives transaction to generate sufficient leverage. This practice could lead to increased operational costs and complexities for certain managers, and may, in some instances have the unintended consequence of increasing undue risks related to the derivatives market.

b. Concentration Restriction

We acknowledge that under Section 2.6.1 of NI 81-102, the Proposed Amendments will increase the aggregate market value all securities of a single issuer sold short, to 10% of NAV.

As discussed earlier in this letter, RPIA utilizes hedging strategies in its private alternative funds that make extensive use of short selling to hedge against interest rate risk within fixed-income portfolios. The strategy has proved to be an effective way of achieving this objective and often does not require extensive use of the derivatives market. In particular, these strategies largely consist of holding investment grade corporate fixed-income securities while short selling government issued fixed-income securities. Such a strategy would not be implementable given the 10% issuer concentration restriction and will in turn, result in increased use of the derivatives market to achieve the desired hedging results. This again could result in operational complexities and may lead to additional risk exposure related to the use of derivatives.

We note that "government securities" as defined in NI 81-102 are excluded from the concentration restriction in Section 2.1 of NI 81-102. This is understandable given the nature and risk profile of these securities, and we strongly urge that the CSA consider applying the same exemption to the issuer concentration limits as it pertains to short selling. These government securities generally exhibit

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characteristics that result in them being regarded as some of the lowest risk and highly liquid securities available, and we believe that the risks associated with maintaining short positions in these do not present undue risk to investors.

2. Custodianship of Portfolio Assets

RPIA supports the comment made by AIMA Canada with regards to custody related matters under Part 6 of NI 81-102. In particular, we reference their comments regarding the seemingly unintended consequences of the custodial provisions related to short sales (Section 6.8.1 of NI 81-102). These restrictions will reduce the practicality of implementing short selling strategies in line with the Proposed Amendments, since it will likely lead to excessive costs and operational complexities. Furthermore, given the limited number of borrowing agents available in Canada for this purpose, this requirement may prevent otherwise permitted short selling activities of alternative funds.

We note that the comments made by AIMA Canada with respect to permitting prime brokers to act as custodians of alternative funds is of crucial importance. It will materially improve the operational efficiencies of alternative fund managers and will also provide an effective solution to the short selling custody related concerns noted above.

3. Counterparty Exposure Limits

RPIA echoes the view of AIMA Canada with regards to the counterparty exposure limit of 10% under Section 2.7 of NI 81-102. We agree that it is not clear that there is any undue risk from being exposed to a qualified counterparty that maintains a designated credit rating, as required by NI 81-102. We further note that the counterparty exposure limit does not currently apply to commodity pool funds under NI 81-104, and we do not agree with the elimination of this exemption under the Proposed Amendments for the purpose of alternative funds.

Conclusion

RPIA strongly believes that introducing regulation which would permit retail investors to access alternative investment strategies is, without doubt, an encouraging development within the Canadian investment fund landscape. We truly feel that these strategies, if employed in a suitable and appropriate fashion, will have a positive impact on the risk adjusted performance of investor portfolios. We stress that investor education will be paramount to ensure a clear and appropriate understanding of the risks associated with various types of alternative strategies. We conclude by stating that alternative investment managers should be governed by appropriate regulations that will permit them to employ their often unique strategies. Only by providing

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alternative managers with the ability to apply and demonstrate their expertise and value, will Canadian retail investors truly have access to the same alternative strategies currently reserved for institutions and other select investors.

We once again congratulate the CSA for their ongoing efforts and would be pleased to provide additional comments on the views expressed in this letter, or partake in further discussion with the CSA on this important matter.

Sincerely,

Richard Pilosof
Managing Partner and Chief Executive Officer

Mike Quinn
Partner and Chief Investment Officer