December 22, 2016

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
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

In care of

The Secretary
Ontario Securities Commission
20 Queen Street West
19th Floor, Box 55
Toronto, Ontario 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:

RE: CSA Notice and Request for Comment - Modernization of Investment Fund Product Regulation – Alternative Funds ("CSA Notice")

We are providing comments on behalf of the Members of The Investment Funds Institute of Canada in response to the CSA Notice and the proposed Framework for Modernization of Investment Fund Product Regulation – Alternative Funds (collectively, the "Proposal").

General Comments

Our Members appreciate the additional flexibility that the Proposal will provide "conventional" mutual funds for investments in commodities and investments in certain underlying funds. Allowing alternative funds to be made available to retail investors provides increased investment choice and access to new investment opportunities for retail investors.

We suggest several additional changes to the investment restrictions for "conventional" mutual funds to provide greater flexibility to investors.

It makes sense to bring alternative funds within the general framework of NI 81-102 because most of the same regulatory regime for mutual funds in NI 81-102 will also apply to alternative funds. To clarify the different investment restrictions that will apply to each type of NI 81-102 fund we recommend that a summary of the different investment restrictions are included in the Companion Policy 81-102 CP. We attach as Appendix B a comparison of the differences prepared by Borden Ladner Gervais LLP for your consideration.

In this letter we provide general comments on the Proposal, and comments on issues not specifically addressed in the CSA's questions. In Appendix A we provide responses to most of the questions posed in Annex A to the CSA Notice, however we have not responded to those questions relating solely to non-redeemable funds.

We also understand that several of our Members will make their own submissions raising unique issues and requesting consideration of other changes to the investment restrictions discussed in the Proposal.

"Alternative Funds" Label

In the Summary of Comments portion of the CSA Notice, the CSA note that the term "alternative fund" will only apply to mutual funds, for descriptive purposes, to reflect that these funds are permitted to engage in certain strategies or to invest in asset classes that are not necessarily available to more "conventional" mutual funds. The CSA further confirm that they are not proposing any mandatory naming conventions or other labelling requirements and are proposing removal of the warning label currently applicable to commodity pools because they recognize that not all alternative funds or strategies are inherently riskier than a "conventional" mutual fund.

Consistent with the CSA's intent, it is important that the descriptive terms "alternative fund" and "conventional mutual fund" not become defined terms. We see these descriptive terms as being a convenient substitute for more accurate but overlong and cumbersome descriptions such as "mutual funds that are permitted to adopt strategies not necessarily available to more conventional mutual funds".

We recognize the challenge in identifying one- or two-word product-type labels that conveniently distinguish between fund types, but the risk of adopting these descriptive terms as defined terms based on a notion of comparability between such funds presupposes understanding about the types of funds being compared, and whether they may be "alternative", "more conventional" or even "traditional". Disclosure that reflects each product's specific characteristics is preferable to labels that rely on comparisons, and mandatory comparative disclosure with other products such as that the CSA have in mind in the Proposal.

We echo this concern in our comments regarding the proposed Point of Sale disclosure requirements for alternative funds.

Investment Restrictions for Alternative Funds:

Definition of "Illiquid Asset"

The definition of "illiquid asset" in NI 81-102 is problematic. A key element of the definition is that the portfolio asset "cannot be readily disposed of through market facilities on which public quotations in common use are widely available at an amount that at least approximates the amount at which the portfolio asset is valued in calculating the net asset value per security of the investment fund,…" [emphasis added] . Accordingly any asset that can be readily disposed of at such a value, but only through a market where there is no widely available public quotation - perhaps the security trades only in an institutional market to which portfolio managers have access - would automatically be deemed to be an illiquid asset. Defining an asset is illiquid because it trades on a market that lacks public, or widely available, quotations is too narrow. In the institutional context, securities that can be readily traded for their appropriate value on a

market that provides full pre-trade price transparency to all participants in that market, and that otherwise do not have the risks associated with truly "illiquid" securities, should meet the test for liquid assets.

We acknowledge that liquidity risk management goes beyond the Proposal, and that currently there are a number of initiatives internationally on liquidity risk management for investment fund products that the CSA are monitoring for potential impact on their work. We welcome further discussions with the CSA on this topic.

We understand that several of our Members will make submissions that raise unique issues and propose options with respect to the current definition of illiquid assets as it applies to their respective businesses.

Investments in Illiquid Assets

The Proposal imposes the same limit on investments in illiquid assets as applies currently to "conventional" mutual funds (10% of NAV at the time of purchase, with a hard cap of 15% of NAV). This contrasts with the 20% of NAV limit proposed for non-redeemable funds. We recommend the CSA consider adopting, for alternative fund investments in illiquid assets, a higher time of purchase limit, at least consistent with the 15% limit for mutual funds in the United States. In 1992 the U.S. Securities and Exchange Commission increased the permitted level of mutual fund investments in illiquid assets from 10% to 15% of NAV[1]. The rationale for allowing mutual funds to invest an additional 5% of their net assets in illiquid securities was to provide additional capital to small business without significantly increasing the risk to any fund. Assessing the experience of U.S. mutual funds since this limit was increased should provide evidence that a similar increase for alternative funds in Canada is unlikely to significantly increase the risk to these funds.

Borrowing

Proposed section 2.6(2) of NI 81-102 states that "An alternative fund or a non-redeemable investment fund may borrow cash in excess of the limits set out in subsection (1) provided that … (c) the borrowing agreement entered into is in accordance with normal industry practice and on standard commercial terms for the type of transaction." [emphasis added]. For greater clarity, we request confirmation that alternative and non-redeemable funds will be permitted to grant a security interest in their assets and/or give indemnities in respect of borrowing arrangements under 2.6(2), both of which are considered normal industry practices.

We also request a clarifying amendment to proposed section 2.6(2), specifically the portion that states "borrow cash in excess of the limits set out in subsection (1)…" The amendment should make more explicit how the existing 5% borrowing limit to settle portfolio transactions in subsection (1) will interact with the new 50% borrowing limit for borrowing for leverage.

Fund-of-Fund Structures

Although the Proposal permits "conventional" mutual funds to invest up to 10% of NAV in alternative funds and non-redeemable investment funds subject to NI 81-102, we recommend the CSA consider increasing this limit to 20% of NAV to provide investors access to more flexible alternative investment strategies.

We commend the CSA for codifying commonly-granted relief regarding investments in other mutual funds. We recommend that the CSA also consider codifying existing exemptive relief granted to a number of mutual funds permitting them to invest in ETFs traded on exchanges in jurisdictions outside of Canada (for example, U.S.-listed commodity-tracking ETFs). Consistent with the conditions that accompany those relief orders, the regulatory regime applicable to

[1] Revisions of Guidelines to Form N-1A, Federal Register, Vol. 57, 9828, 9829 (March 20, 1992).

those ETFs should be equivalent to those applicable to similar Canadian ETFs and the stock exchanges in those jurisdictions should be subject to equivalent regulatory oversight to securities exchanges in Canada.

Again in relation to commodity investments we request clarification on how the "look through" test for physical commodity investment limits relates to the underlying fund investment limit. It should be made clear whether a commodity ETF is included in the calculation set out in s. 2.3(3) and, if so, whether it is to be excluded from the underlying fund restrictions in s. 2.5.

Point-of-Sale Disclosure

In addition to our response to the CSA's specific questions on Fund Facts disclosure, we have comments on several aspects of the proposed disclosure requirements for alternative funds. We encourage the CSA to consult specifically on the content of the alternative fund point-of-sale disclosure documents, in particular the Fund Facts, once the substantive disclosure issues have been settled.

As we noted earlier, we concur with the CSA's decision not to mandate naming conventions or other labelling requirements for the various investment fund types, and to maintain phrases such as "alternative fund" and "conventional mutual fund" as descriptive terms and not as defined terms. This means that care must be taken to avoid the introduction of such descriptive terms into the point-of-sale documents as if they were defined terms. For example the proposal to require a text box in the Fund Facts that reads, in part: "This mutual fund is an alternative fund" uses the descriptive term as a defined term contrary to the CSA's intent to avoid labelling.

Our Members disagree with the proposal to require comparative disclosure in the point-of-sale documents. It is essential that the point-of-sale documents provide disclosure of the characteristics of the particular investment funds that are described in them. However mandating language in the disclosure documents that, for example, compares alternative funds with "conventional mutual funds" might be entirely misleading to investors. It is understood that an investor should know the differences between two funds that may be recommended to them, regardless of the type(s) of funds in those recommendations. In this regard we support consultations with IIROC and the MFDA to determine how differences between various types of investment fund are, or ought to be, discussed with clients. This would inform the development of the appropriate disclosures that will best support those client discussions.

Fund Risk Methodology

We appreciate the CSA's confirmation (in Annex B to the CSA Notice) that there is no presumption that all alternative funds are more risky than "conventional" mutual funds and that the CSA's mandatory risk rating methodology based on standard deviation would also be applicable to alternative funds.

As the CSA just released its final risk rating methodology on December 8, 2016 we are only now able to analyze the applicability of that methodology to alternative funds, and whether the proposed broader access to certain asset classes and investment strategies might necessitate modifications to the methodology.

There is more work to be done before the methodology can be applied to alternative funds. For instance, the Canadian Investment Funds Standards Committee ("CIFSC") currently has only one general "catch-all" category for funds that apply "alternative strategies". This is due primarily to the wide variety of different investment strategies used by those funds, making it difficult to compare one fund with its peers. IFIC's Fund Categorization Working Group is considering the best categorization approach to recommend to CIFSC for these funds. It is hoped that fund managers will not apply their own individual criteria to the alternative funds they manage. Similarly, as the CSA have already acknowledged, applying a blanket classification of "high risk" to all of these funds, without further analysis, is inappropriate and not necessarily accurate in all cases.

Distribution of Alternative Funds:

The Proposal replaces the current commodity pool proficiency requirements in NI 81-104 with the current proficiency and suitability requirements for investment fund distributors. The MFDA, in conjunction with the CSA, may require additional proficiency. We look forward to working with the MFDA as it considers the appropriate requirements for distribution of alternative funds by MFDA members and registrants, and to assisting MFDA registrants to become proficient to distribute these products in time for implementation of the framework.

Alternative Fund Financial Disclosure

IFIC's Accounting Advisory Working Group notes that the CSA Notice does not seek comment on the potential implications of the Proposal on existing MRFP disclosure requirements in NI 81-106. Some clarification in this regard may be helpful, in particular relating to TER and total return calculations. Commentary on treatment of costs related to short sale transactions would be beneficial to ensure consistency of application. In addition, the benefit and understandability of the split of total return between short and long portfolio positions should be considered. We would be happy to provide additional details on these matters.

* * * * *

We appreciate the opportunity to comment on the consultation. If you have any questions or comments, please contact me by email at rhensel@ific.ca or by phone at 416-309-2314.

Yours sincerely,

THE INVESTMENT FUNDS INSTITUTE OF CANADA

By: Ralf Hensel
General Counsel, Corporate Secretary & Vice President, Policy

APPENDIX A

CSA Alternative Funds Framework

Responses to Questions in Annex A to CSA Notice

Topic:	CSA Question:	Industry Response:
Definition of "Alternative Fund"	***1**. Under the Proposed Amendments, we are seeking to replace the term "commodity pool" with "alternative fund" in NI 81-102. We seek feedback on whether the term "alternative fund" best reflects the funds that are to be subject to the Proposed Amendments. If not, please propose other terms that may better reflect these types of funds. For example, would the term "nonconventional mutual fund" better reflect these types of funds?*	Our Members are content with the phrase "alternative funds" for these products on the basis that this phrase will be used as a descriptive term, and not become a defined term for use in a mandatory naming convention or labelling requirement.
Investment Restrictions		
Asset Classes	***2**. We are seeking feedback on whether there are particular asset classes common under typical "alternative" investment strategies, but have not been contemplated for alternative funds under the Proposed Amendments, that we should be considering, and why.*	Our Members have identified loans, loan syndications (without regard to administrative responsibilities), real estate and mortgages as common asset classes under typical "alternative" investment strategies that should also be contemplated for investment by alternative funds.
Concentration	***3**. We are proposing to raise the concentration limit for alternative funds to 20% of NAV at the time of purchase, meaning the limit must be observed only at the time of purchasing additional securities of an issuer. Should we also consider introducing an absolute upper limit or "hard cap" on concentration, which would require a fund to begin divesting its holdings of an issuer if the hard cap is breached, even passively, which is similar to the approach taken with illiquid assets under NI 81-102? Please explain why or why not.*	Our Members are generally content with the proposed concentration limit for alternative funds of 20% of NAV at the time of purchase, and do not believe a hard cap is necessary.

Illiquid Assets	***4****. We are not proposing to raise the illiquid asset limits for alternative funds under the Proposed Amendments. Are there strategies commonly used by alternative funds for which a higher illiquid asset investment threshold would be appropriate? Please be specific.*	Alternative funds commonly use several strategies for which a higher illiquid asset investment threshold is appropriate, including investments in distressed securities, loans and non-guaranteed mortgages, as well as merger arbitrage strategies. Investing in such assets is intended to capture an illiquidity premium associated with such assets.
	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.*	Yes, the frequency of redemptions of an alternative fund should be considered in determining the appropriate illiquid asset limit, as the less frequent the fund's redemptions, the more illiquid the assets can be, and vice-versa. A fund's redemption frequency is a key consideration in the responsible management of its investment portfolio.
Borrowing	***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*	Yes, alternative funds should be permitted to borrow from a broader range of entities beyond those that qualify as a custodian for investment fund assets in Canada, which the CSA have confirmed, includes dealers that act as prime brokers in Canada. The Proposal does not identify the CSA's concerns underlying the restriction to Canadian. At the very least, alternative funds should be permitted to borrow from U.S. lenders since funds are already permitted to post U.S. collateral against their borrowing. The CSA have confirmed that Canadian prime brokers are permitted lenders, but some funds use non-Canadian prime brokers that often provide them with credit. In light of established business practice, and absent more information about the CSA's concerns, we recommend that alternative funds also be permitted to borrow from non-Canadian prime brokers.

Total Leverage Limit	***9.*** *Are there specific types of funds, or strategies currently employed by commodity pools or non-redeemable investment funds that will be particularly impacted by the proposed 3 times leverage limit? Please be specific.*	Yes, absolute return funds may find the proposed leverage limit to be insufficient, as would funds that are hedging different sources of risk, particularly if they use multiple hedging instruments, unless borrowing for hedging purposes is excluded from the calculations as is recommended in our response to question 10.
	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?*	The proposed 3X leverage limit should exclude the use of specified derivatives for hedging purposes, since such borrowing does not impact the amount leveraged. Similarly short-sales of government securities should be excluded from the short-selling limit calculations.
	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.*	Our Members are generally satisfied with the use of the notional amount calculation method.

Disclosure		
Fund Facts Disclosure	***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.*	It would be helpful if the CSA could provide a sample Fund Facts for alternative funds. Consistent with our view that disclosure comparing alternative funds and "conventional" mutual funds is unnecessary, we recommend such disclosure be removed from the Fund Facts. The CSA have noted the central objective of the Fund Facts is to provide key information that is important for investors to consider when they purchase an investment product. There is currently no comparative language in the Fund Facts for "conventional mutual funds" as against any other fund types. In the summary disclosure regime for ETFs released on December 8, 2016, the CSA have mandated disclosure in the ETF Facts about the unique trading and pricing characteristics of ETFs, but no mandated comparative language as against mutual funds, with the exception of a minor reference to similarity, "like mutual funds", required in the Trading ETFs and Net asset value (NAV) sections. We urge the CSA to be consistent in their disclosure requirements in the ETF Facts and Fund Facts for all mutual fund types. The proposed requirement to include in the point of sale disclosure documents of an alternative fund the phrase "This mutual fund is an alternative fund", as is proposed to be included in the text box on the Fund Facts, or a similar phrase, is inappropriate and inconsistent with the CSA's confirmation that they are not proposing any mandatory naming conventions or other labelling requirements for alternative funds. The phrase "alternative fund" is meant to be for descriptive purposes only and is not to become a defined term.

		Our Members have other concerns with the proposed mandated content, and location of certain disclosures, in the proposed Fund Facts for alternative funds. It is more helpful to readers to have disclosure of unique characteristics of alternative funds in the appropriate section(s) of the document. As an example, information on redemptions is best included in the Quick Facts section. We suggest discussions with IIROC and the MFDA to determine how differences between the various investment funds ought to be discussed with clients. This would help inform the most appropriate disclosure to include in the Fund Facts to support those client discussions.
	14. *It is expected that the Fund Facts, and eventually the ETF Facts, will require the risk level of the mutual fund described in that document to be disclosed in accordance with the CSA Risk Classification Methodology (the Methodology) once it comes into effect. In the course of our consultations related to the Methodology, we have indicated our view that standard deviation can be applied to a broad range of fund types (asset class exposures, fund structures, manager strategies, etc.). However, in light of the proposed changes to the investment restrictions that are being contemplated, we seek feedback on the impact the Proposed Amendments would have on the applicability of the Methodology to alternative funds. In particular, given that alternative funds will have broadened access to certain asset classes and investment strategies, we seek feedback on what modifications might need to be made to the Methodology. For example, would the ability of alternative funds to engage in strategies involving leverage require additional factors beyond standard deviation to be taken into account?*	We appreciate the CSA's confirmation that there is no presumption that all alternative funds are more risky than "conventional" mutual funds and that the CSA's mandatory risk rating methodology based on standard deviation could also be appropriate for alternative funds. More analysis of the CSA's final risk rating methodology for mutual funds and ETFs, released on December 8, 2016, will be necessary to consider the applicability of that methodology to alternative funds and to identify any modifications to the CSA methodology that may be necessary.

Point of Sale	***15.*** *We seek feedback from fund managers regarding any specific or unique challenges or expenses that may arise with implementing point of sale disclosure for non-exchange traded alternative funds compared to other mutual funds that have already implemented a point of sale disclosure regime*	There are no obvious unique challenges from the fund managers' perspective with respect to implementing point of sale disclosure for non-exchange traded alternative funds. Investment fund managers are already well-versed in the production and filing requirements for the simplified prospectus, AIF and Fund Facts documents. There should be few, if any, documentary challenges on the distribution side. However, necessary advisor and dealer training on these new products, particularly to prepare for discussions with clients about the features of alternative funds, and implementation of potential new proficiency requirements in the MFDA channel will result in transition costs for distributors.
Transition		
	16. *We are seeking feedback on the proposed transition periods under the Proposed Amendments and whether they are sufficient to allow existing funds to transition to the updated regulatory regime? Please be specific.*	We expect that it will be primarily existing closed end funds and commodity pools created under NI 81-104 that would seek to transition into the new alternative funds regime in NI 81-102. To ease any transition that may be required or desired we recommend that one-time blanket exemptive relief be included in the final rule, and that the relief make it clear that there is no requirement forcing existing funds to transition over to the new regime.

REVISED NI 81-102 INVESTMENT RESTRICTIONS – *AT A GLANCE*

Investment Restriction*	**Alternative funds**	**Conventional mutual funds and ETFs (mutual funds)**	**Closed end funds (Non-redeemable investment funds)**
***Proposed changes are indicated in bold italic type**			
Concentration Restriction	***20 percent of NAV, subject to carve-outs***	10 percent of NAV, subject to carve-outs	***20 percent of NAV, subject to carve-outs***
Control restriction	No more than 10 percent of votes / equity securities of an issuer		
Restrictions on types of investments	No investment in: • real property • mortgages other than guaranteed mortgages • loan syndications / participations if any responsibility for administering the loan	No investment in: • real property • mortgages other than guaranteed mortgages • ***commodities other than 10 percent in certain precious metals (waived for precious metals funds)*** • loan syndications / participations if any responsibility for administering the loan	***No investment in:*** • ***real property*** • ***mortgages other than guaranteed mortgages*** • ***loan syndications / participations if any responsibility for administering the loan***
Illiquid assets	10 percent of NAV at time of investment (hard cap of 15 percent)		***20 percent of NAV at time of investment (hard cap of 25 percent)***
Fund-of-fund investments	• ***100 percent in underlying alternative mutual funds, non-redeemable investment funds, conventional mutual funds and ETFs***	• ***10 percent in underlying alternative funds and non-redeemable investment funds*** • ***100 percent in underlying conventional mutual funds and ETFs***	• ***100 percent in underlying alternative funds*** • 100 percent in underlying non-redeemable investment funds, conventional mutual funds and ETFs
Borrowing	***Limited to 50 percent of NAV, subject to restrictions***	Limited to 5 percent of NAV, subject to restrictions	***Limited to 50 percent of NAV, subject to restrictions***
Short-selling	***Up to 50 percent of NAV, with single issuer limited to 10 percent of NAV; no cash cover required***	Up to 20 percent of NAV, with single issuer limited to 5 percent of NAV; 150 percent cash cover required in all cases	***Up to 50 percent of NAV, with single issuer limited to 10 percent of NAV; no cash cover required***
Total borrowing and short-selling	***Aggregate limit of 50 percent of NAV at all times***	N/A	***Aggregate limit of 50 percent of NAV at all times***
Derivatives for hedging and non-hedging purposes	• ***No designated rating requirements for the derivative or counterparty*** • ***Counterparty exposure limit of 10 percent of NAV for derivatives, other than for cleared specified derivatives***	• Designated rating requirements for the derivative or counterparty • Counterparty exposure limit of 10 percent of NAV	• ***No designated rating requirements for the derivative or counterparty*** • ***Counterparty exposure limit of 10 percent of NAV for derivatives, other than for cleared specified derivatives***
Derivatives for non-hedging purposes	Exempt	Cover required for specified derivatives transactions	Exempt
Leverage	***Cannot exceed 3x NAV***	Leverage prohibited	***Cannot exceed 3x NAV***
Securities lending, repurchase and reverse repurchase arrangements	Permitted, subject to conditions		