

This document is an unofficial consolidation of all amendments to National Instrument 81-102 *Mutual Funds* and Companion Policy 81-102CP, applying from **September 28, 2009**. This document is for reference purposes only and is not an official statement of the law.

## NATIONAL INSTRUMENT 81-102 MUTUAL FUNDS

### TABLE OF CONTENTS

<b><u>PART</u></b>	<b><u>TITLE</u></b>
PART 1	DEFINITIONS AND APPLICATION
1.1	Definitions
1.2	Application
1.3	Interpretation
PART 2	INVESTMENTS
2.1	Concentration Restriction
2.2	Control Restrictions
2.3	Restrictions Concerning Types of Investments
2.4	Restrictions Concerning Illiquid Assets
2.5	Investments in Other Mutual Funds
2.6	Investment Practices
2.7	Transactions in Specified Derivatives for Hedging and Non-hedging Purposes
2.8	Transactions in Specified Derivatives for Purposes Other than Hedging
2.9	Transactions in Specified Derivatives for Hedging Purposes
2.10	Adviser Requirements
2.11	Commencement of Use of Specified Derivatives by a Mutual Fund
2.12	Securities Loans
2.13	Repurchase Transactions
2.14	Reverse Repurchase Transactions
2.15	Agent for Securities Lending, Repurchase and Reverse Repurchase Transactions
2.16	Controls and Records
2.17	Commencement of Securities Lending, Repurchase and Reverse Repurchase Transactions by a Mutual Fund
PART 3	NEW MUTUAL FUNDS
3.1	Initial Investment in a New Mutual Fund
3.2	Prohibition Against Distribution
3.3	Prohibition Against Reimbursement of Organization Costs
PART 4	CONFLICTS OF INTEREST
4.1	Prohibited Investments
4.2	Self-Dealing

- 4.3 Exception
- 4.4 Liability and Indemnification
  
- PART 5 FUNDAMENTAL CHANGES
  - 5.1 Matters Requiring Securityholder Approval
  - 5.2 Approval of Securityholders
  - 5.3 Circumstances in Which Approval of Securityholders Not Required
    - 5.3.1 Change of Auditor of the Mutual Fund
  - 5.4 Formalities Concerning Meetings of Securityholders
  - 5.5 Approval of Securities Regulatory Authority
  - 5.6 Pre-Approved Reorganizations and Transfers
  - 5.7 Applications
  - 5.8 Matters Requiring Notice
  - 5.9 Relief from Certain Regulatory Requirements
  - 5.10 [Repealed]
  
- PART 6 CUSTODIANSHIP OF PORTFOLIO ASSETS
  - 6.1 General
  - 6.2 Entities Qualified to Act as Custodian or Sub-Custodian for Assets Held in Canada
  - 6.3 Entities Qualified to Act as Sub-Custodian for Assets Held outside Canada
  - 6.4 Contents of Custodian and Sub-Custodian Agreements
  - 6.5 Holding of Portfolio Assets and Payment of Fees
  - 6.6 Standard of Care
  - 6.7 Review and Compliance Reports
  - 6.8 Custodial Provisions relating to Derivatives and Securities Lending, Repurchase and Reverse Repurchase Agreements
  - 6.9 Separate Account for Paying Expenses
  
- PART 7 INCENTIVE FEES
  - 7.1 Incentive Fees
  - 7.2 Multiple Portfolio Advisers
  
- PART 8 CONTRACTUAL PLANS
  - 8.1 Contractual Plans
  
- PART 9 SALE OF SECURITIES OF A MUTUAL FUND
  - 9.1 Transmission and Receipt of Purchase Orders
  - 9.2 Acceptance of Purchase Orders
  - 9.3 Issue Price of Securities
  - 9.4 Delivery of Funds and Settlement
  
- PART 10 REDEMPTION OF SECURITIES OF A MUTUAL FUND
  - 10.1 Requirements for Redemptions
  - 10.2 Transmission and Receipt of Redemption Orders
  - 10.3 Redemption Price of Securities
  - 10.4 Payment of Redemption Price
  - 10.5 Failure to Complete Redemption Order
  - 10.6 Suspension of Redemptions

PART 11 COMMINGLING OF CASH

- 11.1 Principal Distributors
- 11.2 Participating Dealers
- 11.3 Trust Accounts
- 11.4 Exemption
- 11.5 Right of Inspection

PART 12 COMPLIANCE REPORTS

- 12.1 Compliance Reports

PART 13 [Repealed]

PART 14 RECORD DATE

- 14.1 Record Date

PART 15 SALES COMMUNICATIONS AND PROHIBITED REPRESENTATIONS

- 15.1 Ability to Make Sales Communications
- 15.2 Sales Communications - General Requirements
- 15.3 Prohibited Disclosure in Sales Communications
- 15.4 Required Disclosure and Warnings in Sales Communications
- 15.5 Disclosure Regarding Distribution Fees
- 15.6 Performance Data - General Requirements
- 15.7 Advertisements
- 15.8 Performance Measurement Periods Covered by Performance Data
- 15.9 Changes affecting Performance Data
- 15.10 Formula for Calculating Standard Performance Data
- 15.11 Assumptions for Calculating Standard Performance Data
- 15.12 Sales Communications During the Waiting Period
- 15.13 Prohibited Representations
- 15.14 Sales Communication - Multi-Class Mutual Funds

PART 16 [Repealed]

PART 17 [Repealed]

PART 18 SECURITYHOLDER RECORDS

- 18.1 Maintenance of Records
- 18.2 Availability of Records

PART 19 EXEMPTIONS AND APPROVALS

- 19.1 Exemption
- 19.2 Exemption or Approval under Prior Policy
- 19.3 Revocation of Exemptions

PART 20 TRANSITIONAL

APPENDIX A - Futures Exchanges for the Purpose of Subsection 2.7(4) - Derivative Counterparty

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Exposure Limits

APPENDIX B-1, APPENDIX B-2 AND APPENDIX B-3 - Compliance Reports

APPENDIX C - Provisions contained in Securities Legislation for the Purpose of Subsection 4.1(5) –  
Prohibited Investments

**NATIONAL INSTRUMENT 81-102  
MUTUAL FUNDS**

**PART 1        DEFINITIONS AND APPLICATION**

**1.1        Definitions - In this Instrument**

“acceptable clearing corporation” means a clearing corporation that is an acceptable clearing corporation under the Joint Regulatory Financial Questionnaire and Report;

“advertisement” means a sales communication that is published or designed for use on or through a public medium;

“approved credit rating” means, for a security or instrument, a rating at or above one of the following rating categories issued by an approved credit rating organization for that security or instrument or a category that replaces one of the following rating categories if

- (a) there has been no announcement by the approved credit rating organization of which the mutual fund or its manager is or reasonably should be aware that the rating of the security or instrument to which the approved credit rating was given may be down-graded to a rating category that would not be an approved credit rating, and
- (b) no approved credit rating organization has rated the security or instrument in a rating category that is not an approved credit rating:

Approved Credit Rating Organization	Commercial Paper/ Short Term Debt	Long Term Debt
Dominion Bond Rating Service Limited	R-1 (low)	A
Fitch Ratings	F1	A
Moody's Investors Service	P-1	A2
Standard & Poor's	A-1(Low)	A”;

“approved credit rating organization” means Dominion Bond Rating Service Limited, Fitch Ratings, Moody's Investors Service, Standard & Poor's and any of their respective successors;

“asset allocation service” means an administrative service under which the investment of a person or company is allocated, in whole or in part, among mutual funds to which this Instrument applies and reallocated among those mutual funds and, if applicable, other assets according to an asset allocation strategy;

“book-based system” means a system for the central handling of securities or equivalent bookbased entries under which all securities of a class or series deposited within the system are treated as fungible and may be transferred or pledged by bookkeeping entry without physical delivery;

“cash cover” means any of the following portfolio assets of a mutual fund that are held by the mutual fund, have not been allocated for specific purposes and are available to satisfy all or part of the obligations arising from a position in specified derivatives held by the mutual fund:

1. Cash.
2. Cash equivalents.
3. Synthetic cash.
4. Receivables of the mutual fund that arise from the disposition of portfolio assets, net of payables that arise from the acquisition of portfolio assets.
5. Securities purchased by the mutual fund in a reverse repurchase transaction under section 2.14, to the extent of the cash paid for those securities by the mutual fund.
6. Commercial paper that has a term to maturity of 365 days or less and an approved credit rating and that was issued by a person or company other than a government or permitted supranational agency.

“cash equivalent” means an evidence of indebtedness that has a remaining term to maturity of 365 days or less and that is issued, or fully and unconditionally guaranteed as to principal and interest, by

- (a) the government of Canada or the government of a jurisdiction,
- (b) the government of the United States of America, the government of one of the states of the United States of America, the government of another sovereign state or a permitted supranational agency, if, in each case, the evidence of indebtedness has an approved credit rating, or
- (c) a Canadian financial institution, or a financial institution that is not incorporated or organized under the laws of Canada or of a jurisdiction if, in either case, evidences of indebtedness of that issuer or guarantor that are rated as short term debt by an approved credit rating organization have an approved credit rating;

“clearing corporation” means an organization through which trades in options or standardized futures are cleared and settled;

“clearing corporation option” means an option, other than an option on futures, issued by a clearing corporation;

“conventional convertible security” means a security of an issuer that is, according to its terms, convertible into, or exchangeable for, other securities of the issuer, or of an affiliate of the issuer;

“conventional floating rate debt instrument” means an evidence of indebtedness of which the interest obligations are based upon a benchmark commonly used in commercial lending arrangements;

“conventional warrant or right” means a security of an issuer, other than a clearing corporation, that gives the holder the right to purchase securities of the issuer or of an affiliate of the issuer;

“currency cross hedge” means the substitution by a mutual fund of a risk to one currency for a risk to another currency, if neither currency is a currency in which the mutual fund determines its net asset value

per security and the aggregate amount of currency risk to which the mutual fund is exposed is not increased by the substitution;

“custodian” means the institution appointed by a mutual fund to act as custodian of the portfolio assets of the mutual fund;

“dealer managed mutual fund” means a mutual fund the portfolio adviser of which is a dealer manager;

“dealer manager” means

- (a) a specified dealer that acts as a portfolio adviser,
- (b) a portfolio adviser in which a specified dealer, or a partner, director, officer, salesperson or principal shareholder of a specified dealer, directly or indirectly owns of record or beneficially, or exercises control or direction over, securities carrying more than 10 percent of the total votes attaching to securities of the portfolio adviser, or
- (c) a partner, director or officer of a portfolio adviser referred to in paragraph (b);

“debt-like security” means a security purchased by a mutual fund, other than a conventional convertible security or a conventional floating rate debt instrument, that evidences an indebtedness of the issuer if

- (a) either
  - (i) the amount of principal, interest or principal and interest to be paid to the holder is linked in whole or in part by a formula to the appreciation or depreciation in the market price, value or level of one or more underlying interests on a predetermined date or dates, or
  - (ii) the security provides the holder with a right to convert or exchange the security into or for the underlying interest or to purchase the underlying interest, and
- (b) on the date of acquisition by the mutual fund, the percentage of the purchase price attributable to the component of the security that is not linked to an underlying interest is less than 80 percent of the purchase price paid by the mutual fund;

“delta” means the positive or negative number that is a measure of the change in market value of an option relative to changes in the value of the underlying interest of the option;

“equivalent debt” means, in relation to an option, swap, forward contract or debt-like security, an evidence of indebtedness of approximately the same term as, or a longer term than, the remaining term to maturity of the option, swap, contract or debt-like security and that ranks equally with, or subordinate to, the claim for payment that may arise under the option, swap, contract or debt-like security;

“forward contract” means an agreement, not entered into with, or traded on, a stock exchange or futures exchange or cleared by a clearing corporation, to do one or more of the following on terms or at a price established by or determinable by reference to the agreement and at or by a time in the future established by or determinable by reference to the agreement:

1. Make or take delivery of the underlying interest of the agreement.
2. Settle in cash instead of delivery;

“fundamental investment objectives” means the investment objectives of a mutual fund that define both the fundamental nature of the mutual fund and the fundamental investment features of the mutual fund that distinguish it from other mutual funds;

“futures exchange” means an association or organization operated to provide the facilities necessary for the trading of standardized futures;

“government security” means an evidence of indebtedness issued, or fully and unconditionally guaranteed as to principal and interest, by any of the government of Canada, the government of a jurisdiction or the government of the United States of America;

“guaranteed mortgage” means a mortgage fully and unconditionally guaranteed, or insured, by the government of Canada, by the government of a jurisdiction or by an agency of any of those governments or by a corporation approved by the Office of the Superintendent of Financial Institutions to offer its services to the public in Canada as an insurer of mortgages;

“hedging” means the entering into of a transaction, or a series of transactions, and the maintaining of the position or positions resulting from the transaction or series of transactions

- (a) if
  - (i) the intended effect of the transaction, or the intended cumulative effect of the series of transactions, is to offset or reduce a specific risk associated with all or a portion of an existing investment or position or group of investments or positions,
  - (ii) the transaction or series of transactions results in a high degree of negative correlation between changes in the value of the investment or position, or group of investments or positions, being hedged and changes in the value of the instrument or instruments with which the investment or position is hedged, and
  - (iii) there are reasonable grounds to believe that the transaction or series of transactions no more than offset the effect of price changes in the investment or position, or group of investments or positions, being hedged, or
- (b) if the transaction, or series of transactions, is a currency cross hedge;

“illiquid asset” means

- (a) a portfolio asset that 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 mutual fund, or

- (b) a restricted security held by a mutual fund, the resale of which is prohibited by a representation, undertaking or agreement by the mutual fund or by the predecessor in title of the mutual fund;

“independent review committee” means the independent review committee of the investment fund established under National Instrument 81-107 *Independent Review Committee for Investment Funds*;

“index mutual fund” means a mutual fund that has adopted fundamental investment objectives that require the mutual fund to

- (a) hold the securities that are included in a permitted index or permitted indices of the mutual fund in substantially the same proportion as those securities are reflected in that permitted index or those permitted indices, or
- (b) invest in a manner that causes the mutual fund to replicate the performance of that permitted index or those permitted indices;

“index participation unit” means a security traded on a stock exchange in Canada or the United States and issued by an issuer the only purpose of which is to

- (a) hold the securities that are included in a specified widely quoted market index in substantially the same proportion as those securities are reflected in that index, or
- (b) invest in a manner that causes the issuer to replicate the performance of that index;

“investor fees” means, in connection with the purchase, conversion, holding, transfer or redemption of securities of a mutual fund, all fees, charges and expenses that are or may become payable by a securityholder of the mutual fund to a member of the organization of the mutual fund other than a member of the organization acting solely as a participating dealer;

“Joint Regulatory Financial Questionnaire and Report” means the Joint Regulatory Financial Questionnaire and Report of various Canadian SROs on the date that this Instrument comes into force and every successor to the form that does not materially lessen the criteria for an entity to be recognized as an “acceptable clearing corporation”;

“long position” means a position held by a mutual fund that, for

- (a) an option, entitles the mutual fund to elect to purchase, sell, receive or deliver the underlying interest or, instead, pay or receive cash,
- (b) a standardized future or forward contract, obliges the mutual fund to accept delivery of the underlying interest or, instead, pay or receive cash,
- (c) a call option on futures, entitles the mutual fund to elect to assume a long position in standardized futures,
- (d) a put option on futures, entitles the mutual fund to elect to assume a short position in

standardized futures, and

- (e) a swap, obliges the mutual fund to accept delivery of the underlying interest or receive cash;

“management expense ratio” means the ratio, expressed as a percentage, of the expenses of a mutual fund to its average net asset value, calculated in accordance with Part 15 of National Instrument 81-106 *Investment Fund Continuous Disclosure*;

“manager” means a person or company that directs the business, operations and affairs of a mutual fund;

“material change” has the meaning ascribed to that term in National Instrument 81-106 *Investment Fund Continuous Disclosure*;

“member of the organization” has the meaning ascribed to that term in National Instrument 81-105 *Mutual Fund Sales Practices*;

“money market fund” means a mutual fund that has and intends to continue to have

- (a) all of its assets invested in any or all of
  - (i) cash,
  - (ii) cash equivalents,
  - (iii) evidences of indebtedness, other than cash equivalents, that have remaining terms to maturity of 365 days or less, or
  - (iv) floating rate evidences of indebtedness not referred to in subparagraph (ii) or (iii), if the principal amounts of the obligations will continue to have a market value of approximately par at the time of each change in the rate to be paid to the holders of the evidences of indebtedness,
- (b) a portfolio with a dollar-weighted average term to maturity not exceeding 90 days, calculated on the basis that the term of a floating rate obligation is the period remaining to the date of the next rate setting,
- (c) not less than 95 percent of its assets invested in cash, cash equivalents or evidences of indebtedness denominated in a currency in which the net asset value per security of the mutual fund is calculated, and
- (d) not less than 95 percent of its assets invested in any or all of
  - (i) cash,
  - (ii) cash equivalents, or
  - (iii) evidences of indebtedness of issuers the commercial paper of which has an

approved credit rating;

“mortgage” includes a hypothec or security that creates a charge on real property in order to secure a debt;

“mutual fund conflict of interest investment restrictions” means the provisions of securities legislation that

- (a) prohibit a mutual fund from knowingly making or holding an investment in any person or company who is a substantial security holder, as defined in securities legislation, of the mutual fund, its management company, manager or distribution company;
- (b) prohibit a mutual fund from knowingly making or holding an investment in any person or company in which the mutual fund, alone or together with one or more related mutual funds, is a substantial security holder, as defined in securities legislation;
- (c) prohibit a mutual fund from knowingly making or holding an investment in an issuer in which any person or company who is a substantial security holder of the mutual fund, its management company, manager or distribution company, has a significant interest, as defined in securities legislation;
- (d) prohibit a mutual fund, a responsible person as defined in securities legislation, a portfolio adviser or a registered person acting under a management contract from knowingly causing any investment portfolio managed by it, or a mutual fund, to invest in, or prohibit a mutual fund from investing in, any issuer in which a responsible person, as defined in securities legislation, is an officer or director unless the specific fact is disclosed to the mutual fund, securityholder or client, and where securities legislation requires it, the written consent of the client to the investment is obtained before the purchase;
- (e) prohibit a mutual fund, a responsible person as defined in securities legislation, or a portfolio adviser knowingly causing any investment portfolio managed by it to purchase or sell, or prohibit a mutual fund from purchasing or selling, the securities of any issuer from or to the account of a responsible person, as defined in securities legislation, an associate of a responsible person or the portfolio adviser; and
- (f) prohibit a portfolio adviser or a registered person acting under a management contract from subscribing to or buying securities on behalf of a mutual fund, where his or her own interest might distort his or her judgment, unless the specific fact is disclosed to the client and the written consent of the client to the investment is obtained before the subscription or purchase;

“mutual fund conflict of interest reporting requirements” means the provisions of securities legislation that require the filing of a report with the securities regulatory authority in prescribed form that discloses every transaction of purchase or sale of portfolio assets between the mutual fund and specified related persons or companies;

“net asset value” means the value of the total assets of the investment fund less the value of the total

liabilities of the investment fund, as at a specific date, determined in accordance with Part 14 of National Instrument 81-106 *Investment Fund Continuous Disclosure*;

“NI 81-107” means National Instrument 81-107 *Independent Review Committee for Investment Funds*;

“non-resident sub-adviser” means a person or company providing portfolio management advice

- (a) whose principal place of business is outside of Canada,
- (b) that advises a portfolio adviser to a mutual fund, and
- (c) that is not registered under securities legislation in the jurisdiction in which the portfolio adviser that it advises is located;

“option” means an agreement that provides the holder with the right, but not the obligation, to do one or more of the following on terms or at a price established by or determinable by reference to the agreement at or by a time established by the agreement:

1. Receive an amount of cash determinable by reference to a specified quantity of the underlying interest of the option.
2. Purchase a specified quantity of the underlying interest of the option.
3. Sell a specified quantity of the underlying interest of the option;

“option on futures” means an option the underlying interest of which is a standardized future;

“order receipt office” means, for a mutual fund

- (a) the principal office of the mutual fund,
- (b) the principal office of the principal distributor of the mutual fund, or
- (c) a location to which a purchase order or redemption order for securities of the mutual fund is required or permitted by the mutual fund to be delivered by participating dealers or the principal distributor of the mutual fund;

“participating dealer” means a dealer other than the principal distributor that distributes securities of a mutual fund;

“participating fund” means a mutual fund in which an asset allocation service permits investment;

“performance data” means a rating, ranking, quotation, discussion or analysis regarding an aspect of the investment performance of a mutual fund, an asset allocation service, a security, an index or a benchmark;

“permitted gold certificate” means a certificate representing gold if the gold is

- (a) available for delivery in Canada, free of charge, to or to the order of the holder of the

certificate,

- (b) of a minimum fineness of 995 parts per 1,000,
- (c) held in Canada,
- (d) in the form of either bars or wafers, and
- (e) if not purchased from a bank listed in Schedule I, II or III of the *Bank Act (Canada)*, fully insured against loss and bankruptcy by an insurance company licensed under the laws of Canada or a jurisdiction;

“permitted index” means, in relation to a mutual fund, a market index that is

- (a) both
  - (i) administered by an organization that is not affiliated with any of the mutual fund, its manager, its portfolio adviser or its principal distributor, and
  - (ii) available to persons or companies other than the mutual fund, or
- (b) widely recognized and used;

“permitted supranational agency” means the African Development Bank, the Asian Development Bank, the Caribbean Development Bank, the European Bank for Reconstruction and Development, the Inter-American Development Bank, the International Bank for Reconstruction and Development, the International Finance Corporation, and any person or company prescribed under paragraph (g) of the definition of “foreign property” in subsection 206(1) of the ITA;

“physical commodity”, means, in an original or processed state, an agricultural product, forest product, product of the sea, mineral, metal, hydrocarbon fuel product, precious stone or other gem;

“portfolio adviser” means a person or company that provides investment advice or portfolio management services under a contract with the mutual fund or with the manager of the mutual fund;

“portfolio asset” means an asset of a mutual fund;

“pricing date” means, for the sale of a security of a mutual fund, the date on which the net asset value per security of the mutual fund is calculated for the purpose of determining the price at which that security is to be issued;

“principal distributor” means a person or company through whom securities of a mutual fund are distributed under an arrangement with the mutual fund or its manager that provides

- (a) an exclusive right to distribute the securities of the mutual fund in a particular area, or
- (b) a feature that gives or is intended to give the person or company a material competitive advantage over others in the distribution of the securities of the mutual fund;

“public quotation” includes, for the purposes of calculating the amount of illiquid assets held by a mutual fund, any quotation of a price for a fixed income security made through the inter-dealer bond market;

“purchase” means, in connection with an acquisition of a portfolio asset by a mutual fund, an acquisition that is the result of a decision made and action taken by the mutual fund;

“qualified security” means

- (a) an evidence of indebtedness that is issued, or fully and unconditionally guaranteed as to principal and interest, by
  - (i) the government of Canada or the government of a jurisdiction,
  - (ii) the government of the United States of America, the government of one of the states of the United States of America, the government of another sovereign state, or a permitted supranational agency, if, in each case, the evidence of indebtedness has an approved credit rating, or
  - (iii) a Canadian financial institution or a financial institution that is not incorporated or organized under the laws of Canada or of a jurisdiction if, in either case, evidences of indebtedness of that issuer or guarantor that are rated as short term debt by an approved credit rating organization have an approved credit rating, or
- (b) commercial paper that has a term to maturity of 365 days or less and an approved credit rating and that was issued by a person or company other than a government or permitted supranational agency;

“report to securityholders” means a report that includes annual or interim financial statements, or an annual or interim management report of fund performance, and that is delivered to securityholders of a mutual fund;

“restricted security” means a security, other than a specified derivative, the resale of which is restricted or limited by a representation, undertaking or agreement by the mutual fund or by the mutual fund’s predecessor in title, or by law;

“RSP clone fund” means a mutual fund that has adopted fundamental investment objectives to link its performance to the performance of another mutual fund whose securities constitute foreign property for registered plans and to ensure that the securities of the mutual fund will not constitute foreign property under the ITA;

“sales communication” means a communication relating to, and by, a mutual fund or asset allocation service, its promoter, manager, portfolio adviser, principal distributor, a participating dealer or a person or company providing services to any of them, that

- (a) is made
  - (i) to a securityholder of the mutual fund or participant in the asset allocation

service, or

- (ii) to a person or company that is not a securityholder of the mutual fund or participant in the asset allocation service, to induce the purchase of securities of the mutual fund or the use of the asset allocation service, and
- (b) is not contained in any of the following documents of the mutual fund:
  1. A simplified prospectus or preliminary or *pro forma* simplified prospectus.
  2. An annual information form or preliminary or *pro forma* annual information form.
  3. Financial statements, including the notes to the financial statements and the auditor's report on the financial statements.
  4. A trade confirmation.
  5. A statement of account;
  6. Annual or interim management report of fund performance;

“short position” means a position held by a mutual fund that, for

- (a) an option, obliges the mutual fund, at the election of another, to purchase, sell, receive or deliver the underlying interest, or, instead, pay or receive cash,
- (b) a standardized future or forward contract, obliges the mutual fund, at the election of another, to deliver the underlying interest or, instead, pay or receive cash,
- (c) a call option on futures, obliges the mutual fund, at the election of another, to assume a short position in standardized futures, and
- (d) a put option on futures, obliges the mutual fund, at the election of another, to assume a long position in standardized futures;

“special warrant” means a security that, by its terms or the terms of an accompanying contractual obligation, entitles or requires the holder to acquire another security without payment of material additional consideration and obliges the issuer of the special warrant or the other security to undertake efforts to file a prospectus to qualify the distribution of the other security;

“specified asset-backed security” means a security that

- (a) is primarily serviced by the cash flows of a discrete pool of receivables or other financial assets, either fixed or revolving, that by their terms convert into cash within a finite time, and any rights or assets designed to assure the servicing or timely distribution of proceeds to securityholders, and

- (b) by its terms entitles an investor in that security to a return of the investment of that investor at or by a time established by or determinable by reference to an agreement, except as a result of losses incurred on, or the non-performance of, the financial assets;

“specified dealer” means a dealer other than a dealer whose activities as a dealer are restricted by the terms of its registration to one or both of

- (a) acting solely in respect of mutual fund securities, or
- (b) acting solely in respect of transactions in which a person or company registered in the category of exempt market dealer in a jurisdiction is permitted to engage;

“specified derivative” means an instrument, agreement or security, the market price, value or payment obligations of which are derived from, referenced to or based on an underlying interest, other than

- (a) a conventional convertible security,
- (b) a specified asset-backed security,
- (c) an index participation unit,
- (d) a government or corporate strip bond,
- (e) a capital, equity dividend or income share of a subdivided equity or fixed income security,
- (f) a conventional warrant or right, or
- (g) a special warrant;

“standardized future” means an agreement traded on a futures exchange pursuant to standardized conditions contained in the by-laws, rules or regulations of the futures exchange, and cleared by a clearing corporation, to do one or more of the following at a price established by or determinable by reference to the agreement and at or by a time established by or determinable by reference to the agreement:

1. Make or take delivery of the underlying interest of the agreement.
2. Settle the obligation in cash instead of delivery of the underlying interest;

“sub-custodian” means, for a mutual fund, an entity that has been appointed to hold portfolio assets of the mutual fund in accordance with section 6.1 by either the custodian or a subcustodian of the mutual fund;

“swap” means an agreement that provides for

- (a) an exchange of principal amounts,
- (b) the obligation to make, and the right to receive, cash payments based upon the value,

level or price, or on relative changes or movements of the value, level or price, of one or more underlying interests, which payments may be netted against each other, or

- (c) the right or obligation to make, and the right or obligation to receive, physical delivery of an underlying interest instead of the cash payments referred to in paragraph (b);

“synthetic cash” means a position that in aggregate provides the holder with the economic equivalent of the return on a banker’s acceptance accepted by a bank listed in Schedule I of the *Bank Act* (Canada) and that consists of

- (a) a long position in a portfolio of shares and a short position in a standardized future of which the underlying interest consists of a stock index, if
  - (i) there is a high degree of positive correlation between changes in the value of the portfolio of shares and changes in the value of the stock index, and
  - (ii) the ratio between the value of the portfolio of shares and the standardized future is such that, for any change in the value of one, a change of similar magnitude occurs in the value of the other,
- (b) a long position in the evidences of indebtedness issued, or fully and unconditionally guaranteed as to principal and interest, by any of the government of Canada or the government of a jurisdiction and a short position in a standardized future of which the underlying interest consists of evidences of indebtedness of the same issuer and same term to maturity, if
  - (i) there is a high degree of positive correlation between changes in the value of the portfolio of evidences of indebtedness and changes in the value of the standardized future, and
  - (ii) the ratio between the value of the evidences of indebtedness and the standardized future is such that, for any change in the value of one, a change of similar magnitude occurs in the value of the other; or
- (c) a long position in securities of an issuer and a short position in a standardized future of which the underlying interest is securities of that issuer, if the ratio between the value of the securities of that issuer and the position in the standardized future is such that, for any change in the value of one, a change of similar magnitude occurs in the value of the other;

“underlying interest” means, for a specified derivative, the security, commodity, financial instrument, currency, interest rate, foreign exchange rate, economic indicator, index, basket, agreement, benchmark or any other reference, interest or variable, and, if applicable, the relationship between any of the foregoing, from, to or on which the market price, value or payment obligation of the specified derivative is derived, referenced or based; and

“underlying market exposure” means, for a position of a mutual fund in

- (a) an option, the quantity of the underlying interest of the option position multiplied by the market value of one unit of the underlying interest, multiplied, in turn, by the delta of the option,
- (b) a standardized future or forward contract, the quantity of the underlying interest of the position multiplied by the current market value of one unit of the underlying interest; or
- (c) a swap, the underlying market exposure, as calculated under paragraph (b), for the long position of the mutual fund in the swap.

**1.2 Application** - This Instrument applies only to

- (a) a mutual fund that offers or has offered securities under a simplified prospectus for so long as the mutual fund remains a reporting issuer; and
- (b) a person or company in respect of activities pertaining to a mutual fund referred to in paragraph (a) or pertaining to the filing of a simplified prospectus to which subsection 3.1(1) applies.

**1.3 Interpretation**

- (1) Each section, part, class or series of a class of securities of a mutual fund that is referable to a separate portfolio of assets is considered to be a separate mutual fund for purposes of this Instrument.
- (2) A mutual fund that renews or extends a securities lending, repurchase or reverse repurchase transaction is entering into a securities lending, repurchase or reverse repurchase agreement for the purposes of section 2.12, 2.13 or 2.14.
- (3) In this Instrument, a reference to a "simplified prospectus" includes a prospectus, a reference to a "preliminary simplified prospectus" includes a preliminary prospectus and a reference to a "*pro forma* simplified prospectus" includes a *pro forma* prospectus.

**PART 2 INVESTMENTS**

**2.1 Concentration Restriction**

- (1) A mutual fund shall not purchase a security of an issuer, enter into a specified derivatives transaction or purchase index participation units if, immediately after the transaction, more than 10 percent of the net assets of the mutual fund, taken at market value at the time of the transaction, would be invested in securities of any issuer.
- (2) Subsection (1) does not apply to a purchase of a government security, a security issued by a clearing corporation, a security issued by a mutual fund to which this Instrument and National Instrument 81-101 apply, or an index participation unit that is a security of a mutual fund.
- (3) In determining a mutual fund's compliance with the restrictions contained in this section, the mutual fund shall, for each long position in a specified derivative that is held by the mutual fund

for purposes other than hedging and for each index participation unit held by the mutual fund, consider that it holds directly the underlying interest of that specified derivative or its proportionate share of the securities held by the issuer of the index participation unit.

- (4) Despite subsection (3), the mutual fund shall not include in the determination referred to in subsection (3) a security or instrument that is a component of, but that represents less than 10 percent of
  - (a) a stock or bond index that is the underlying interest of a specified derivative; or
  - (b) the securities held by the issuer of an index participation unit.
- (5) Despite subsection (1), an index mutual fund, the name of which includes the word “index”, may, in order to satisfy its fundamental investment objectives, purchase a security, enter into a specified derivatives transaction or purchase index participation units if its simplified prospectus contains the disclosure referred to in subsection (5) of Item 6 and subsection (5) of Item 9 of Part B of Form 81-101F1 *Contents of Simplified Prospectus*.

## **2.2 Control Restrictions**

- (1) A mutual fund shall not
  - (a) purchase a security of an issuer if, immediately after the purchase, the mutual fund would hold securities representing more than 10 percent of
    - (i) the votes attaching to the outstanding voting securities of that issuer; or
    - (ii) the outstanding equity securities of that issuer; or
  - (b) purchase a security for the purpose of exercising control over or management of the issuer of the security.
- (1.1) Subsection (1) does not apply to the purchase of a security issued by a mutual fund to which this Instrument and National Instrument 81-101 apply, or an index participation unit that is a security of a mutual fund.
- (2) If a mutual fund acquires a security of an issuer other than as the result of a purchase, and the acquisition results in the mutual fund exceeding the limits described in paragraph (1)(a), the mutual fund shall as quickly as is commercially reasonable, and in any event no later than 90 days after the acquisition, reduce its holdings of those securities so that it does not hold securities exceeding those limits.
- (3) In determining its compliance with the restrictions contained in this section, a mutual fund shall
  - (a) assume the conversion of special warrants held by it; and
  - (b) consider that it holds directly the underlying securities represented by any American depositary receipts held by it.

**2.3 Restrictions Concerning Types of Investments** - A mutual fund shall not

- (a) purchase real property;
- (b) purchase a mortgage, other than a guaranteed mortgage;
- (c) purchase a guaranteed mortgage if, immediately after the purchase, more than 10 percent of the net assets of the mutual fund, taken at market value at the time of the purchase, would consist of guaranteed mortgages;
- (d) purchase a gold certificate, other than a permitted gold certificate;
- (e) purchase gold or a permitted gold certificate if, immediately after the purchase, more than 10 percent of the net assets of the mutual fund, taken at market value at the time of the purchase, would consist of gold and permitted gold certificates;
- (f) except to the extent permitted by paragraphs (d) and (e), purchase a physical commodity;
- (g) purchase, sell or use a specified derivative other than in compliance with sections 2.7 to 2.11;
- (h) purchase, sell or use a specified derivative the underlying interest of which is
  - (i) a physical commodity other than gold, or
  - (ii) a specified derivative of which the underlying interest is a physical commodity other than gold; or
- (i) purchase an interest in a loan syndication or loan participation if the purchase would require the mutual fund to assume any responsibilities in administering the loan in relation to the borrower.

**2.4 Restrictions Concerning Illiquid Assets**

- (1) A mutual fund shall not purchase an illiquid asset if, immediately after the purchase, more than 10 percent of the net assets of the mutual fund, taken at market value at the time of the purchase, would consist of illiquid assets.
- (2) A mutual fund shall not have invested, for a period of 90 days or more, more than 15 percent of its net assets, taken at market value, in illiquid assets.
- (3) If more than 15 percent of the net assets of a mutual fund, taken at market value, are illiquid assets, the mutual fund shall, as quickly as is commercially reasonable, take all necessary steps to reduce the percentage of its net assets made up of illiquid assets to 15 percent or less.

**2.5 Investments in Other Mutual Funds**

- (1) For the purposes of this section, a mutual fund is considered to be holding a security of another mutual fund if
  - (a) it holds securities issued by the other mutual fund, or
  - (b) it is maintaining a position in a specified derivative for which the underlying interest is a security of the other mutual fund.
- (2) A mutual fund shall not purchase or hold a security of another mutual fund unless,
  - (a) the other mutual fund is subject to this Instrument and National Instrument 81-101,
  - (b) at the time of the purchase of that security, the other mutual fund holds no more than 10% of the market value of its net assets in securities of other mutual funds,
  - (c) the securities of the mutual fund and the securities of the other mutual fund are qualified for distribution in the local jurisdiction,
  - (d) no management fees or incentive fees are payable by the mutual fund that, to a reasonable person, would duplicate a fee payable by the other mutual fund for the same service,
  - (e) no sales fees or redemption fees are payable by the mutual fund in relation to its purchases or redemptions of the securities of the other mutual fund if the other mutual fund is managed by the manager or an affiliate or associate of the manager of the mutual fund, and
  - (f) no sales fees or redemption fees are payable by the mutual fund in relation to its purchases or redemptions of securities of the other mutual fund that, to a reasonable person, would duplicate a fee payable by an investor in the mutual fund.
- (3) Paragraphs (2)(a) and (c) do not apply if the security
  - (a) is an index participation unit issued by a mutual fund, or
  - (b) is issued by another mutual fund established with the approval of the government of a foreign jurisdiction and the only means by which the foreign jurisdiction permits investment in the securities of issuers of that foreign jurisdiction is through that type of mutual fund.
- (4) Paragraph (2)(b) does not apply if the other mutual fund
  - (a) is a RSP clone fund, or
  - (b) in accordance with this section purchases or holds securities
    - (i) of a money market fund, or
    - (ii) that are index participation units issued by a mutual fund.

- (5) Paragraph (2)(f) does not apply to brokerage fees incurred for the purchase or sale of an index participation unit issued by a mutual fund.
- (6) A mutual fund that holds securities of another mutual fund that is managed by the same manager or an affiliate or associate of the manager
  - (a) shall not vote any of those securities, and
  - (b) may, if the manager so chooses, arrange for all of the securities it holds of the other mutual fund to be voted by the beneficial holders of securities of the mutual fund.
- (7) The mutual fund conflict of interest investment restrictions and the mutual fund conflict of interest reporting requirements do not apply to a mutual fund which purchases or holds securities of another mutual fund if the purchase or holding is made in accordance with this section.

**2.6 Investment Practices - A mutual fund shall not**

- (a) borrow cash or provide a security interest over any of its portfolio assets unless
  - (i) the transaction is a temporary measure to accommodate requests for the redemption of securities of the mutual fund while the mutual fund effects an orderly liquidation of portfolio assets, or to permit the mutual fund to settle portfolio transactions and, after giving effect to all transactions undertaken under this subparagraph, the outstanding amount of all borrowings of the mutual fund does not exceed five percent of the net assets of the mutual fund taken at market value at the time of the borrowing,
  - (ii) the security interest is required to enable the mutual fund to effect a specified derivative transaction under this Instrument, is made in accordance with industry practice for that type of transaction and relates only to obligations arising under that particular specified derivatives transaction, or
  - (iii) the security interest secures a claim for the fees and expenses of the custodian or a sub-custodian of the mutual fund for services rendered in that capacity as permitted by subsection 6.4(3);
- (b) purchase securities on margin, unless permitted by section 2.7 or 2.8;
- (c) sell securities short, unless permitted by section 2.7 or 2.8;
- (d) purchase a security, other than a specified derivative, that by its terms may require the mutual fund to make a contribution in addition to the payment of the purchase price;
- (e) engage in the business of underwriting, or marketing to the public, securities of any other issuer;
- (f) lend cash or portfolio assets other than cash;

- (g) guarantee securities or obligations of a person or company; or
- (h) purchase securities other than through market facilities through which these securities are normally bought and sold unless the purchase price approximates the prevailing market price or the parties are at arm's length in connection with the transaction.

## **2.7 Transactions in Specified Derivatives for Hedging and Non-hedging Purposes**

- (1) A mutual fund shall not purchase an option that is not a clearing corporation option or a debt-like security or enter into a swap or a forward contract unless
  - (a) in the case of an option, swap or forward contract, the option, swap or contract has a remaining term to maturity of
    - (i) three years or less, or
    - (ii) between three and five years if, at the time of the transaction, the option, swap or contract provides the mutual fund with a right, at its election, to eliminate its exposure under the option, swap or contract no later than three years after the mutual fund has purchased the option or entered into the swap or contract; and
  - (b) at the time of the transaction, the option, debt-like security, swap or contract, or equivalent debt of the counterparty, or of a person or company that has fully and unconditionally guaranteed the obligations of the counterparty in respect of the option, debt-like security, swap or contract, has an approved credit rating.
- (2) If the credit rating of an option that is not a clearing corporation option, the credit rating of a debt-like security, swap or forward contract, or the credit rating of the equivalent debt of the writer or guarantor of the option, debt-like security, swap or contract, falls below the level of approved credit rating while the option, debt-like security, swap or contract is held by a mutual fund, the mutual fund shall take the steps that are reasonably required to close out its position in the option, debt-like security, swap or contract in an orderly and timely fashion.
- (3) Despite any other provisions contained in this Part, a mutual fund may enter into a trade to close out all or part of a position in a specified derivative, in which case the cash cover held to cover the underlying market exposure of the part of the position that is closed out may be released.
- (4) The mark-to-market value of the exposure of a mutual fund under its specified derivatives positions with any one counterparty other than an acceptable clearing corporation or a clearing corporation that clears and settles transactions made on a futures exchange listed in Appendix A, calculated in accordance with subsection (5), shall not exceed, for a period of 30 days or more, 10 percent of the net assets of the mutual fund.
- (5) The mark-to-market value of specified derivatives positions of a mutual fund with any one counterparty shall be, for the purposes of subsection (4),
  - (a) if the mutual fund has an agreement with the counterparty that provides for netting or the

right of set-off, the net mark-to-market value of the specified derivatives positions of the mutual fund; and

- (b) in all other cases, the aggregated mark-to-market value of the specified derivative positions of the mutual fund.

## **2.8 Transactions in Specified Derivatives for Purposes Other than Hedging**

(1) A mutual fund shall not

- (a) purchase a debt-like security that has an options component or an option, unless, immediately after the purchase, not more than 10 percent of the net assets of the mutual fund, taken at market value at the time of the purchase, would consist of those instruments held for purposes other than hedging;
- (b) write a call option, or have outstanding a written call option, that is not an option on futures unless, as long as the position remains open, the mutual fund holds
  - (i) an equivalent quantity of the underlying interest of the option,
  - (ii) a right or obligation, exercisable at any time that the option is exercisable, to acquire an equivalent quantity of the underlying interest of the option, and cash cover that, together with margin on account for the position, is not less than the amount, if any, by which the strike price of the right or obligation to acquire the underlying interest exceeds the strike price of the option, or
  - (iii) a combination of the positions referred to in subparagraphs (i) and (ii) that is sufficient, without recourse to other assets of the mutual fund, to enable the mutual fund to satisfy its obligations to deliver the underlying interest of the option;
- (c) write a put option, or have outstanding a written put option, that is not an option on futures, unless, as long as the position remains open, the mutual fund holds
  - (i) a right or obligation, exercisable at any time that the option is exercisable, to sell an equivalent quantity of the underlying interest of the option, and cash cover in an amount that, together with margin on account for the position, is not less than the amount, if any, by which the strike price of the option exceeds the strike price of the right or obligation to sell the underlying interest,
  - (ii) cash cover that, together with margin on account for the option position, is not less than the strike price of the option, or
  - (iii) a combination of the positions referred to in subparagraphs (i) and (ii) that is sufficient, without recourse to other assets of the mutual fund, to enable the mutual fund to acquire the underlying interest of the option;
- (d) open or maintain a long position in a debt-like security that has a component that is a

- long position in a forward contract, or in a standardized future or forward contract, unless the mutual fund holds cash cover in an amount that, together with margin on account for the specified derivative and the market value of the specified derivative, is not less than, on a daily mark-to-market basis, the underlying market exposure of the specified derivative;
- (e) open or maintain a short position in a standardized future or forward contract, unless the mutual fund holds
- (i) an equivalent quantity of the underlying interest of the future or contract,
  - (ii) a right or obligation to acquire an equivalent quantity of the underlying interest of the future or contract and cash cover that together with margin on account for the position is not less than the amount, if any, by which the strike price of the right or obligation to acquire the underlying interest exceeds the forward price of the contract, or
  - (iii) a combination of the positions referred to in subparagraphs (i) and (ii) that is sufficient, without recourse to other assets of the mutual fund, to enable the mutual fund to deliver the underlying interest of the future or contract; or
- (f) enter into, or maintain, a swap position unless
- (i) for periods when the mutual fund would be entitled to receive payments under the swap, the mutual fund holds cash cover in an amount that, together with margin on account for the swap and the market value of the swap, is not less than, on a daily mark-to-market basis, the underlying market exposure of the swap; and
  - (ii) for periods when the mutual fund would be required to make payments under the swap, the mutual fund holds
    - (A) an equivalent quantity of the underlying interest of the swap,
    - (B) a right or obligation to acquire an equivalent quantity of the underlying interest of the swap and cash cover that, together with margin on account for the position, is not less than the aggregate amount of the obligations of the mutual fund under the swap, or
    - (C) a combination of the positions referred to in clauses (A) and (B) that is sufficient, without recourse to other assets of the mutual fund, to enable the mutual fund to satisfy its obligations under the swap.
- (2) A mutual fund shall treat any synthetic cash position on any date as providing the cash cover equal to the notional principal value of a banker's acceptance then being accepted by a bank listed in Schedule I of the *Bank Act* (Canada) that would produce the same annualized return as the synthetic cash position is then producing.

**2.9 Transactions in Specified Derivatives for Hedging Purposes** - Sections 2.1, 2.2, 2.4 and 2.8 do not apply to the use of specified derivatives by a mutual fund for hedging purposes.

**2.10 Adviser Requirements**

- (1) If a portfolio adviser of a mutual fund receives advice from a non-resident sub-adviser concerning the use of options or standardized futures by the mutual fund, the mutual fund shall not invest in or use options or standardized futures unless
  - (a) the obligations and duties of the non-resident sub-adviser are set out in a written agreement with the portfolio adviser; and
  - (b) the portfolio adviser contractually agrees with the mutual fund to be responsible for any loss that arises out of the failure of the non-resident sub-adviser
    - (i) to exercise the powers and discharge the duties of its office honestly, in good faith and in the best interests of the mutual fund, and
    - (ii) to exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances.
- (2) A mutual fund shall not relieve a portfolio adviser of the mutual fund from liability for loss for which the portfolio adviser has assumed responsibility under paragraph (1)(b) that arises out of the failure of the relevant non-resident sub-adviser
  - (a) to exercise the powers and discharge the duties of its office honestly, in good faith and in the best interests of the mutual fund, or
  - (b) to exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances.
- (3) Despite subsection 4.4(3), a mutual fund may indemnify a portfolio adviser against legal fees, judgments and amounts paid in settlement, actually and reasonably incurred by that person or company in connection with services provided by a non-resident sub-adviser for which the portfolio adviser has assumed responsibility under paragraph (1)(b), only if
  - (a) those fees, judgments and amounts were not incurred as a result of a breach of the standard of care described in subsection (1) or (2); and
  - (b) the mutual fund has reasonable grounds to believe that the action or inaction that caused the payment of the fees, judgments and amounts paid in settlement was in the best interests of the mutual fund.
- (4) A mutual fund shall not incur the cost of any portion of liability insurance that insures a person or company for a liability except to the extent that the person or company may be indemnified for that liability under this section.

**2.11 Commencement of Use of Specified Derivatives by a Mutual Fund**

- (1) A mutual fund that has not used specified derivatives shall not begin using specified derivatives unless
  - (a) its simplified prospectus contains the disclosure required for mutual funds using derivatives; and
  - (b) the mutual fund has provided to its securityholders, not less than 60 days before it begins using specified derivatives, written notice that discloses its intent to begin using specified derivatives and the disclosure required for mutual funds using derivatives.
- (2) A mutual fund is not required to provide the notice referred to in paragraph (1)(b) if each simplified prospectus of the mutual fund since the later of January 1, 1994 and its inception contains the disclosure required for mutual funds using specified derivatives.

## **2.12 Securities Loans**

- (1) Despite any other provision of this Instrument, a mutual fund may enter into a securities lending transaction as lender if the following conditions are satisfied for the transaction:
  1. The transaction is administered and supervised in the manner required by sections 2.15 and 2.16.
  2. The transaction is made under a written agreement that implements the requirements of this section.
  3. Securities are loaned by the mutual fund in exchange for collateral.
  4. The securities transferred, either by the mutual fund or to the mutual fund as collateral, as part of the transaction are immediately available for good delivery under applicable legislation.
  5. The collateral to be delivered to the mutual fund at the beginning of the transaction
    - (a) is received by the mutual fund either before or at the same time as it delivers the loaned securities; and
    - (b) has a market value equal to at least 102 percent of the market value of the loaned securities.
  6. The collateral to be delivered to the mutual fund is one or more of
    - (a) cash;
    - (b) qualified securities;
    - (c) securities that are immediately convertible into, or exchangeable for, securities of the same issuer, class or type, and the same term, if applicable, as the securities

that are being loaned by the mutual fund, and in at least the same number as those loaned by the mutual fund; or

- (d) irrevocable letters of credit issued by a Canadian financial institution that is not the counterparty, or an affiliate of the counterparty, of the mutual fund in the transaction, if evidences of indebtedness of the Canadian financial institution that are rated as short term debt by an approved credit rating organization have an approved credit rating.
7. The collateral and loaned securities are marked to market on each business day, and the amount of collateral in the possession of the mutual fund is adjusted on each business day to ensure that the market value of collateral maintained by the mutual fund in connection with the transaction is at least 102 percent of the market value of the loaned securities.
  8. If an event of default by a borrower occurs, the mutual fund, in addition to any other remedy available under the agreement or applicable law, has the right under the agreement to retain and dispose of the collateral to the extent necessary to satisfy its claims under the agreement.
  9. The borrower is required to pay promptly to the mutual fund amounts equal to and as compensation for all dividends and interest paid, and all distributions made, on the loaned securities during the term of the transaction.
  10. The transaction is a "securities lending arrangement" under section 260 of the ITA.
  11. The mutual fund is entitled to terminate the transaction at any time and recall the loaned securities within the normal and customary settlement period for securities lending transactions in the market in which the securities are lent.
  12. Immediately after the mutual fund enters into the transaction, the aggregate market value of all securities loaned by the mutual fund in securities lending transactions and not yet returned to it or sold by the mutual fund in repurchase transactions under section 2.13 and not yet repurchased does not exceed 50 percent of the total assets of the mutual fund, and for such purposes collateral held by the mutual fund for the loaned securities and cash held by the mutual fund for the sold securities shall not be included in total assets.
- (2) A mutual fund may hold all cash delivered to it as the collateral in a securities lending transaction or may use the cash to purchase
    - (a) qualified securities having a remaining term to maturity no longer than 90 days;
    - (b) securities under a reverse repurchase agreement permitted by section 2.14; or
    - (c) a combination of the securities referred to in paragraphs (a) and (b).
  - (3) A mutual fund, during the term of a securities lending transaction, shall hold all, and shall not invest or dispose of any, non-cash collateral delivered to it as collateral in the transaction.

## 2.13 Repurchase Transactions

- (1) Despite any other provision of this Instrument, a mutual fund may enter into a repurchase transaction if the following conditions are satisfied for the transaction:
1. The transaction is administered and supervised in the manner required by sections 2.15 and 2.16.
  2. The transaction is made under a written agreement that implements the requirements of this section.
  3. Securities are sold for cash by the mutual fund, with the mutual fund assuming an obligation to repurchase the securities for cash.
  4. The securities transferred by the mutual fund as part of the transaction are immediately available for good delivery under applicable legislation.
  5. The cash to be delivered to the mutual fund at the beginning of the transaction
    - (a) is received by the mutual fund either before or at the same time as it delivers the sold securities; and
    - (b) is in an amount equal to at least 102 percent of the market value of the sold securities.
  6. The sold securities are marked to market on each business day, and the amount of sale proceeds in the possession of the mutual fund is adjusted on each business day to ensure that the amount of cash maintained by the mutual fund in connection with the transaction is at least 102 percent of the market value of the sold securities.
  7. If an event of default by a purchaser occurs, the mutual fund, in addition to any other remedy available under the agreement or applicable law, has the right under the agreement to retain or dispose of the sale proceeds delivered to it by the purchaser to the extent necessary to satisfy its claims under the agreement.
  8. The purchaser of the securities is required to pay promptly to the mutual fund amounts equal to and as compensation for all dividends and interest paid, and all distributions made, on the sold securities during the term of the transaction.
  9. The transaction is a "securities lending arrangement" under section 260 of the ITA.
  10. The term of the repurchase agreement, before any extension or renewal that requires the consent of both the mutual fund and the purchaser, is not more than 30 days.
  11. Immediately after the mutual fund enters into the transaction, the aggregate market value of all securities loaned by the mutual fund in securities lending transactions under section 2.12 and not yet returned to it or sold by the mutual fund in repurchase transactions and not yet repurchased does not exceed 50 percent of the total assets of the mutual fund, and

for such purposes collateral held by the mutual fund for the loaned securities and the cash held by the mutual fund for the sold securities shall not be included in total assets.

- (2) A mutual fund may hold cash delivered to it as consideration for sold securities in a repurchase transaction or may use the cash to purchase
- (a) qualified securities having a remaining term to maturity no longer than 30 days;
  - (b) securities under a reverse repurchase agreement permitted by section 2.14; or
  - (c) a combination of the securities referred to in paragraphs (a) and (b).

## **2.14 Reverse Repurchase Transactions**

- (1) Despite any other provision of this Instrument, a mutual fund may enter into a reverse repurchase transaction if the following conditions are satisfied for the transaction:
- 1. The transaction is administered and supervised in the manner required by sections 2.15 and 2.16.
  - 2. The transaction is made under a written agreement that implements the requirements of this section.
  - 3. Qualified securities are purchased for cash by the mutual fund, with the mutual fund assuming the obligation to resell them for cash.
  - 4. The securities transferred as part of the transaction are immediately available for good delivery under applicable legislation.
  - 5. The securities to be delivered to the mutual fund at the beginning of the transaction
    - (a) are received by the mutual fund either before or at the same time as it delivers the cash used by it to purchase those securities; and
    - (b) have a market value equal to at least 102 percent of the cash paid for the securities by the mutual fund.
  - 6. The purchased securities are marked to market on each business day, and either the amount of cash paid for the purchased securities or the amount of purchased securities in the possession of the seller or the mutual fund is adjusted on each business day to ensure that the market value of purchased securities held by the mutual fund in connection with the transaction is not less than 102 percent of the cash paid by the mutual fund.
  - 7. If an event of default by a seller occurs, the mutual fund, in addition to any other remedy available in the agreement or applicable law, has the right under the agreement to retain or dispose of the purchased securities delivered to it by the seller to the extent necessary to satisfy its claims under the agreement.

8. The transaction is a "securities lending arrangement" under section 260 of the ITA.
9. The term of the reverse repurchase agreement, before any extension or renewal that requires the consent of both the seller and the mutual fund, is not more than 30 days.

### **2.15 Agent for Securities Lending, Repurchase and Reverse Repurchase Transactions**

- (1) The manager of a mutual fund shall appoint an agent or agents to act on behalf of the mutual fund in administering the securities lending and repurchase transactions entered into by the mutual fund.
- (2) The manager of a mutual fund may appoint an agent or agents to act on behalf of the mutual fund to administer the reverse repurchase transactions entered into by the mutual fund.
- (3) The custodian or a sub-custodian of the mutual fund shall be the agent appointed under subsection (1) or (2).
- (4) The manager of a mutual fund shall not authorize an agent to enter into a securities lending, repurchase or, if applicable, reverse repurchase transactions on behalf of the mutual fund until the agent enters into a written agreement with the manager and the mutual fund in which
  - (a) the mutual fund and the manager provide instructions to the agent on the parameters to be followed in entering into the type of transactions to which the agreement pertains;
  - (b) the agent agrees to comply with this Instrument, accepts the standard of care referred to in subsection (5) and agrees to ensure that all transactions entered into by it on behalf of the mutual fund will comply with this Instrument; and
  - (c) the agent agrees to provide to the mutual fund and the manager regular, comprehensive and timely reports summarizing the mutual fund's securities lending, repurchase and reverse repurchase transactions, as applicable.
- (5) An agent appointed under this section, in administering the securities lending, repurchase and, if applicable, reverse repurchase transactions of the mutual fund shall exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances.

### **2.16 Controls and Records**

- (1) A mutual fund shall not enter into transactions under sections 2.12, 2.13 or 2.14 unless,
  - (a) for transactions to be entered into through an agent appointed under section 2.15, the manager has reasonable grounds to believe that the agent has established and maintains appropriate internal controls and procedures and records; and
  - (b) for reverse repurchase transactions directly entered into by the mutual fund without an agent, the manager has established and maintains appropriate internal controls, procedures and records.

- (2) The internal controls, procedures and records referred to in subsection (1) shall include
  - (a) a list of approved borrowers, purchasers and sellers based on generally accepted creditworthiness standards;
  - (b) as applicable, transaction and credit limits for each counterparty; and
  - (c) collateral diversification standards.
- (3) The manager of a mutual fund shall, on a periodic basis not less frequently than annually,
  - (a) review the agreements with any agent appointed under section 2.15 to determine if the agreements are in compliance with this Instrument;
  - (b) review the internal controls described in subsection (2) to ensure their continued adequacy and appropriateness;
  - (c) make reasonable enquiries as to whether the agent is administering the securities lending, repurchase or reverse repurchase transactions of the mutual fund in a competent and responsible manner, in conformity with the requirements of this Instrument and in conformity with the agreement between the agent, the manager and the mutual fund entered into under subsection 2.15(4);
  - (d) review the terms of any agreement between the mutual fund and an agent entered into under subsection 2.15(4) in order to determine if the instructions provided to the agent in connection with the securities lending, repurchase or reverse repurchase transactions of the mutual fund continue to be appropriate; and
  - (e) make or cause to be made any changes that may be necessary to ensure that
    - (i) the agreements with agents are in compliance with this Instrument,
    - (ii) the internal controls described in subsection (2) are adequate and appropriate,
    - (iii) the securities lending, repurchase or reverse repurchase transactions of the mutual fund are administered in the manner described in paragraph (c), and
    - (iv) the terms of each agreement between the mutual fund and an agent entered into under subsection 2.15(4) are appropriate.

**2.17 Commencement of Securities Lending, Repurchase and Reverse Repurchase Transactions by a Mutual Fund**

- (1) A mutual fund shall not enter into securities lending, repurchase or reverse repurchase transactions unless
  - (a) its simplified prospectus contains the disclosure required for mutual funds entering into those types of transactions; and

- (b) the mutual fund has provided to its securityholders, not less than 60 days before it begins entering into those types of transactions, written notice that discloses its intent to begin entering into those types of transactions and the disclosure required for mutual funds entering into those types of transactions.
- (2) Paragraph (1)(b) does not apply to a mutual fund that has entered into reverse repurchase agreements as permitted by a decision of the securities regulatory authority or regulator.
- (3) Paragraph (1)(b) does not apply if each simplified prospectus of the mutual fund since its inception contains the disclosure referred to in paragraph (1)(a).

### **PART 3 NEW MUTUAL FUNDS**

#### **3.1 Initial Investment in a New Mutual Fund**

- (1) No person or company shall file a simplified prospectus for a newly established mutual fund unless
  - (a) an investment of at least \$150,000 in securities of the mutual fund has been made, and those securities are beneficially owned, before the time of filing by
    - (i) the manager, a portfolio adviser, a promoter or a sponsor of the mutual fund,
    - (ii) the partners, directors, officers or securityholders of any of the manager, a portfolio adviser, a promoter or a sponsor of the mutual fund, or
    - (iii) a combination of the persons or companies referred to subparagraphs (i) and (ii);  
or
  - (b) the simplified prospectus of the mutual fund states that the mutual fund will not issue securities other than those referred to in paragraph (a) unless subscriptions aggregating not less than \$500,000 have been received by the mutual fund from investors other than the persons and companies referred to in paragraph (a) and accepted by the mutual fund.
- (2) A mutual fund shall not redeem a security issued upon an investment in the mutual fund referred to in paragraph (1)(a) until \$500,000 has been received from persons or companies other than the persons and companies referred to in paragraph (1)(a).

**3.2 Prohibition Against Distribution** - If a simplified prospectus of a mutual fund contains the disclosure described in paragraph 3.1(1)(b), the mutual fund shall not distribute any securities unless the subscriptions described in that disclosure, together with payment for the securities subscribed for, have been received.

**3.3 Prohibition Against Reimbursement of Organization Costs** - None of the costs of incorporation, formation or initial organization of a mutual fund, or of the preparation and filing of any of the preliminary simplified prospectus, preliminary annual information form, initial

simplified prospectus or annual information form of the mutual fund shall be borne by the mutual fund or its securityholders.

## **PART 4 CONFLICTS OF INTEREST**

### **4.1 Prohibited Investments**

- (1) A dealer managed mutual fund shall not knowingly make an investment in a class of securities of an issuer during, or for 60 days after, the period in which the dealer manager of the mutual fund, or an associate or affiliate of the dealer manager of the mutual fund, acts as an underwriter in the distribution of securities of that class of securities, except as a member of the selling group distributing five percent or less of the securities underwritten.
- (2) A dealer managed mutual fund shall not knowingly make an investment in a class of securities of an issuer of which a partner, director, officer or employee of the dealer manager of the mutual fund, or a partner, director, officer or employee of an affiliate or associate of the dealer manager, is a partner, director or officer, unless the partner, director, officer or employee
  - (a) does not participate in the formulation of investment decisions made on behalf of the dealer managed mutual fund;
  - (b) does not have access before implementation to information concerning investment decisions made on behalf of the dealer managed mutual fund; and
  - (c) does not influence, other than through research, statistical and other reports generally available to clients, the investment decisions made on behalf of the dealer managed mutual fund.
- (3) Subsections (1) and (2) do not apply to an investment in a class of securities issued or fully and unconditionally guaranteed by the government of Canada or the government of a jurisdiction.
- (4) Subsection (1) does not apply to an investment in a class of securities of an issuer if, at the time of each investment
  - (a) the independent review committee of the dealer managed mutual fund has approved the transaction under subsection 5.2(2) of NI 81-107;
  - (b) in a class of debt securities of an issuer other than a class of securities referred to in subsection (3), the security has been given, and continues to have, an approved rating by an approved credit rating organization;
  - (c) in any other class of securities of an issuer,
    - (i) the distribution of the class of equity securities is made by prospectus filed with one or more securities regulatory authorities or regulators in Canada, and
    - (ii) during the 60 day period referred to in subsection (1) the investment is made on an exchange on which the class of equity securities of the issuer is listed and

traded; and

- (d) no later than the time the dealer managed mutual fund files its annual financial statements, the manager of the dealer managed mutual fund files the particulars of each investment made by the dealer managed mutual fund during its most recently completed financial year.
- (5) The corresponding provisions contained in securities legislation referred to in Appendix C do not apply with respect to an investment in a class of securities of an issuer referred to in subsection (4) if the investment is made in accordance with that subsection.

#### **4.2 Self-Dealing**

- (1) A mutual fund shall not purchase a security from, sell a security to, or enter into a securities lending, repurchase or reverse repurchase transaction under section 2.12, 2.13 or 2.14 with, any of the following persons or companies:
  - 1. The manager, portfolio adviser or trustee of the mutual fund.
  - 2. A partner, director or officer of the mutual fund or of the manager, portfolio adviser or trustee of the mutual fund.
  - 3. An associate or affiliate of a person or company referred to in paragraph 1 or 2.
  - 4. A person or company, having fewer than 100 securityholders of record, of which a partner, director or officer of the mutual fund or a partner, director or officer of the manager or portfolio adviser of the mutual fund is a partner, director, officer or securityholder.
- (2) Subsection (1) applies in the case of a sale of a security to, or a purchase of a security from, a mutual fund only if the person or company that would be selling to, or purchasing from, the mutual fund would be doing so as principal.

#### **4.3 Exception**

- (1) Section 4.2 does not apply to a purchase or sale of a security by a mutual fund if the price payable for the security is
  - (a) not more than the ask price of the security as reported by any available public quotation in common use, in the case of a purchase by the mutual fund; or
  - (b) not less than the bid price of the security as reported by any available public quotation in common use, in the case of a sale by the mutual fund.
- (2) Section 4.2 does not apply to a purchase or sale of a class of debt securities by a mutual fund from, or to, another mutual fund managed by the same manager or an affiliate of the manager, if, at the time of the transaction

- (a) the mutual fund is purchasing from, or selling to, another mutual fund to which NI 81-107 applies;
- (b) the independent review committee of the mutual fund has approved the transaction under subsection 5.2(2) of NI 81-107; and
- (c) the transaction complies with subsection 6.1(2) of NI 81-107.

#### **4.4 Liability and Indemnification**

- (1) An agreement or declaration of trust by which a person or company acts as manager of a mutual fund shall provide that the manager is responsible for any loss that arises out of the failure of the manager, or of any person or company retained by the manager or the mutual fund to discharge any of the manager's responsibilities to the mutual fund,
  - (a) to exercise the powers and discharge the duties of its office honestly, in good faith and in the best interests of the mutual fund, and
  - (b) to exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances.
- (2) A mutual fund shall not relieve the manager of the mutual fund from liability for loss that arises out of the failure of the manager, or of any person retained by the manager or the mutual fund to discharge any of the manager's responsibilities to the mutual fund,
  - (a) to exercise the powers and discharge the duties of its office honestly, in good faith and in the best interests of the mutual fund, or
  - (b) to exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances.
- (3) A mutual fund may indemnify a person or company providing services to it against legal fees, judgments and amounts paid in settlement, actually and reasonably incurred by that person or company in connection with services provided by that person or company to the mutual fund, if
  - (a) those fees, judgments and amounts were not incurred as a result of a breach of the standard of care described in subsection (1) or (2); and
  - (b) the mutual fund has reasonable grounds to believe that the action or inaction that caused the payment of the fees, judgments and amounts paid in settlement was in the best interests of the mutual fund.
- (4) A mutual fund shall not incur the cost of any portion of liability insurance that insures a person or company for a liability except to the extent that the person or company may be indemnified for that liability under this section.
- (5) This section does not apply to any losses to a mutual fund or securityholder arising out of an action or inaction by

- (a) a director of the mutual fund; or
  - (b) a custodian or sub-custodian of the mutual fund, except as set out in subsection (6).
- (6) This section applies to any losses to a mutual fund or securityholder arising out of an action or inaction by a custodian or sub-custodian acting as agent of the mutual fund in administering the securities lending, repurchase or reverse repurchase transactions of the mutual fund.

## **PART 5 FUNDAMENTAL CHANGES**

**5.1 Matters Requiring Securityholder Approval** - The prior approval of the securityholders of a mutual fund, given as provided in section 5.2, is required before

- (a) the basis of the calculation of a fee or expense that is charged to the mutual fund or directly to its securityholders by the mutual fund or its manager in connection with the holding of securities of the mutual fund is changed in a way that could result in an increase in charges to the mutual fund or to its securityholders;
  - (a.1) a fee or expense, to be charged to the mutual fund or directly to its securityholders by the mutual fund or its manager in connection with the holding of securities of the mutual fund that could result in an increase in charges to the mutual fund or to its securityholders, is introduced;
- (b) the manager of the mutual fund is changed, unless the new manager is an affiliate of the current manager;
- (c) the fundamental investment objectives of the mutual fund are changed;
- (d) [Repealed]
- (e) the mutual fund decreases the frequency of the calculation of its net asset value per security;
- (f) the mutual fund undertakes a reorganization with, or transfers its assets to, another mutual fund, if
  - (i) the mutual fund ceases to continue after the reorganization or transfer of assets, and
  - (ii) the transaction results in the securityholders of the mutual fund becoming securityholders in the other mutual fund; or
- (g) the mutual fund undertakes a reorganization with, or acquires assets from, another mutual fund, if
  - (i) the mutual fund continues after the reorganization or acquisition of assets,
  - (ii) the transaction results in the securityholders of the other mutual fund becoming securityholders in the mutual fund, and
  - (iii) the transaction would be a material change to the mutual fund.

## **5.2 Approval of Securityholders**

- (1) Unless a greater majority is required by the constating documents of the mutual fund, the laws applicable to the mutual fund or an applicable agreement, the approval of the securityholders of the mutual fund to a matter referred to in section 5.1 shall be given by a resolution passed by at least a majority of the votes cast at a meeting of the securityholders of the mutual fund duly called and held to consider the matter.
- (2) Despite subsection (1), the holders of securities of a class or series of a class of securities of a mutual fund shall vote separately as a class or series of a class on a matter referred to in section 5.1 if that class or series of a class is affected by the action referred to in section 5.1 in a manner different from holders of securities of other classes or series of a class.
- (3) Despite section 5.1 and subsections (1) and (2), if the constating documents of the mutual fund so provide, the holders of securities of a class or series of a class of securities of a mutual fund shall not be entitled to vote on a matter referred to in section 5.1 if they, as holders of the class or series of a class, are not affected by the action referred to in section 5.1.

## **5.3 Circumstances in Which Approval of Securityholders Not Required**

- (1) Despite section 5.1, the approval of securityholders of a mutual fund is not required to be obtained for a change referred to in paragraph 5.1(a)
  - (a) if
    - (i) the mutual fund is at arm's length to the person or company charging the fee or expense to the mutual fund referred to in paragraph 5.1(a) that is changed,
    - (ii) the simplified prospectus of the mutual fund discloses that, although the approval of securityholders will not be obtained before making the changes, securityholders will be sent a written notice at least 60 days before the effective date of the change that is to be made that could result in an increase in charges to the mutual fund, and
    - (iii) the notice referred to in subparagraph (ii) is actually sent 60 days before the effective date of the change; or
  - (b) if
    - (i) the mutual fund is permitted by this Instrument to be described as a "no-load" fund,
    - (ii) the simplified prospectus of the mutual fund discloses that securityholders will be sent a written notice at least 60 days before the effective date of a change that is to be made that could result in an increase in charges to the mutual fund, and
    - (iii) the notice referred to in subparagraph (ii) is actually sent 60 days before the effective date of the change.

- (2) Despite section 5.1, the approval of securityholders of a mutual fund is not required to be obtained for a change referred to in paragraph 5.1(f) if
  - (a) the independent review committee of the mutual fund has approved the change under subsection 5.2(2) of NI 81-107;
  - (b) the mutual fund is being reorganized with, or its assets are being transferred to, another mutual fund to which this Instrument and NI 81-107 apply and that is managed by the manager, or an affiliate of the manager, of the mutual fund;
  - (c) the reorganization or transfer of assets of the mutual fund complies with the criteria in paragraphs 5.6(1)(a), (b), (c), (d), (g), (h) and (i) and subsection 5.6(2);
  - (d) the simplified prospectus of the mutual fund discloses that, although the approval of securityholders may not be obtained before making the change, securityholders will be sent a written notice at least 60 days before the effective date of the change; and
  - (e) the notice referred to in paragraph (d) to securityholders is sent 60 days before the effective date of the change.

**5.3.1 Change of Auditor of the Mutual Fund** – The auditor of the mutual fund may not be changed unless

- (a) the independent review committee of the mutual fund has approved the change of auditor under subsection 5.2(2) of NI 81-107;
- (b) the simplified prospectus of the mutual fund discloses that, although the approval of securityholders will not be obtained before making the change, securityholders will be sent a written notice at least 60 days before the effective date of the change, and
- (c) the notice referred to in paragraph (b) to securityholders is sent 60 days before the effective date of the change.

**5.4 Formalities Concerning Meetings of Securityholders**

- (1) A meeting of securityholders of a mutual fund called to consider any matter referred to in section 5.1 shall be called on written notice sent not less than 21 days before the date of the meeting.
- (2) The notice referred to in subsection (1) shall contain or be accompanied by a statement that includes
  - (a) a description of the change or transaction proposed to be made or entered into and, if the matter is one referred to in paragraph 5.1(a), the effect that the change would have had on the management expense ratio of the mutual fund had the change been in force throughout the mutual fund's last completed financial year;
  - (b) the date of the proposed implementation of the change or transaction; and

- (c) all other information and documents necessary to comply with the applicable proxy solicitation requirements of securities legislation for the meeting.

## **5.5 Approval of Securities Regulatory Authority**

- (1) The approval of the securities regulatory authority or regulator is required before
  - (a) the manager of a mutual fund is changed, unless the new manager is an affiliate of the current manager;
  - (b) a reorganization or transfer of assets of a mutual fund is implemented, if the transaction will result in the securityholders of the mutual fund becoming securityholders in another mutual fund;
  - (c) a change of the custodian of a mutual fund is implemented, if there has been or will be, in connection with the proposed change, a change of the type referred to in paragraph (a); or
  - (d) a mutual fund suspends, other than under section 10.6, the rights of securityholders to request that the mutual fund redeem their securities.
- (2) No person or company, or affiliate or associate of that person or company, may act as manager of a mutual fund if that person or company, or an affiliate or associate of that person or company, has acquired control of a manager of the mutual fund unless the approval of the securities regulatory authority or regulator has been obtained for the change in control.
- (3) Despite subsection (1), in Ontario only the regulator may grant an approval referred to in subsection (1).

## **5.6 Pre-Approved Reorganizations and Transfers**

- (1) Despite subsection 5.5(1), the approval of the securities regulatory authority or regulator is not required to implement a transaction referred to in paragraph 5.5(1)(b) if
  - (a) the mutual fund is being reorganized with, or its assets are being transferred to, another mutual fund to which this Instrument applies and that
    - (i) is managed by the manager, or an affiliate of the manager, of the mutual fund,
    - (ii) a reasonable person would consider to have substantially similar fundamental investment objectives, valuation procedures and fee structure as the mutual fund,
    - (iii) is not in default of any requirement of securities legislation, and
    - (iv) has a current simplified prospectus in the local jurisdiction;
  - (b) the transaction is a “qualifying exchange” within the meaning of section 132.2 of the ITA or is a tax-deferred transaction under subsection 85(1), 85.1(1), 86(1) or 87(1) of the ITA;

- (c) the transaction contemplates the wind-up of the mutual fund as soon as reasonably possible following the transaction;
- (d) the portfolio assets of the mutual fund to be acquired by the other mutual fund as part of the transaction
  - (i) may be acquired by the other mutual fund in compliance with this Instrument, and
  - (ii) are acceptable to the portfolio adviser of the other mutual fund and consistent with the other mutual fund's fundamental investment objectives;
- (e) the transaction is approved
  - (i) by the securityholders of the mutual fund in accordance with paragraph 5.1(f), and
  - (ii) if required, by the securityholders of the other mutual fund in accordance with paragraph 5.1(g);
- (f) the materials sent to securityholders of the mutual fund in connection with the approval under paragraph 5.1(f) include
  - (i) a circular that, in addition to other requirements prescribed by law, describes the proposed transaction, the mutual fund into which the mutual fund will be reorganized, the income tax considerations for the mutual funds participating in the transaction and their securityholders, and, if the mutual fund is a corporation and the transaction involves its shareholders becoming securityholders of a mutual fund that is established as a trust, a description of the material differences between being a shareholder of a corporation and being a securityholder of a trust,
  - (ii) if not previously sent to all securityholders, the current simplified prospectus and the most recent annual and interim financial statements that have been made public for the mutual fund into which the mutual fund will be reorganized, and
  - (iii) a statement that securityholders may obtain an annual information form for the mutual fund into which the mutual fund will be reorganized by contacting that mutual fund at a specified address or telephone number;
- (g) the mutual fund has complied with Part 11 of National Instrument 81-106 *Investment Fund Continuous Disclosure* in connection with the making of the decision to proceed with the transaction by the board of directors of the manager of the mutual fund or of the mutual fund;
- (h) the mutual funds participating in the transaction bear none of the costs and expenses associated with the transaction; and

- (i) securityholders of the mutual fund continue to have the right to redeem securities of the mutual fund up to the close of business on the business day immediately before the effective date of the transaction.
- (2) A mutual fund that has continued after a transaction described in paragraph 5.5(1)(b) shall, if the audit report accompanying its audited financial statements for its first completed financial year after the transaction contains a reservation in respect of the value of the portfolio assets acquired by the mutual fund in the transaction, send a copy of those financial statements to each person or company that was a securityholder of a mutual fund that was terminated as a result of the transaction and that is not a securityholder of the mutual fund.

## **5.7 Applications**

- (1) An application for an approval required under section 5.5 shall contain,
  - (a) if the application is required by paragraph 5.5(1)(a) or subsection 5.5(2),
    - (i) details of the proposed transaction,
    - (ii) details of the proposed new manager or the person or company proposing to acquire control of the manager,
    - (iii) as applicable, the names, residence addresses and birthdates of
      - (A) all proposed new partners, directors or officers of the manager,
      - (B) all partners, directors or officers of the person or company proposing to acquire control of the manager,
      - (C) any proposed new individual trustee of the mutual fund, and
      - (D) any new directors or officers of the mutual fund,
    - (iv) all information necessary to permit the securities regulatory authority to conduct security checks on the individuals referred to in subparagraph (iii),
    - (v) sufficient information to establish the integrity and experience of the persons or companies referred to in subparagraphs (ii) and (iii), and
    - (vi) details of how the proposed transaction will affect the management and administration of the mutual fund;
  - (b) if the application is required by paragraph 5.5(1)(b),
    - (i) details of the proposed transaction,
    - (ii) details of the total annual returns of each of the mutual funds for each of the

- previous five years,
- (iii) a description of the differences between the fundamental investment objectives, investment strategies, valuation procedures and fee structure of each of the mutual funds and any other material differences between the mutual funds, and
  - (iv) a description of those elements of the proposed transaction that make section 5.6 inapplicable;
- (c) if the application is required by paragraph 5.5(1)(c), sufficient information to establish that the proposed custodial arrangements will be in compliance with Part 6;
  - (d) if the application relates to a matter that would constitute a material change for the mutual fund, a draft of an amendment to the simplified prospectus of the mutual fund reflecting the change; and
  - (e) if the matter is one that requires the approval of securityholders, confirmation that the approval has been obtained or will be obtained before the change is implemented.
- (2) A mutual fund that applies for an approval under paragraph 5.5(1)(d) shall
- (a) make that application to the securities regulatory authority or regulator in the jurisdiction in which the head office or registered office of the mutual fund is situate; and
  - (b) concurrently file a copy of the application so made with the securities regulatory authority or the regulator in the local jurisdiction if the head office or registered office of the mutual fund is not situated in the local jurisdiction.
- (3) A mutual fund that has complied with subsection (2) in the local jurisdiction may suspend the right of securityholders to request that the mutual fund redeem their securities if
- (a) the securities regulatory authority or regulator in the jurisdiction in which the head office or registered office of the mutual fund is situate has granted approval to the application made under paragraph (2)(a); and
  - (b) the securities regulatory authority or regulator in the local jurisdiction has not notified the mutual fund, by the close of business on the business day immediately following the day on which the copy of the application referred to in paragraph (2)(b) was received, either that
    - (i) the securities regulatory authority or regulator has refused to grant approval to the application, or
    - (ii) this subsection may not be relied upon by the mutual fund in the local jurisdiction.

## 5.8 Matters Requiring Notice

- (1) No person or company that is a manager of a mutual fund may continue to act as manager of the mutual fund following a direct or indirect change of control of the person or company unless
  - (a) notice of the change of control was given to all securityholders of the mutual fund at least 60 days before the change; and
  - (b) the notice referred to in paragraph (a) contains the information that would be required by law to be provided to securityholders if securityholder approval of the change were required to be obtained.
- (2) No mutual fund shall terminate unless notice of the termination is given to all securityholders of the mutual fund at least 60 days before termination.
- (3) The manager of a mutual fund that has terminated shall give notice of the termination to the securities regulatory authority within 30 days of the termination.

### **5.9 Relief from Certain Regulatory Requirements**

- (1) The mutual fund conflict of interest investment restrictions and the mutual fund conflict of interest reporting requirements do not apply to a transaction referred to in paragraph 5.5(1)(b) if the approval of the securities regulatory authority or regulator has been given to the transaction.
- (2) The mutual fund conflict of interest investment restrictions and the mutual fund conflict of interest reporting requirements do not apply to a transaction described in section 5.6.

### **5.10 [Repealed]**

## **PART 6 CUSTODIANSHIP OF PORTFOLIO ASSETS**

### **6.1 General**

- (1) Except as provided in sections 6.8 and 6.9, all portfolio assets of a mutual fund shall be held under the custodianship of one custodian that satisfies the requirements of section 6.2.
- (2) Except as provided in subsection 6.5(3) and sections 6.8 and 6.9, portfolio assets of a mutual fund shall be held
  - (a) in Canada by the custodian or a sub-custodian of the mutual fund; or
  - (b) outside Canada by the custodian or a sub-custodian of the mutual fund, if appropriate to facilitate portfolio transactions of the mutual fund outside Canada.
- (3) The custodian or a sub-custodian of a mutual fund may appoint one or more sub-custodians to hold portfolio assets of the mutual fund, if, for each appointment,
  - (a) written consent to the appointment has been provided by the mutual fund and, if the appointment is by a sub-custodian, the custodian of the mutual fund;

- (b) the sub-custodian that is to be appointed is a person or company described in section 6.2 or 6.3, as applicable;
  - (c) the arrangements under which a sub-custodian is appointed are such that the mutual fund may enforce rights directly, or require the custodian or a sub-custodian to enforce rights on behalf of the mutual fund, to the portfolio assets held by the appointed sub-custodian; and
  - (d) the appointment is otherwise in compliance with this Instrument.
- (4) The written consent referred to in paragraph (3)(a) may be in the form of a general consent, contained in the agreement governing the relationship between the mutual fund and the custodian, or the custodian and the sub-custodian, to the appointment of persons or companies that are part of an international network of sub-custodians within the organization of the appointed custodian or sub-custodian.
- (5) A custodian or sub-custodian shall provide to the mutual fund a list of each person or company that is appointed sub-custodian under a general consent referred to in subsection (4).
- (6) Despite any other provisions of this Part, the manager of a mutual fund shall not act as custodian or sub-custodian of the mutual fund.

**6.2 Entities Qualified to Act as Custodian or Sub-Custodian for Assets Held in Canada** - The custodian of a mutual fund, and a sub-custodian of a mutual fund that is to hold portfolio assets of the mutual fund in Canada, shall be one of the following:

1. A bank listed in Schedule I, II or III of the *Bank Act* (Canada).
2. A trust company that is incorporated under the laws of Canada or a jurisdiction and licensed or registered under the laws of Canada or a jurisdiction, and that has shareholders' equity, as reported in its most recent audited financial statements, of not less than \$10,000,000.
3. A company that is incorporated under the laws of Canada or of a jurisdiction, and that is an affiliate of a bank or trust company referred to in paragraph 1 or 2, if
  - (a) the company has shareholders' equity, as reported in its most recent audited financial statements that have been made public, of not less than \$10,000,000; or
  - (b) the bank or trust company has assumed responsibility for all of the custodial obligations of the company in respect of that mutual fund.

**6.3 Entities Qualified to Act as Sub-Custodian for Assets Held outside Canada** – A sub-custodian of a mutual fund that is to hold portfolio assets of the mutual fund outside of Canada shall be one of the following:

1. An entity referred to in section 6.2.

2. An entity that
  - (a) is incorporated or organized under the laws of a country, or a political subdivision of a country, other than Canada;
  - (b) is regulated as a banking institution or trust company by the government, or an agency of the government, of the country under whose laws it is incorporated or organized or a political subdivision of that country; and
  - (c) has shareholders' equity, as reported in its most recent audited financial statements, of not less than the equivalent of \$100,000,000.
3. An affiliate of an entity referred to in paragraph 1 or 2 if
  - (a) the affiliate has shareholders' equity, as reported in its most recent audited financial statements that have been made public, of not less than the equivalent of \$100,000,000; or
  - (b) the entity referred to in paragraph 1 or 2 has assumed responsibility for all of the custodial obligations of the affiliate in respect of that mutual fund.

#### **6.4 Contents of Custodian and Sub-Custodian Agreements**

- (1) All custodian agreements and sub-custodian agreements of a mutual fund shall provide for matters relating to
  - (a) the requirements concerning the location of portfolio assets contained in subsection 6.1(2);
  - (b) the appointment of a sub-custodian required by subsection 6.1(3);
  - (c) the requirements concerning lists of sub-custodians contained in subsection 6.1(5);
  - (d) the method of holding portfolio assets required by section 6.5 and subsection 6.8(4);
  - (e) the standard of care and responsibility for loss required by section 6.6; and
  - (f) the review and compliance reports required by section 6.7.
- (2) A sub-custodian agreement concerning the portfolio assets of a mutual fund shall provide for the safekeeping of portfolio assets on terms consistent with the custodian agreement of the mutual fund.
- (3) No custodian agreement or sub-custodian agreement concerning the portfolio assets of a mutual fund shall
  - (a) provide for the creation of any security interest on the portfolio assets of the mutual fund

except for a good faith claim for payment of the fees and expenses of the custodian or sub-custodian for acting in that capacity or to secure the obligations of the mutual fund to repay borrowings by the mutual fund from a custodian or sub-custodian for the purpose of settling portfolio transactions; or

- (b) contain a provision that would require the payment of a fee to the custodian or sub-custodian for the transfer of the beneficial ownership of portfolio assets of the mutual fund, other than for safekeeping and administrative services in connection with acting as custodian or sub-custodian.

## **6.5 Holding of Portfolio Assets and Payment of Fees**

- (1) Except as provided in subsections (2) and (3) and sections 6.8 and 6.9, portfolio assets of a mutual fund not registered in the name of the mutual fund shall be registered in the name of the custodian or a sub-custodian of the mutual fund or any of their respective nominees with an account number or other designation in the records of the custodian sufficient to show that the beneficial ownership of the portfolio assets is vested in the mutual fund.
- (2) Portfolio assets of a mutual fund issued in bearer form shall be designated or segregated by the custodian or a sub-custodian of the mutual fund or the applicable nominee so as to show that the beneficial ownership of the property is vested in the mutual fund.
- (3) A custodian or sub-custodian of a mutual fund may deposit portfolio assets of the mutual fund with a depository, or a clearing agency, that operates a book-based system.
- (4) The custodian or sub-custodian of a mutual fund arranging for the deposit of portfolio assets of the mutual fund with, and their delivery to, a depository, or clearing agency, that operates a book-based system shall ensure that the records of any of the applicable participants in that book-based system or the custodian contain an account number or other designation sufficient to show that the beneficial ownership of the portfolio assets is vested in the mutual fund.
- (5) A mutual fund shall not pay a fee to a custodian or sub-custodian for the transfer of beneficial ownership of portfolio assets of the mutual fund other than for safekeeping and administrative services in connection with acting as custodian or sub-custodian.

## **6.6 Standard of Care**

- (1) The custodian and each sub-custodian of a mutual fund, in carrying out their duties concerning the safekeeping of, and dealing with, the portfolio assets of the mutual fund, shall exercise
  - (a) the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances; or
  - (b) at least the same degree of care as they exercise with respect to their own property of a similar kind, if this is a higher degree of care than the degree of care referred to in paragraph (a).
- (2) A mutual fund shall not relieve the custodian or a sub-custodian of the mutual fund from liability

to the mutual fund or to a securityholder of the mutual fund for loss that arises out of the failure of the custodian or sub-custodian to exercise the standard of care imposed by subsection (1).

- (3) A mutual fund may indemnify a custodian or sub-custodian against legal fees, judgments and amounts paid in settlement, actually and reasonably incurred by that entity in connection with custodial or sub-custodial services provided by that entity to the mutual fund, if those fees, judgments and amounts were not incurred as a result of a breach of the standard of care described in subsection (1).
- (4) A mutual fund shall not incur the cost of any portion of liability insurance that insures a custodian or sub-custodian for a liability, except to the extent that the custodian or sub-custodian may be indemnified for that liability under this section.

## **6.7 Review and Compliance Reports**

- (1) The custodian of a mutual fund shall, on a periodic basis not less frequently than annually,
  - (a) review the custodian agreement and all sub-custodian agreements of the mutual fund to determine if those agreements are in compliance with this Part;
  - (b) make reasonable enquiries as to whether each sub-custodian satisfies the applicable requirements of section 6.2 or 6.3; and
  - (c) make or cause to be made any changes that may be necessary to ensure that
    - (i) the custodian and sub-custodian agreements are in compliance with this Part; and
    - (ii) all sub-custodians of the mutual fund satisfy the applicable requirements of section 6.2 or 6.3.
- (2) The custodian of a mutual fund shall, not more than 60 days after the end of each financial year of the mutual fund, advise the mutual fund in writing
  - (a) of the names and addresses of all sub-custodians of the mutual fund;
  - (b) whether the custodian and sub-custodian agreements are in compliance with this Part; and
  - (c) whether, to the best of the knowledge and belief of the custodian, each sub-custodian satisfies the applicable requirements of section 6.2 or 6.3.
- (3) A copy of the report referred to in subsection (2) shall be delivered by or on behalf of the mutual fund to the securities regulatory authority within 30 days after the filing of the annual financial statements of the mutual fund.

## **6.8 Custodial Provisions relating to Derivatives and Securities Lending, Repurchase and Reverse Repurchase Agreements**

- (1) A mutual fund may deposit portfolio assets as margin for transactions in Canada involving

clearing corporation options, options on futures or standardized futures with a dealer that is a member of an SRO that is a participating member of CIPF if the amount of margin deposited does not, when aggregated with the amount of margin already held by the dealer on behalf of the mutual fund, exceed 10 percent of the net assets of the mutual fund, taken at market value as at the time of deposit.

- (2) A mutual fund may deposit portfolio assets with a dealer as margin for transactions outside Canada involving clearing corporation options, options on futures or standardized futures if
  - (a) in the case of standardized futures and options on futures, the dealer is a member of a futures exchange or, in the case of clearing corporation options, is a member of a stock exchange, and, as a result in either case, is subject to a regulatory audit;
  - (b) the dealer has a net worth, determined from its most recent audited financial statements that have been made public, in excess of the equivalent of \$50 million; and
  - (c) the amount of margin deposited does not, when aggregated with the amount of margin already held by the dealer on behalf of the mutual fund, exceed 10 percent of the net assets of the mutual fund, taken at market value as at the time of deposit.
- (3) A mutual fund may deposit with its counterparty portfolio assets over which it has granted a security interest in connection with a particular specified derivatives transaction.
- (4) The agreement by which portfolio assets of a mutual fund are deposited in accordance with subsection (1), (2) or (3) shall require the person or company holding portfolio assets of the mutual fund so deposited to ensure that its records show that that mutual fund is the beneficial owner of the portfolio assets.
- (5) A mutual fund may deliver portfolio assets to a person or company in satisfaction of its obligations under a securities lending, repurchase or reverse purchase agreement that complies with this Instrument if the collateral, cash proceeds or purchased securities that are delivered to the mutual fund in connection with the transaction are held under the custodianship of the custodian or a sub-custodian of the mutual fund in compliance with this Part.

**6.9 Separate Account for Paying Expenses** - A mutual fund may deposit cash in Canada with an institution referred to in paragraph 1 or 2 of section 6.2 to facilitate the payment of regular operating expenses of the mutual fund.

## **PART 7 INCENTIVE FEES**

**7.1 Incentive Fees** - A mutual fund shall not pay, or enter into arrangements that would require it to pay, and no securities of a mutual fund shall be sold on the basis that an investor would be required to pay, a fee that is determined by the performance of the mutual fund, unless

- (a) the fee is calculated with reference to a benchmark or index that
  - (i) reflects the market sectors in which the mutual fund invests according to its fundamental investment objectives,

- (ii) is available to persons or companies other than the mutual fund and persons providing services to it, and
- (iii) is a total return benchmark or index;
- (b) the payment of the fee is based upon a comparison of the cumulative total return of the mutual fund against the cumulative total percentage increase or decrease of the benchmark or index for the period that began immediately after the last period for which the performance fee was paid; and
- (c) the method of calculation of the fee and details of the composition of the benchmark or index are described in the simplified prospectus of the mutual fund.

**7.2 Multiple Portfolio Advisers** - Section 7.1 applies to fees payable to a portfolio adviser of a mutual fund that has more than one portfolio adviser, if the fees are calculated on the basis of the performance of the portfolio assets under management by that portfolio adviser, as if those portfolio assets were a separate mutual fund.

## **PART 8 CONTRACTUAL PLANS**

**8.1 Contractual Plans** - No securities of a mutual fund shall be sold by way of a contractual plan unless

- (a) the contractual plan was established, and its terms described in a simplified prospectus that was filed with the securities regulatory authority, before the date that this Instrument came into force;
- (b) there have been no changes made to the contractual plan or the rights of securityholders under the contractual plan since the date that this Instrument came into force; and
- (c) the contractual plan has continued to be operated in the same manner after the date that this Instrument came into force as it was on that date.

## **PART 9 SALE OF SECURITIES OF A MUTUAL FUND**

**9.1 Transmission and Receipt of Purchase Orders**

- (1) Each purchase order for securities of a mutual fund received by a participating dealer at a location that is not its principal office shall, on the day the order is received, be sent by same day or next day courier, same day or next day priority post, telephone or electronic means, without charge to the person or company placing the order or to the mutual fund, to the principal office of the participating dealer or a person or company providing services to the participating dealer.
- (2) Each purchase order for securities of a mutual fund received by a participating dealer at its principal office, a person or company providing services to the participating dealer, or by the principal distributor of the mutual fund at a location that is not an order receipt office of the mutual fund shall, on the day the order is received, be sent by same day or next day courier, same

day or next day priority post, telephone or electronic means, without charge to the person or company placing the order or to the mutual fund, to an order receipt office of the mutual fund.

- (3) Despite subsections (1) and (2), a purchase order for securities of a mutual fund received at a location referred to in those subsections after normal business hours on a business day, or on a day that is not a business day, may be sent, in the manner and to the place required by those subsections, on the next business day.
- (4) A participating dealer, a principal distributor or a person or company providing services to the participating dealer or principal distributor, that sends purchase orders electronically may
  - (a) specify a time on a business day by which a purchase order must be received in order that it be sent electronically on that business day; and
  - (b) despite subsections (1) and (2), send electronically on the next business day a purchase order received after the time specified under paragraph (a).
- (5) A mutual fund is deemed to have received a purchase order for securities of the mutual fund when the order is received at an order receipt office of the mutual fund.
- (6) Despite subsection (5), a mutual fund may provide that a purchase order for securities of the mutual fund received at an order receipt office of the mutual fund after a specified time on a business day, or on a day that is not a business day, will be considered to be received by the mutual fund on the next business day following the day of actual receipt.
- (7) A principal distributor or participating dealer shall ensure that a copy of each purchase order received in a jurisdiction is sent, by the time it is sent to the order receipt office of the mutual fund under subsection (2), to a person responsible for the supervision of trades made on behalf of clients for the principal distributor or participating dealer in the jurisdiction.

**9.2 Acceptance of Purchase Orders** - A mutual fund may reject a purchase order for the purchase of securities of the mutual fund if

- (a) the rejection of the order is made no later than one business day after receipt by the mutual fund of the order;
- (b) on rejection of the order, all cash received with the order is refunded immediately; and
- (c) the simplified prospectus of the mutual fund states that the right to reject a purchase order for securities of the mutual fund is reserved and reflects the requirements of paragraphs (a) and (b).

**9.3 Issue Price of Securities** - The issue price of a security of a mutual fund to which a purchase order pertains shall be the net asset value per security of that class, or series of a class, next determined after the receipt by the mutual fund of the order.

**9.4 Delivery of Funds and Settlement**

- (1) A principal distributor, a participating dealer, or a person or company providing services to the principal distributor or participating dealer shall forward any cash received for payment of the issue price of securities of a mutual fund to an order receipt office of the mutual fund so that the cash arrives at the order receipt office as soon as practicable and in any event no later than the third business day after the pricing date.
- (2) Payment of the issue price of securities of a mutual fund shall be made to the mutual fund on or before the third business day after the pricing date for the securities by
  - (a) a payment of cash in a currency in which the net asset value per security of the mutual fund is calculated; or
  - (b) good delivery of securities if
    - (i) the mutual fund would at the time of payment be permitted to purchase those securities,
    - (ii) the securities are acceptable to the portfolio adviser of the mutual fund and consistent with the mutual fund's investment objectives, and
    - (iii) the value of the securities is at least equal to the issue price of the securities of the mutual fund for which they are payment, valued as if the securities were portfolio assets of the mutual fund.
- (3) [Repealed]
- (4) If payment of the issue price of the securities of a mutual fund to which a purchase order pertains is not made on or before the third business day after the pricing date or if the mutual fund has been paid the issue price by a cheque or method of payment that is subsequently not honoured,
  - (a) the mutual fund shall redeem the securities to which the purchase order pertains as if it had received an order for the redemption of the securities on the fourth business day after the pricing date or on the day on which the mutual fund first knows that the method of payment will not be honoured; and
  - (b) the amount of the redemption proceeds derived from the redemption shall be applied to reduce the amount owing to the mutual fund on the purchase of the securities and any banking costs incurred by the mutual fund in connection with the dishonoured cheque.
- (5) If the amount of the redemption proceeds referred to in subsection (4) exceeds the aggregate of issue price of the securities and any banking costs incurred by the mutual fund in connection with the dishonoured cheque, the difference shall belong to the mutual fund.
- (6) If the amount of the redemption proceeds referred to in subsection (4) is less than the issue price of the securities and any banking costs incurred by the mutual fund in connection with the dishonoured cheque,
  - (a) if the mutual fund has a principal distributor, the principal distributor shall pay,

immediately upon notification by the mutual fund, to the mutual fund the amount of the deficiency; or

- (b) if the mutual fund does not have a principal distributor, the participating dealer that delivered the relevant purchase order to the mutual fund shall pay immediately, upon notification by the mutual fund, to the mutual fund the amount of the deficiency.

## **PART 10 REDEMPTION OF SECURITIES OF A MUTUAL FUND**

### **10.1 Requirements for Redemptions**

- (1) No mutual fund shall pay redemption proceeds unless
  - (a) if the security of the mutual fund to be redeemed is represented by a certificate, the mutual fund has received the certificate or appropriate indemnities in connection with a lost certificate; and
  - (b) either
    - (i) the mutual fund has received a written redemption order, duly completed and executed by or on behalf of the securityholder, or
    - (ii) the mutual fund permits the making of redemption orders by telephone or electronic means by, or on behalf of, a securityholder who has made prior arrangements with the mutual fund in that regard and the relevant redemption order is made in compliance with those arrangements.
- (2) A mutual fund may establish reasonable requirements applicable to securityholders who wish to have the mutual fund redeem securities, not contrary to this Instrument, as to procedures to be followed and documents to be delivered
  - (a) by the time of delivery of a redemption order to an order receipt office of the mutual fund; or
  - (b) by the time of payment of redemption proceeds.
- (3) The manager shall provide to securityholders of a mutual fund at least annually a statement outlining the requirements referred to in subsection (1) and established by the mutual fund under subsection (2), and containing
  - (a) detailed reference to all documentation required for redemption of securities of the mutual fund;
  - (b) detailed instructions on the manner in which documentation is to be delivered to participating dealers or the mutual fund;
  - (c) a description of all other procedural or communication requirements; and

- (d) an explanation of the consequences of failing to meet timing requirements.
- (4) The statement referred to in subsection (3) is not required to be separately provided, in any year, if the requirements are described in any document that is sent to all securityholders in that year.

## **10.2 Transmission and Receipt of Redemption Orders**

- (1) Each redemption order for securities of a mutual fund received by a participating dealer at a location that is not its principal office shall, on the day the order is received, be sent by same day or next day courier, same day or next day priority post, telephone or electronic means, without charge to the relevant securityholder or to the mutual fund, to the principal office of the participating dealer or a person or company providing services to the participating dealer.
- (2) Each redemption order for securities of a mutual fund received by a participating dealer at its principal office, by the principal distributor of the mutual fund at a location that is not an order receipt office of the mutual fund, or a person or company providing services to the participating dealer or principal distributor shall, on the day the order is received, be sent by same day or next day courier, same day or next day priority post, telephone or electronic means, without charge to the relevant securityholder or to the mutual fund, to an order receipt office of the mutual fund.
- (3) Despite subsections (1) and (2), a redemption order for securities of a mutual fund received at a location referred to in those subsections after normal business hours on a business day, or on a day that is not a business day, may be sent, in the manner and to the place required by those subsections, on the next business day.
- (4) A participating dealer, a principal distributor, or a person or company providing services to the participating dealer or principal distributor, that sends redemption orders electronically may
  - (a) specify a time on a business day by which a redemption order must be received in order that it be sent electronically on that business day; and
  - (b) despite subsections (1) and (2), send electronically on the next business day a redemption order received after the time specified under paragraph (a).
- (5) A mutual fund is deemed to have received a redemption order for securities of the mutual fund when the order is received at an order receipt office of the mutual fund or all requirements of the mutual fund established under paragraph 10.1(2)(a) have been satisfied, whichever is later.
- (6) If a mutual fund determines that its requirements established under paragraph 10.1(2)(a) have not been satisfied, the mutual fund shall notify the securityholder making the redemption order, by the close of business on the business day after the date of the delivery to the mutual fund of the incomplete redemption order, that its requirements established under paragraph 10.1(2)(a) have not been satisfied and shall specify procedures still to be followed or the documents still to be delivered by that securityholder.
- (7) Despite subsection (5), a mutual fund may provide that orders for the redemption of securities that are received at an order receipt office of the mutual fund after a specified time on a business day, or on a day that is not a business day, will be considered to be received by the mutual fund

on the next business day following the day of actual receipt.

**10.3 Redemption Price of Securities** - The redemption price of a security of a mutual fund to which a redemption order pertains shall be the net asset value of a security of that class, or series of a class, next determined after the receipt by the mutual fund of the order.

**10.4 Payment of Redemption Price**

(1) Subject to subsection 10.1(1) and to compliance with any requirements established by the mutual fund under paragraph 10.1(2)(b), a mutual fund shall pay the redemption price for securities that are the subject of a redemption order

(a) within three business days after the date of calculation of the net asset value per security used in establishing the redemption price; or

(b) if payment of the redemption price was not made at the time referred to in paragraph (a) because a requirement established under paragraph 10.1(2)(b) or a requirement of subsection 10.1(1) had not been satisfied, within three business days of

(i) the satisfaction of the relevant requirement, or

(ii) the decision by the mutual fund to waive the requirement, if the requirement was a requirement established under paragraph 10.1(2)(b).

(2) The redemption price of a security, less any applicable investor fees, shall be paid to or to the order of the securityholder of the security.

(3) A mutual fund shall pay the redemption price of a security

(a) in the currency in which the net asset value per security of the redeemed security was denominated; or

(b) with the prior written consent of the securityholder, by making good delivery to the securityholder of portfolio assets, the value of which is equal to the amount at which those portfolio assets were valued in calculating the net asset value per security used to establish the redemption price.

(4) [Repealed]

(5) If the redemption price of a security is paid in currency, a mutual fund is deemed to have made payment

(a) when the mutual fund, its manager or principal distributor mails a cheque or transmits funds in the required amount to or to the order of the securityholder of the securities; or

(b) if the securityholder has requested that redemption proceeds be delivered in a currency other than that permitted in subsection (3), when the mutual fund delivers the redemption proceeds to the manager or principal distributor of the mutual fund for conversion into

that currency and delivery forthwith to the securityholder.

### **10.5 Failure to Complete Redemption Order**

- (1) If a requirement of a mutual fund referred to in subsection 10.1(1) or established under paragraph 10.1(2)(b) has not been satisfied on or before the close of business on the tenth business day after the date of the redemption of the relevant securities, and, in the case of a requirement established under paragraph 10.1(2)(b), the mutual fund does not waive satisfaction of the requirement, the mutual fund shall
  - (a) issue, to the person or company that immediately before the redemption held the securities that were redeemed, a number of securities equal to the number of securities that were redeemed, as if the mutual fund had received from the person or company on the tenth business day after the redemption, and accepted immediately before the close of business on the tenth business day after the redemption, an order for the purchase of that number of securities; and
  - (b) apply the amount of the redemption proceeds to the payment of the issue price of the securities.
- (2) If the amount of the issue price of the securities referred to in subsection (1) is less than the redemption proceeds, the difference shall belong to the mutual fund.
- (3) If the amount of the issue price of the securities referred to in subsection (1) exceeds the redemption proceeds
  - (a) if the mutual fund has a principal distributor, the principal distributor shall pay immediately to the mutual fund the amount of the deficiency;
  - (b) if the mutual fund does not have a principal distributor, the participating dealer that delivered the relevant redemption order to the mutual fund shall pay immediately to the mutual fund the amount of the deficiency; or
  - (c) if the mutual fund has no principal distributor and no dealer delivered the relevant redemption order to the mutual fund, the manager of the mutual fund shall pay immediately to the mutual fund the amount of the deficiency.

### **10.6 Suspension of Redemptions**

- (1) A mutual fund may suspend the right of securityholders to request that the mutual fund redeem its securities for the whole or any part of a period during which normal trading is suspended on a stock exchange, options exchange or futures exchange within or outside Canada on which securities are listed and traded, or on which specified derivatives are traded, if those securities or specified derivatives represent more than 50 percent by value, or underlying market exposure, of the total assets of the mutual fund without allowance for liabilities and if those securities or specified derivatives are not traded on any other exchange that represents a reasonably practical alternative for the mutual fund.

- (2) A mutual fund that has an obligation to pay the redemption price for securities that have been redeemed in accordance with subsection 10.4(1) may postpone payment during a period in which the right of securityholders to request redemption of their securities is suspended, whether that suspension was made under subsection (1) or pursuant to an approval of the securities regulatory authority.
- (3) A mutual fund shall not accept a purchase order for securities of the mutual fund during a period in which it is exercising rights under subsection (1) or at a time in which it is relying on an approval of the securities regulatory authorities contemplated by paragraph 5.5(1)(d).

## **PART 11 COMMINGLING OF CASH**

### **11.1 Principal Distributors**

- (1) Cash received by a principal distributor of a mutual fund, or by a person or company providing services to the mutual fund or the principal distributor, for investment in, or on the redemption of, securities of the mutual fund, or on the distribution of assets of the mutual fund, until disbursed as permitted by subsection (3),
  - (a) shall be accounted for separately and be deposited in a trust account or trust accounts established and maintained in accordance with the requirements of section 11.3; and
  - (b) may be commingled only with cash received by the principal distributor or service provider for the sale or on the redemption of other mutual fund securities.
- (2) Except as permitted by subsection (3), the principal distributor or person or company providing services to the mutual fund or principal distributor shall not use any of the cash referred to in subsection (1) to finance its own or any other operations in any way.
- (3) The principal distributor or person or company providing services to a mutual fund or principal distributor may withdraw cash from a trust account referred to in paragraph (1)(a) for the purpose of
  - (a) remitting to the mutual fund the amount or, if subsection (5) applies, the net amount, to be invested in the securities of the mutual fund;
  - (b) remitting to the relevant persons or companies redemption or distribution proceeds being paid on behalf of the mutual fund; or
  - (c) paying fees, charges and expenses that are payable by an investor in connection with the purchase, conversion, holding, transfer or redemption of securities of the mutual fund.
- (4) All interest earned on cash held in a trust account referred to in paragraph (1)(a) shall be paid to securityholders or to each of the mutual funds to which the trust account pertains, pro rata based on cash flow,
  - (a) no less frequently than monthly if the amount owing to a mutual fund or to a securityholder is \$10 or more; and

- (b) no less frequently than once a year.
- (5) When making payments to a mutual fund, the principal distributor or service provider may offset the proceeds of redemption of securities of the mutual fund or amounts held for distributions to be paid on behalf of the mutual fund held in the trust account against amounts held in the trust account for investment in the mutual fund.

## 11.2 Participating Dealers

- (1) Cash received by a participating dealer, or by a person or company providing services to a participating dealer, for investment in, or on the redemption of, securities of a mutual fund, or on the distribution of assets of a mutual fund, until disbursed as permitted by subsection (3)
  - (a) shall be accounted for separately and shall be deposited in a trust account or trust accounts established and maintained in accordance with section 11.3; and
  - (b) may be commingled only with cash received by the participating dealer or service provider for the sale or on the redemption of other mutual fund securities.
- (2) Except as permitted by subsection (3), the participating dealer or person or company providing services to the participating dealer shall not use any of the cash referred to subsection (1) to finance its own or any other operations in any way.
- (3) A participating dealer or person or company providing services to the participating dealer may withdraw cash from a trust account referred to in paragraph (1)(a) for the purpose of
  - (a) remitting to the mutual fund or the principal distributor of the mutual fund the amount or, if subsection (5) applies, the net amount, to be invested in the securities of the mutual fund;
  - (b) remitting to the relevant persons or companies redemption or distribution proceeds being paid on behalf of the mutual fund; or
  - (c) paying fees, charges and expenses that are payable by an investor in connection with the purchase, conversion, holding, transfer or redemption of securities of the mutual fund.
- (4) All interest earned on cash held in a trust account referred to in paragraph (1)(a) shall be paid to securityholders or to each of the mutual funds to which the trust account pertains, pro rata based on cash flow,
  - (a) no less frequently than monthly if the amount owing to a mutual fund or to a securityholder is \$10 or more; and
  - (b) no less frequently than once a year.
- (5) When making payments to a mutual fund, a participating dealer or service provider may offset the proceeds of redemption of securities of the mutual fund and amounts held for distributions to be

paid on behalf of a mutual fund held in the trust account against amounts held in the trust account for investment in the mutual fund.

- (6) A participating dealer or person providing services to the participating dealer shall permit the mutual fund and the principal distributor, through their respective auditors or other designated representatives, to examine the books and records of the participating dealer to verify the compliance with this section of the participating dealer or person providing services.

**11.3 Trust Accounts** – A principal distributor or participating dealer, or a person or company providing services to the principal distributor or participating dealer, that deposits cash into a trust account in accordance with section 11.1 or 11.2 shall

- (a) advise, in writing, the financial institution with which the account is opened at the time of the opening of the account and annually thereafter, that
- (i) the account is established for the purpose of holding client funds in trust,
  - (ii) the account is to be labelled by the financial institution as a “trust account”,
  - (iii) the account is not to be accessed by any person other than authorized representatives of the principal distributor or participating dealer or of a person or company providing services to the principal distributor or participating dealer, and
  - (iv) the cash in the trust account may not be used to cover shortfalls in any accounts of the principal distributor or participating dealer, or of a person or company providing services to the principal distributor or participating dealer,
- (b) ensure that the trust account bears interest at rates equivalent to comparable accounts of the financial institution; and
- (c) ensure that any charges against the trust account are not paid or reimbursed out of the trust account.

**11.4 Exemption**

- (1) Sections 11.1 and 11.2 do not apply to members of the Investment Dealers Association of Canada.
- (2) A participating dealer that is a member of an SRO referred to in subsection (1) shall permit the mutual fund and the principal distributor, through their respective auditors or other designated representatives, to examine the books and records of the participating dealer to verify the participating dealer’s compliance with the requirements of its association or exchange that relate to the commingling of cash.

**11.5 Right of Inspection** - The mutual fund, its trustee, manager and principal distributor shall ensure that all contractual arrangements made between any of them and any person or company providing services to the mutual fund permit the representatives of the mutual fund, its manager and trustee to examine the books and records of those persons or companies in order to monitor

compliance with this Instrument.

## **PART 12 COMPLIANCE REPORTS**

### **12.1 Compliance Reports**

- (1) A mutual fund that does not have a principal distributor shall complete and file, within 140 days after the financial year end of the mutual fund
  - (a) a report in the form contained in Appendix B-1 describing compliance by the mutual fund during that financial year with the applicable requirements of Parts 9, 10 and 11; and
  - (b) a report by the auditor of the mutual fund, in the form contained in Appendix B-1, concerning the report referred to in paragraph (a).
- (2) The principal distributor of a mutual fund shall complete and file, within 90 days after the financial year end of the principal distributor
  - (a) a report in the form contained in Appendix B-2 describing compliance by the principal distributor during that financial year with the applicable requirements of Parts 9, 10 and 11; and
  - (b) a report by the auditor of the principal distributor or by the auditor of the mutual fund, in the form contained in Appendix B-2, concerning the report referred to in paragraph (a).
- (3) Each participating dealer that distributes securities of a mutual fund in a financial year of the participating dealer shall complete and file, within 90 days after the end of that financial year
  - (a) a report in the form contained in Appendix B-3 describing compliance by the participating dealer during that financial year with the applicable requirements of Parts 9, 10 and 11 in connection with its distribution of securities of all mutual funds in that financial year; and
  - (b) a report by the auditor of the participating dealer, in the form contained in Appendix B-3, concerning the report referred to in paragraph (a).
- (4) Subsection (3) does not apply to members of the Investment Dealers Association of Canada.

## **PART 13 [Repealed]**

## **PART 14 RECORD DATE**

**14.1 Record Date** - The record date for determining the right of securityholders of a mutual fund to receive a dividend or distribution by the mutual fund shall be one of

- (a) the day on which the net asset value per security is determined for the purpose of

- calculating the amount of the payment of the dividend or distribution;
- (b) the last day on which the net asset value per security of the mutual fund was calculated before the day referred to in paragraph (a); or
- (c) if the day referred to in paragraph (b) is not a business day, the last day on which the net asset value per security of the mutual fund was calculated before the day referred to in paragraph (b).

## **PART 15 SALES COMMUNICATIONS AND PROHIBITED REPRESENTATIONS**

**15.1 Ability to Make Sales Communications** - Sales communications pertaining to a mutual fund may be made by a person or company only in accordance with this Part.

### **15.2 Sales Communications - General Requirements**

- (1) Despite any other provision of this Part, no sales communication shall
  - (a) be untrue or misleading; or
  - (b) include a statement that conflicts with information that is contained in the preliminary simplified prospectus, the preliminary annual information form, the simplified prospectus or annual information form
    - (i) of a mutual fund, or
    - (ii) in which an asset allocation service is described.
- (2) All performance data or disclosure specifically required by this Instrument and contained in a written sales communication shall be at least as large as 10-point type.

### **15.3 Prohibited Disclosure in Sales Communications**

- (1) A sales communication shall not compare the performance of a mutual fund or asset allocation service with the performance or change of any benchmark or investment unless
  - (a) it includes all facts that, if disclosed, would be likely to alter materially the conclusions reasonably drawn or implied by the comparison;
  - (b) it presents data for each subject of the comparison for the same period or periods;
  - (c) it explains clearly any factors necessary to make the comparison fair and not misleading; and
  - (d) in the case of a comparison with a benchmark
    - (i) the benchmark existed and was widely recognized and available during the period for which the comparison is made, or

- (ii) the benchmark did not exist for all or part of the period, but a reconstruction or calculation of what the benchmark would have been during that period, calculated on a basis consistent with its current basis of calculation, is widely recognized and available.
- (2) A sales communication for a mutual fund or asset allocation service that is prohibited by paragraph 15.6(a) from disclosing performance data shall not provide performance data for any benchmark or investment other than a mutual fund or asset allocation service under common management with the mutual fund or asset allocation service to which the sales communication pertains.
- (3) Despite subsection (2), a sales communication for an index mutual fund may provide performance data for the index on which the investments of the mutual fund are based if the index complies with the requirements for benchmarks contained in paragraph (1)(d).
- (4) A sales communication shall not refer to a performance rating or ranking of a mutual fund or asset allocation service unless
  - (a) the rating or ranking is prepared by an organization that is not a member of the organization of the mutual fund;
  - (b) standard performance data is provided for any mutual fund or asset allocation service for which a performance rating or ranking is given; and
  - (c) the rating or ranking is provided for each period for which standard performance data is required to be given.
- (5) A sales communication shall not refer to a credit rating of securities of a mutual fund unless
  - (a) the rating is current and was prepared by an approved credit rating organization;
  - (b) there has been no announcement by the approved credit rating organization of which the mutual fund or its manager is or ought to be aware that the credit rating of the securities may be down-graded; and
  - (c) no approved credit rating organization is currently rating the securities at a lower level.
- (6) A sales communication shall not refer to a mutual fund as, or imply that it is, a money fund, cash fund or money market fund unless, at the time the sales communication is used and for each period for which money market fund standard performance data is provided, the mutual fund is and was a money market fund, either under National Policy Statement No. 39 or under this Instrument.
- (7) A sales communication shall not state or imply that a registered retirement savings plan, registered retirement income fund or registered education savings plan in itself, rather than the mutual fund to which the sales communication relates, is an investment.

## 15.4 Required Disclosure and Warnings in Sales Communications

- (1) A written sales communication shall
  - (a) bear the name of the principal distributor or participating dealer that distributed the sales communication; and
  - (b) if the sales communication is not an advertisement, contain the date of first publication of the sales communication.
- (2) A sales communication that includes a rate of return or a mathematical table illustrating the potential effect of a compound rate of return shall contain a statement in substantially the following words:

“[The rate of return or mathematical table shown] is used only to illustrate the effects of the compound growth rate and is not intended to reflect future values of [the mutual fund or asset allocation service] or returns on investment [in the mutual fund or from the use of the asset allocation service].”.
- (3) A sales communication, other than a report to securityholders, of a mutual fund that is not a money market fund and that does not contain performance data shall contain a warning in substantially the following words:

“Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments. Please read the prospectus before investing. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated.”.
- (4) A sales communication, other than a report to securityholders, of a money market fund that does not contain performance data shall contain a warning in substantially the following words:

“Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments. Please read the prospectus before investing. Mutual fund securities are not covered by the Canada Deposit Insurance Corporation or by any other government deposit insurer. There can be no assurances that the fund will be able to maintain its net asset value per security at a constant amount or that the full amount of your investment in the fund will be returned to you. Past performance may not be repeated.”.
- (5) A sales communication for an asset allocation service that does not contain performance data shall contain a warning in substantially the following words:

“Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments and the use of an asset allocation service. Please read the prospectus of the mutual funds in which investment may be made under the asset allocation service before investing. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated.”.

- (6) A sales communication, other than a report to securityholders, of a mutual fund that is not a money market fund and that contains performance data shall contain a warning in substantially the following words:
- “Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments. Please read the prospectus before investing. The indicated rate[s] of return is [are] the historical annual compounded total return[s] including changes in [share or unit] value and reinvestment of all [dividends or distributions] and does [do] not take into account sales, redemption, distribution or optional charges or income taxes payable by any securityholder that would have reduced returns. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated.”.
- (7) A sales communication, other than a report to securityholders, of a money market fund that contains performance data shall contain
- (a) a warning in substantially the following words:
- “Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments. Please read the prospectus before investing. The performance data provided assumes reinvestment of distributions only and does not take into account sales, redemption, distribution or optional charges or income taxes payable by any securityholder that would have reduced returns. Mutual fund securities are not covered by the Canada Deposit Insurance Corporation or by any other government deposit insurer. There can be no assurances that the fund will be able to maintain its net asset value per security at a constant amount or that the full amount of your investment in the fund will be returned to you. Past performance may not be repeated.”; and
- (b) a statement in substantially the following words, immediately following the performance data:
- “This is an annualized historical yield based on the seven day period ended on [date] [annualized in the case of effective yield by compounding the seven day return] and does not represent an actual one year return.”.
- (8) A sales communication for an asset allocation service that contains performance data shall contain a warning in substantially the following words:
- “Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments and the use of an asset allocation service. Please read the prospectus of the mutual funds in which investment may be made under the asset allocation service before investing. The indicated rate[s] of return is [are] the historical annual compounded total return[s] assuming the investment strategy recommended by the asset allocation service is used and after deduction of the fees and charges in respect of the service. The return[s] is [are] based on the historical annual compounded total returns of the participating funds including changes in [share] [unit] value and reinvestment of all [dividends or distributions] and does [do] not take into account sales, redemption,

distribution or optional charges or income taxes payable by any securityholder in respect of a participating fund that would have reduced returns. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated.”.

- (9) A sales communication distributed after the issue of a receipt for a preliminary simplified prospectus of the mutual fund described in the sales communication but before the issue of a receipt for its simplified prospectus shall contain a warning in substantially the following words:

“A preliminary simplified prospectus relating to the fund has been filed with certain Canadian securities commissions or similar authorities. You cannot buy [units] [shares] of the fund until the relevant securities commissions or similar authorities issue receipts for the simplified prospectus of the fund.”.

- (10) A sales communication for a mutual fund or asset allocation service that purports to arrange a guarantee or insurance in order to protect all or some of the principal amount of an investment in the mutual fund or asset allocation service shall
- (a) identify the person or company providing the guarantee or insurance;
  - (b) provide the material terms of the guarantee or insurance, including the maturity date of the guarantee or insurance;
  - (c) if applicable, state that the guarantee or insurance does not apply to the amount of any redemptions before the maturity date of the guarantee or before the death of the securityholder and that redemptions before that date would be based on the net asset value per security of the mutual fund at the time; and
  - (d) modify any other disclosure required by this section appropriately.
- (11) The warnings referred to in this section shall be communicated in a manner that a reasonable person would consider clear and easily understood at the same time as, and through the medium by which, the related sales communication is communicated.

## **15.5 Disclosure Regarding Distribution Fees**

- (1) No person or company shall describe a mutual fund in a sales communication as a “no-load fund” or use words of like effect if on a purchase or redemption of securities of the mutual fund investor fees are payable by an investor or if any fees, charges or expenses are payable by an investor to a participating dealer of the mutual fund named in the sales communication, other than
- (a) fees and charges related to specific optional services;
  - (b) for a mutual fund that is not a money market fund, redemption fees on the redemption of securities of the mutual fund that are redeemed within 90 days after the purchase of the securities, if the existence of the fees is disclosed in the sales communication, or in the simplified prospectus of the mutual fund; or
  - (c) costs that are payable only on the set-up or closing of a securityholder’s account and that

reflect the administrative costs of establishing or closing the account, if the existence of the costs is disclosed in the sales communication, or in the simplified prospectus of the mutual fund.

- (2) If a sales communication describes a mutual fund as “no-load” or uses words to like effect, the sales communication shall
  - (a) indicate the principal distributor or a participating dealer through which an investor may purchase the mutual fund on a no-load basis;
  - (b) disclose that management fees and operating expenses are paid by the mutual fund; and
  - (c) disclose the existence of any trailing commissions paid by a member of the organization of the mutual fund.
- (3) A sales communication containing a reference to the existence or absence of fees or charges, other than the disclosure required by section 15.4 or a reference to the term “no-load”, shall disclose the types of fees and charges that exist.
- (4) The rate of sales charges or commissions for the sale of securities of a mutual fund or the use of an asset allocation service shall be expressed in a sales communication as a percentage of the amount paid by the purchaser and as a percentage of the net amount invested if a reference is made to sales charges or commissions.

**15.6 Performance Data - General Requirements** - No sales communication pertaining to a mutual fund or asset allocation service shall contain performance data of the mutual fund or asset allocation service unless

- (a) either
  - (i) the mutual fund has distributed securities under a simplified prospectus in a jurisdiction for 12 consecutive months, or the asset allocation service has been operated for at least 12 consecutive months and has invested only in participating funds each of which has distributed securities under a simplified prospectus in a jurisdiction for at least 12 consecutive months, or
  - (ii) if the sales communication pertains to a mutual fund or asset allocation service that does not satisfy the requirements of subparagraph (i), the sales communication is sent only to
    - (A) securityholders of the mutual fund or participants in the asset allocation service, or
    - (B) securityholders of a mutual fund or participants in an asset allocation service under common management with the mutual fund or asset allocation service;
- (b) the sales communication also contains standard performance data of the mutual fund or

asset allocation service and, in the case of a written sales communication, the standard performance data is presented in type size that is equal to or larger than that used to present the other performance data;

- (c) the performance data reflects or includes references to all elements of return; and
- (d) except as permitted by subsection 15.3(3), the sales communication does not contain performance data for a period that is before the time when the mutual fund offered its securities under a simplified prospectus or before the asset allocation service commenced operation.

**15.7 Advertisements** - An advertisement for a mutual fund or asset allocation service shall not compare the performance of the mutual fund or asset allocation service with any benchmark or investment other than

- (a) one or more mutual funds or asset allocation services that are under common management or administration with the mutual fund or asset allocation service to which the advertisement pertains;
- (b) one or more mutual funds or asset allocation services that have fundamental investment objectives that a reasonable person would consider similar to the mutual fund or asset allocation service to which the advertisement pertains; or
- (c) an index.

**15.8 Performance Measurement Periods Covered by Performance Data**

- (1) A sales communication, other than a report to securityholders, that relates to a money market fund may provide standard performance data only if
  - (a) the standard performance data has been calculated for the most recent seven day period for which it is practicable to calculate, taking into account publication deadlines; and
  - (b) the seven day period does not start more than 45 days before the date of the appearance, use or publication of the sales communication.
- (2) A sales communication, other than a report to securityholders, that relates to an asset allocation service or to a mutual fund other than a money market fund may provide standard performance data only if
  - (a) the standard performance data has been calculated for the 10, five, three and one year periods and the period since the inception of the mutual fund if the mutual fund has been offering securities by way of simplified prospectus for more than one and less than 10 years; and
  - (b) the periods referred to in paragraph (a) end on the same calendar month end that is
    - (i) not more than 45 days before the date of the appearance or use of the

advertisement in which it is included, and

- (ii) not more than three months before the date of first publication of any other sales communication in which it is included.
- (3) A report to securityholders may contain standard performance data only if
- (a) the standard performance data has been calculated for the 10, five, three and one year periods and the period since the inception of the mutual fund if the mutual fund has been offering securities by way of simplified prospectus for more than one and less than 10 years; and
  - (b) the periods referred to in paragraph (a) end on the day as of which the balance sheet of the financial statements contained in the report to securityholders was prepared.
- (4) A sales communication shall clearly identify the periods for which performance data is calculated.

#### **15.9 Changes affecting Performance Data**

- (1) If, during or after a performance measurement period of performance data contained in a sales communication, there have been changes in the business, operations or affairs of the mutual fund or asset allocation service to which the sales communication pertains that could have materially affected the performance of the mutual fund or asset allocation service, the sales communication shall contain
- (a) summary disclosure of the changes, and of how those changes could have affected the performance had those changes been in effect throughout the performance measurement period; and
  - (b) for a money market fund that during the performance measurement period did not pay or accrue the full amount of any fees and charges of the type described under paragraph 15.11(1)1, disclosure of the difference between the full amounts and the amounts actually charged, expressed as an annualized percentage on a basis comparable to current yield.
- (2) If a mutual fund has, in the last 10 years, undertaken a reorganization with, or acquired assets from, another mutual fund in a transaction that was a material change for the mutual fund or would have been a material change for the mutual fund had this Instrument been in force at the time of the transaction, then, in any sales communication of the mutual fund,
- (a) the mutual fund shall provide summary disclosure of the transaction;
  - (b) the mutual fund may include its performance data covering any part of a period before the transaction only if it also includes the performance data for the other fund for the same periods;
  - (c) the mutual fund shall not include its performance data for any part of a period after the transaction unless

- (i) 12 months have passed since the transaction, or
- (ii) the mutual fund includes in the sales communication the performance data for itself and the other mutual fund referred to in paragraph (b); and
- (d) the mutual fund shall not include any performance data for any period that is composed of both time before and after the transaction.

#### **15.10 Formula for Calculating Standard Performance Data**

- (1) The standard performance data of a mutual fund shall be calculated in accordance with this section.
- (2) In this Part

“current yield” means the yield of a money market fund expressed as a percentage and determined by applying the following formula:

$$\text{current yield} = [\text{seven day return} \times 365/7] \times 100;$$

“effective yield” means the yield of a money market fund expressed as a percentage and determined by applying the following formula:

$$\text{effective yield} = [(\text{seven day return} + 1)^{365/7} - 1] \times 100;$$

“seven day return” means the income yield of an account of a securityholder in a money market fund that is calculated by

- (a) determining the net change, exclusive of new subscriptions other than from the reinvestment of distributions or proceeds of redemption of securities of the money market fund, in the value of the account,
- (b) subtracting all fees and charges of the type referred to in paragraph 15.11(1)3 for the seven day period, and
- (c) dividing the result by the value of the account at the beginning of the seven day period;

“standard performance data” means

- (a) for a money market fund
  - (i) the current yield, or
  - (ii) the current yield and effective yield, if the effective yield is reported in a type size that is at least equal to that of the current yield, and

- (b) for any mutual fund other than a money market fund, the total return calculated in each case in accordance with this section; and

“total return” means the annual compounded rate of return for a mutual fund for a period that would equate the initial value to the redeemable value at the end of the period, expressed as a percentage, and determined by applying the following formula:

$$\text{total return} = [(\text{redeemable value}/\text{initial value})^{(1/N)} - 1] \times 100$$

where N = the length of the performance measurement period in years, with a minimum value of 1.

- (3) If there are fees and charges of the type described in paragraph 15.11(1)1 relevant to the calculation of redeemable value and initial value of the securities of a mutual fund, the redeemable value and initial value of securities of a mutual fund shall be the net asset value of one unit or share of the mutual fund at the beginning or at the end of the performance measurement period, minus the amount of those fees and charges calculated by applying the assumptions referred to in that paragraph to a hypothetical securityholder account.
- (4) If there are no fees and charges of the type described in paragraph 15.11(1)1 relevant to a calculation of total return, the calculation of total return for a mutual fund may assume a hypothetical investment of one security of the mutual fund and be calculated as follows:

- (a) “initial value” means the net asset value of one unit or share of a mutual fund at the beginning of the performance measurement period; and
- (b) “redeemable value” =

$$R \times (1 + D_1/P_1) \times (1 + D_2/P_2) \times (1 + D_3/P_3) \dots \times (1 + D_n/P_n)$$

where R = the net asset value of one unit or security of the mutual fund at the end of the performance measurement period,

D = the dividend or distribution amount per security of the mutual fund at the time of each distribution,

P = the dividend or distribution reinvestment price per security of the mutual fund at the time of each distribution, and

n = the number of dividends or distributions during the performance measurement period.

- (5) Standard performance data of an asset allocation service shall be based upon the standard performance data of its participating funds.
- (6) Performance data

- (a) for a mutual fund other than a money market fund shall be calculated to the nearest one-tenth of one percent; and
- (b) for a money market fund shall be calculated to the nearest one-hundredth of one percent.

### **15.11 Assumptions for Calculating Standard Performance Data**

- (1) The following assumptions shall be made in the calculation of standard performance data of a mutual fund:
  - 1. Recurring fees and charges that are payable by all securityholders
    - (a) are accrued or paid in proportion to the length of the performance measurement period;
    - (b) if structured in a manner that would result in the performance information being dependent on the size of an investment, are calculated on the basis of an investment equal to the greater of \$10,000 or the minimum amount that may be invested; and
    - (c) if fully negotiable, are calculated on the basis of the average fees paid by accounts of the size referred to in paragraph (b).
  - 2. There are no fees and charges related to specific optional services.
  - 3. All fees and charges payable by the mutual fund are accrued or paid.
  - 4. Dividends or distributions by the mutual fund are reinvested in the mutual fund at the net asset value per security of the mutual fund on the reinvestment dates during the performance measurement period.
  - 5. There are no non-recurring fees and charges that are payable by some or all securityholders and no recurring fees and charges that are payable by some but not all securityholders.
  - 6. A complete redemption occurs at the end of the performance measurement period so that the ending redeemable value includes elements of return that have been accrued but not yet paid to securityholders.
- (2) The following assumptions shall be made in the calculation of standard performance data of an asset allocation service:
  - 1. Fees and charges that are payable by participants in the asset allocation service
    - (a) are accrued or paid in proportion to the length of the performance measurement period;
    - (b) if structured in a manner that would result in the performance information being

dependent on the size of an investment, are calculated on the basis of an investment equal to the greater of \$10,000 or the minimum amount that may be invested; and

- (c) if fully negotiable, are calculated on the basis of the average fees paid by accounts of the size referred to in paragraph (b).
2. There are no fees and charges related to specific optional services.
  3. The investment strategy recommended by the asset allocation service is utilized for the performance measurement period.
  4. Transfer fees are
    - (a) accrued or paid;
    - (b) if structured in a manner that would result in the performance information being dependent on the size of an investment, calculated on the basis of an account equal to the greater of \$10,000 or the minimum amount that may be invested; and
    - (c) if the fees and charges are fully negotiable, calculated on the basis of the average fees paid by an account of the size referred to in paragraph (b).
  5. A complete redemption occurs at the end of the performance measurement period so that the ending redeemable value includes elements of return that have been accrued but not yet paid to securityholders.
- (3) The calculation of standard performance data shall be based on actual historical performance and the fees and charges payable by the mutual fund and securityholders, or the asset allocation service and participants, in effect during the performance measurement period.

**15.12 Sales Communications During the Waiting Period** - If a sales communication is used after the issue of a receipt for a preliminary simplified prospectus of the mutual fund described in the sales communication but before the issue of a receipt for its simplified prospectus, the sales communication shall state only

- (a) whether the security represents a share in a corporation or an interest in a non-corporate entity;
- (b) the name of the mutual fund and its manager;
- (c) the fundamental investment objectives of the mutual fund;
- (d) without giving details, whether the security is or will be a qualified investment for a registered retirement savings plan, registered retirement income fund or registered education savings plan or qualifies or will qualify the holder for special tax treatment; and

- (e) any additional information permitted by securities legislation.

### **15.13 Prohibited Representations**

- (1) Securities issued by an unincorporated mutual fund shall be described by a term that is not and does not include the word “shares”.
- (2) No communication by a mutual fund or asset allocation service, its promoter, manager, portfolio adviser, principal distributor, participating dealer or a person providing services to the mutual fund or asset allocation service shall describe a mutual fund as a commodity pool or as a vehicle for investors to participate in the speculative trading of, or leveraged investment in, derivatives, unless the mutual fund is a commodity pool as defined in National Instrument 81-101 Mutual Fund Prospectus Disclosure.

### **15.14 Sales Communication - Multi-Class Mutual Funds** - A sales communication for a mutual fund that distributes different classes or series of securities that are referable to the same portfolio shall not contain performance data unless the sales communication complies with the following requirements:

- 1. The sales communication clearly specifies the class or series of security to which any performance data contained in the sales communication relates.
- 2. If the sales communication refers to more than one class or series of security and provides performance data for any one class or series, the sales communication shall provide performance data for each class or series of security referred to in the sales communication and shall clearly explain the reasons for different performance data among the classes or series.
- 3. A sales communication for a new class or series of security and an existing class or series of security shall not contain performance data for the existing class or series unless the sales communication clearly explains any differences between the new class or series and the existing class or series that could affect performance.

### **PART 16 [Repealed]**

### **PART 17 [Repealed]**

### **PART 18 SECURITYHOLDER RECORDS**

#### **18.1 Maintenance of Records** - A mutual fund that is not a corporation shall maintain, or cause to be maintained, up to date records of

- (a) the names and latest known addresses of each securityholder of the mutual fund;
- (b) the number and class or series of a class of securities held by each securityholder of the mutual fund; and
- (c) the date and details of each issue and redemption of securities, and each distribution, of

the mutual fund.

## **18.2 Availability of Records**

- (1) A mutual fund that is not a corporation shall make, or cause to be made, the records referred to in section 18.1 available for inspection, free of charge, during normal business hours at its principal or head office by a securityholder or a representative of a securityholder, if the securityholder has agreed in writing that the information contained in the register will not be used by the securityholder for any purpose other than attempting to influence the voting of securityholders of the mutual fund or a matter relating to the relationships among the mutual fund, the members of the organization of the mutual fund, and the securityholders, partners, directors and officers of those entities.
- (2) A mutual fund shall, upon written request by a securityholder of the mutual fund, provide, or cause to be provided, to the securityholder a copy of the records referred to in paragraphs 18.1(a) and (b) if the securityholder
  - (a) has agreed in writing that the information contained in the register will not be used by the securityholder for any purpose other than attempting to influence the voting of securityholders of the mutual fund or a matter relating to the administration of the mutual fund; and
  - (b) has paid a reasonable fee to the mutual fund that does not exceed the reasonable costs to the mutual fund of providing the copy of the register.

## **PART 19 EXEMPTIONS AND APPROVALS**

### **19.1 Exemption**

- (1) The regulator or securities regulatory authority may grant an exemption from this Instrument, in whole or in part, subject to such conditions or restrictions as may be imposed in the exemption.
- (2) Despite subsection (1), in Ontario only the regulator may grant such an exemption.

### **19.2 Exemption or Approval under Prior Policy**

- (1) A mutual fund that has obtained, from the regulator or securities regulatory authority, an exemption or waiver from, or approval under, a provision of National Policy Statement No. 39 before this Instrument came into force is exempt from any substantially similar provision of this Instrument, if any, on the same conditions, if any, as are contained in the earlier exemption or approval, unless the regulator or securities regulatory authority has revoked that exemption or waiver under authority provided to it in securities legislation.
- (2) Despite Part 7, a mutual fund that has obtained, from the regulator or securities regulatory authority, approval under National Policy Statement No. 39 to pay incentive fees may continue to pay incentive fees on the terms of that approval if disclosure of the method of calculation of the fees and details of the composition of the benchmark or index used in calculating the fees are described in the simplified prospectus of the mutual fund.

- (3) A mutual fund that intends to rely upon subsection (1) shall, at the time of the first filing of its *pro forma* simplified prospectus after this Instrument comes into force, send to the regulator a letter or memorandum containing
  - (a) a brief description of the nature of the exemption from, or approval under, National Policy Statement No. 39 previously obtained; and
  - (b) the provision in the Instrument that is substantially similar to the provision in National Policy Statement No. 39 from or under which the exemption or approval was previously obtained.

### **19.3 Revocation of Exemptions**

- (1) A mutual fund that has obtained an exemption or waiver from, or approval under, National Policy Statement No. 39 or this Instrument before December 31, 2003, that relates to a mutual fund investing in other mutual funds, may no longer rely on the exemption, waiver or approval as of December 31, 2004;
- (2) In British Columbia, subsection (1) does not apply.

### **PART 20 TRANSITIONAL**

[Note: This unofficial consolidation does not include PART 20, which contains the original historical coming-into-force provision for this Instrument.]

**National Instrument 81-102**

**Appendix A**

**Futures Exchanges for the Purpose of  
Subsection 2.7(4) - Derivative Counterparty Exposure Limits**

**Futures Exchanges**

**Australia**

Sydney Futures Exchange  
Australian Financial Futures Market

**Austria**

Osterreichische Termin-und Option Borse (OTOB - The Austrian Options and Futures Exchange)

**Belgium**

Belfox CV (Belgium Futures and Options Exchange)

**Brazil**

Bolsa Brasileira de Futuros  
Bolsa de Mercadorias & Futuros  
Bolsa de Valores de Rio de Janeiro

**Canada**

The Winnipeg Commodity Exchange  
The Toronto Futures Exchange  
The Montreal Exchange

**Denmark**

Kobenhavus Fondsbors (Copenhagen Stock Exchange)  
Garenti fonden for Dankse Optioner og Futures (Guarantee Fund for Danish Options and Futures)  
Futop (Copenhagen Stock Exchange)

**Finland**

Helsinki Stock Exchange  
Oy Suomen Optiopörssi (Finnish Options Exchange)  
Suomen Optionmeklarit Oy (Finnish Options Market)

**France**

Unofficial Consolidation – September 28, 2009

Marché à terme international de France S.A. (MATIF S.A.)

Marché des option négociables à Paris (MUNCP)

**Germany**

DTB Deutsche Terminbörse GmbH  
EUREX

**Hong Kong**

Hong Kong Futures Exchange Limited

**Ireland**

Irish Futures and Options Exchange

**Italy**

Milan Italiano Futures Exchange

**Japan**

Osaka Shoken Torihikisho (Osaka Securities Exchange)  
The Tokyo Commodity Exchange for Industry  
The Tokyo International Financial Futures Exchange  
Tokyo Grain Exchange  
Tokyo Stock Exchange

**Netherlands**

AEX Options & Futures Exchange  
EOE-Optiebeurs (European Options Exchange)  
Financiele Termijnmarkt Amsterdam N.V.

**New Zealand**

New Zealand Futures and Options Exchange

**Norway**

Oslo Stock Exchange

**Philippines**

Manila International Futures Exchange

**Portugal**

Bosa de Derivatives de Porto

**Singapore**

Singapore Commodity Exchange (SICOM)  
Singapore International Monetary Exchange Limited (SIMEX)

**Spain**

Meff Renta Fija  
Meff Renta Variable

**Sweden**

OM Stockholm Fondkommission AB

**Switzerland**

EUREX

**United Kingdom**

International Petroleum Exchange (IPE)  
London International Financial Futures and Options Exchange (LIFFE)  
London Metal Exchange (LME)  
OM London

**United States**

Chicago Board of Options Exchange (CBOE)  
Chicago Board of Trade (CBOT)  
Chicago Mercantile Exchange (CME)  
Commodity Exchange, Inc. (COMEX)  
Financial Instrument Exchange (Finex) a division of the New York Cotton Exchange  
Board of Trade of Kansas City, Missouri, Inc.  
Mid-America Commodity Exchange  
Minneapolis Grain Exchange (MGE)  
New York Futures Exchange, Inc. (NYFE)  
New York Mercantile Exchange (NYMEX)  
New York Board of Trade (NYBOT)  
Pacific Stock Exchange  
Philadelphia Board of Trade (PBOT)  
Twin Cities Board of Trade

**National Instrument 81-102**

**Appendix B-1**

**Compliance Report**

TO: [The appropriate securities regulatory authorities]

FROM: [Name of mutual fund]

RE: Compliance Report on National Instrument 81-102  
For the year ended [insert date]

We hereby confirm that we have complied with the applicable requirements of Parts 9, 10 and 11 of National Instrument 81-102 for the year ended [insert date] [except as follows:] [list exceptions, if any].

[NAME of mutual fund]

Signature

Name and office of the person  
executing this report

Date

**National Instrument 81-102**

**Appendix B-1**

**Audit Report**

TO: [The appropriate securities regulatory authorities]

RE: Compliance Report on National Instrument 81-102  
For the year ended [insert date]

We have audited [name of mutual fund]'s report made under section 12.1 of National Instrument 81-102 regarding its compliance for the year ended [insert date] with the applicable requirements of Parts 9, 10 and 11 of that National Instrument. Compliance with these requirements is the responsibility of the management of [name of mutual fund] (the "Fund"). Our responsibility is to express an opinion on management's compliance report based on our audit.

We conducted our audit in accordance with the standards for assurance engagements established by The Canadian Institute of Chartered Accountants. Those standards require that we plan and perform an audit to obtain reasonable assurance as a basis for our opinion. Such an audit includes examining, on a test basis, evidence supporting the assertions in management's compliance report.

In our opinion, the Fund's report presents fairly, in all material respects, the Fund's compliance for the year ended [insert date] with the applicable requirements of Parts 9, 10 and 11 of National Instrument 81-102.

This report is provided solely for the purpose of assisting the securities regulatory authority [ies] to which it is addressed in discharging its [their] responsibilities and should not be used for any other purpose.

City  
Date  
76

Chartered Accountants

**National Instrument 81-102**

**Appendix B-2**

**Compliance Report**

TO: [The appropriate securities regulatory authorities]

FROM: [Name of principal distributor] (the “Distributor”)

RE: Compliance Report on National Instrument 81-102  
For the year ended [insert date]

FOR: [Name(s) of the mutual fund (the “Fund[s]”)]

We hereby confirm that we have complied with the applicable requirements of Parts 9, 10 and 11 of National Instrument 81-102 in respect of the Fund[s] for the year ended [insert date] [except as follows:] [list exceptions, if any].

[NAME of the Distributor]

Signature

Name and office of the person  
executing this report

Date

**National Instrument 81-102**

**Appendix B-2**

**Audit Report**

TO: [The appropriate securities regulatory authorities]

RE: Compliance Report on National Instrument 81-102  
For the year ended [insert date]

We have audited [name of principal distributor]’s report made under section 12.1 of National Instrument 81-102 regarding its compliance for the year ended [insert date] with the applicable requirements of Parts 9, 10 and 11 of that National Instrument in respect of the [name of mutual funds] (the “Funds”). Compliance with these requirements is the responsibility of the management of [name of principal distributor] (the “Company”). Our responsibility is to express an opinion on management’s compliance report based on our audit.

We conducted our audit in accordance with the standards for assurance engagements established by The Canadian Institute of Chartered Accountants. Those standards require that we plan and perform an audit to obtain reasonable assurance as a basis for our opinion. Such an audit includes examining, on a test basis, evidence supporting the assertions in management’s compliance report.

In our opinion, the Company’s report presents fairly, in all material respects, the Company’s compliance for the year ended [insert date] with the applicable requirements of Parts 9, 10 and 11 of National Instrument 81-102 in respect of the Funds.

This report is provided solely for the purpose of assisting the securities regulatory authority [ies] to which it is addressed in discharging its [their] responsibilities and should not be used for any other purpose.

City  
Date

Chartered Accountants

**National Instrument 81-102**

**Appendix B-3**

**Compliance Report**

TO: [The appropriate securities regulatory authorities]

FROM: [Name of participating dealer] (the “Distributor”)

RE: Compliance Report on National Instrument 81-102  
For the year ended [insert date]

We hereby confirm that we have sold mutual fund securities to which National Instrument 81-102 is applicable. In connection with our activities in distributing these securities, we have complied with the applicable requirements of Parts 9, 10 and 11 of National Instrument 81-102 for the year ended [insert date] [except as follows:] [list exceptions, if any].

[NAME of the Distributor]

Signature

Name and office of the person  
executing this report

Date

**National Instrument 81-102**

**Appendix B-3**

**Audit Report**

TO: [The appropriate securities regulatory authorities]

RE: Compliance Report on National Instrument 81-102  
For the year ended [insert date]

We have audited [name of participating dealer]'s report made under section 12.1 of National Instrument 81-102 regarding its compliance for the year ended [insert date] with the applicable requirements of Parts 9, 10 and 11 of that National Instrument in respect of sales of mutual fund securities. Compliance with these requirements is the responsibility of the management of [name of participating dealer] (the "Company"). Our responsibility is to express an opinion on management's compliance report based on our audit.

We conducted our audit in accordance with the standards for assurance engagements established by The Canadian Institute of Chartered Accountants. Those standards require that we plan and perform an audit to obtain reasonable assurance as a basis for our opinion. Such an audit includes examining, on a test basis, evidence supporting the assertions in management's compliance report.

In our opinion, the Company's report presents fairly, in all material respects, the Company's compliance for the year ended [insert date] with the applicable requirements of Parts 9, 10 and 11 of National Instrument 81-102 in respect of sales of mutual fund securities.

This report is provided solely for the purpose of assisting the securities regulatory authority [ies] to which it is addressed in discharging its [their] responsibilities and should not be used for any other purpose.

City  
Date

Chartered Accountants

**National Instrument 81-102**

**Appendix C**

**Provisions Contained in Securities Legislation for the Purpose of Subsection 4.1(5) –  
Prohibited Investments**

<b>Jurisdiction</b>	<b>Securities Legislation Reference</b>
British Columbia	s. 81 of the <i>Securities Rules</i> (British Columbia)
Newfoundland and Labrador	s. 191 of Reg 805/96
New Brunswick	s13.2 of Local Rule 31-501 <i>Registration Requirements</i>
Nova Scotia	s. 67 of the General Securities Rules

**Companion Policy 81-102CP**  
**to**  
**National Instrument 81-102 *Mutual Funds***

**Table of Contents**

<b><u>PART</u></b>	<b><u>TITLE</u></b>
PART 1	PURPOSE
1.1	Purpose
PART 2	COMMENTS ON DEFINITIONS CONTAINED IN THE INSTRUMENT
2.1	“asset allocation service”
2.2	“cash equivalent”
2.3	“clearing corporation”
2.4	“debt-like security”
2.5	“fundamental investment objectives”
2.6	“guaranteed mortgage”
2.7	“hedging”
2.8	“illiquid asset”
2.9	“manager”
2.10	“option”
2.11	“performance data”
2.12	“public medium”
2.13	“purchase”
2.14	“restricted security”
2.15	“sales communication”
2.16	“specified derivative”
2.17	“standardized future”
2.18	“swap”
PART 3	INVESTMENTS
3.1	Evidences of Indebtedness of Foreign Governments and Supranational Agencies
3.2	Index Mutual Funds
3.3	Special Warrants
3.4	Investment in Other Mutual Funds
3.5	Instalments of Purchase Price
3.6	Purchase of Evidences of Indebtedness
3.7	Securities Lending, Repurchase and Reverse Repurchase Transactions
3.8	Prohibited Investments
PART 4	USE OF SPECIFIED DERIVATIVES
4.1	Exercising Options on Futures
4.2	Registration Matters
4.3	Leveraging
4.4	Cash Cover
PART 5	LIABILITY AND INDEMNIFICATION

**Unofficial Consolidation – September 28, 2009**

- 5.1 Liability and Indemnification
- 5.2 Securities Lending, Repurchase and Reverse Repurchase Transactions

**PART 6 SECURITYHOLDER MATTERS**

- 6.1 Meetings of Securityholders
- 6.2 Limited Liability
- 6.3 Calculation of Fees

**PART 7 CHANGES**

- 7.1 Integrity and Competence of Mutual Fund Management Groups
- 7.2 Mergers and Conversions of Mutual Funds
- 7.3 Regulatory Approval for Reorganizations
- 7.4 [Deleted]
- 7.5 Circumstances in Which Approval of Securityholders Not Required
- 7.6 Change of Auditor
- 7.7 Connection to NI 81-107

**PART 8 CUSTODIANSHIP OF PORTFOLIO ASSETS**

- 8.1 Standard of Care
- 8.2 Book-Based System
- 8.3 Compliance

**PART 9 CONTRACTUAL PLANS**

- 9.1 Contractual Plans

**PART 10 SALES AND REDEMPTIONS OF SECURITIES**

- 10.1 General
- 10.2 Interpretation
- 10.3 Receipt of Orders
- 10.4 Backward Pricing
- 10.5 Coverage of Losses

**PART 11 COMMINGLING OF CASH**

- 11.1 Commingling of Cash

**PART 12 [Deleted]**

**PART 13 PROHIBITED REPRESENTATIONS AND SALES COMMUNICATIONS**

- 13.1 Misleading Sales Communications
- 13.2 Other Provisions

**PART 14 [Deleted]**

**PART 15 SECURITYHOLDER RECORDS**

- 15.1 Securityholder Records

**PART 16 EXEMPTIONS AND APPROVALS**

- 16.1 Need for Multiple or Separate Applications

**Unofficial Consolidation – September 28, 2009**

- 16.2 Exemptions under Prior Policies
- 16.3 Waivers and Orders concerning “Fund of Funds”

**Companion Policy 81-102CP**  
**to**  
**National Instrument 81-102 *Mutual Funds***

**PART 1        PURPOSE**

- 1.1        Purpose** - The purpose of this Policy is to state the views of the Canadian securities regulatory authorities on various matters relating to National Instrument 81-102 *Mutual Funds* (the “Instrument”), including
- (a) the interpretation of various terms used in the Instrument;
  - (b) recommendations concerning the operating procedures that the Canadian securities regulatory authorities suggest that mutual funds, or persons performing services for mutual funds, adopt to ensure compliance with the Instrument;
  - (c) discussions of circumstances in which the Canadian securities regulatory authorities have granted relief from particular requirements of National Policy Statement No. 39 (“NP39”), the predecessor to the Instrument, and the conditions that those authorities imposed in granting that relief; and
  - (d) recommendations concerning applications for approvals required under, or relief from, provisions of the Instrument.

**PART 2        COMMENTS ON DEFINITIONS CONTAINED IN THE INSTRUMENT**

- 2.1        “asset allocation service”** - The definition of “asset allocation service” in the Instrument includes only specific administrative services in which an investment in mutual funds subject to the Instrument is an integral part. The Canadian securities regulatory authorities do not view this definition as including general investment services such as discretionary portfolio management that may, but are not required to, invest in mutual funds subject to this Instrument.
- 2.2        “cash equivalent”** - The definition of “cash equivalent” in the Instrument includes certain evidences of indebtedness of Canadian financial institutions. This includes banker’s acceptances.
- 2.3        “clearing corporation”** - The definition of “clearing corporation” in the Instrument includes both incorporated and unincorporated organizations, which may, but need not, be part of an options or futures exchange.
- 2.4        “debt-like security”** - Paragraph (b) of the definition of “debt-like security” in the Instrument provides that the value of the component of an instrument that is not linked to the underlying interest of the instrument must account for less than 80 percent of the aggregate value of the instrument in order that the instrument be considered a debt-like security. The Canadian securities regulatory authorities have structured this provision in this manner to emphasize what they consider the most appropriate manner to value these instruments. That is, one should first value the component of the instrument that is not linked to the underlying interest, as this is often much

easier to value than the component that is linked to the underlying interest. The Canadian securities regulatory authorities recognize the valuation difficulties that can arise if one attempts to value, by itself, the component of an instrument that is linked to the underlying interest.

## 2.5 “fundamental investment objectives”

- (1) The definition of “fundamental investment objectives” is relevant in connection with paragraph 5.1(c) of the Instrument, which requires that the approval of securityholders of a mutual fund be obtained before any change is made to the fundamental investment objectives of the mutual fund. The fundamental investment objectives of a mutual fund are required to be disclosed in a simplified prospectus under Part B of Form 81-101F1 *Contents of Simplified Prospectus*. The definition of “fundamental investment objectives” contained in the Instrument uses the language contained in the disclosure requirements of Part B of Form 81-101F1, and the definition should be read to include the matters that would have to be disclosed under the Item of Part B of the form concerning “Fundamental Investment Objectives”. Accordingly, any change to the mutual fund requiring a change to that disclosure would trigger the requirement for securityholder approval under paragraph 5.1(c) of the Instrument.
- (2) Part B of Form 81-101F1 sets out, among other things, the obligation that a mutual fund disclose in a simplified prospectus both its fundamental investment objectives and its investment strategies. The matters required to be disclosed under the Item of Part B of the form relating to “Investment Strategies” are not “fundamental investment objectives” under the Instrument.
- (3) Generally speaking, the “fundamental investment objectives” of a mutual fund are those attributes that define its fundamental nature. For example, mutual funds that are guaranteed or insured, or that pursue a highly specific investment approach such as index funds or derivative funds, may be defined by those attributes. Often the manner in which a mutual fund is marketed will provide evidence as to its fundamental nature; a mutual fund whose advertisements emphasize, for instance, that investments are guaranteed likely will have the existence of a guarantee as a “fundamental investment objective”.
- (4) The Canadian securities regulatory authorities are of the view that whether the securities of a mutual fund are foreign property under the ITA is linked to the mutual fund’s fundamental investment objectives. Therefore, a change in the method by which the mutual fund is managed that results in its securities going from being foreign property to being non-foreign property, or vice versa, would be likely due to a change in the mutual fund’s fundamental investment objectives.
- (5) One component of the definition of “fundamental investment objectives” is that those objectives distinguish a mutual fund from other mutual funds. This component does not imply that the fundamental investment objectives for each mutual fund must be unique. Two or more mutual funds can have identical fundamental investment objectives.

**2.6 “guaranteed mortgage”** - A mortgage insured under the *National Housing Act* (Canada) or similar provincial statutes is a “guaranteed mortgage” for the purposes of the Instrument.

**2.7 “hedging”**

- (1) One component of the definition of “hedging” is the requirement that hedging transactions result in a “high degree of negative correlation between changes in the value of the investment or position, or group of investments or positions, being hedged and changes in the value of the instrument or instruments with which the investment or position is hedged”. The Canadian securities regulatory authorities are of the view that there need not be complete congruence between the hedging instrument or instruments and the position or positions being hedged if it is reasonable to regard the one as a hedging instrument for the other, taking into account the closeness of the relationship between fluctuations in the price of the two and the availability and pricing of hedging instruments.
- (2) The definition of “hedging” includes a reference to the “maintaining” of the position resulting from a hedging transaction or series of hedging transactions. The inclusion of this component in the definition requires a mutual fund to ensure that a transaction continues to offset specific risks of the mutual fund in order that the transaction be considered a “hedging” transaction under the Instrument; if the “hedging” position ceases to provide an offset to an existing risk of a mutual fund, then that position is no longer a hedging position under the Instrument, and can be held by the mutual fund only in compliance with the specified derivatives rules of the Instrument that apply to non-hedging positions. The component of the definition that requires the “maintaining” of a hedge position does not mean that a mutual fund is locked into a specified derivatives position; it simply means that the specified derivatives position must continue to satisfy the definition of “hedging” in order to receive hedging treatment under the Instrument.
- (3) Paragraph (b) of the definition of “hedging” has been included to ensure that currency cross hedging continues to be permitted under the Instrument. Currency cross hedging is the substitution of currency risk associated with one currency for currency risk associated with another currency, if neither currency is a currency in which the mutual fund determines its net asset value per security and the aggregate amount of currency risk to which the mutual fund is exposed is not increased by the substitution. Currency cross hedging is to be distinguished from currency hedging, as that term is ordinarily used. Ordinary currency hedging, in the context of mutual funds, would involve replacing the mutual fund’s exposure to a “non-net asset value” currency with exposure to a currency in which the mutual fund calculates its net asset value per security. That type of currency hedging is subject to paragraph (a) of the definition of “hedging”.

**2.8** “**illiquid asset**” - A portfolio asset of a mutual fund that meets the definition of “illiquid asset” will be an illiquid asset even if a person or company, including the manager or the portfolio adviser of a mutual fund or a partner, director or officer of the manager or portfolio adviser of a mutual fund or any of their respective associates or affiliates, has agreed to purchase the asset from the mutual fund. That type of agreement does not affect the words of the definition, which defines “illiquid asset” in terms of whether that asset cannot be readily disposed of through market facilities on which public quotations in common use are widely available.

**2.9** “**manager**” - The definition of “manager” under the Instrument only applies to the person or company that actually directs the business of the mutual fund, and does not apply to others, such as trustees, that do not actually carry out this function. Also, a “manager” would not include a person or company whose duties are limited to acting as a service provider to the mutual fund, such as a portfolio adviser.

**2.10** “**option**” - The definition of “option” includes warrants, whether or not the warrants are listed on a stock exchange or quoted on an over-the-counter market.

**2.11 “performance data”** - The term “performance data” includes data on an aspect of the investment performance of a mutual fund, an asset allocation service, security, index or benchmark. This could include data concerning return, volatility or yield. The Canadian securities regulatory authorities note that the term “performance data” would not include a rating prepared by an independent organization reflecting the credit quality, rather than the performance, of, for instance, a mutual fund’s portfolio or the participating funds of an asset allocation service.

**2.12 “public medium”** - An “advertisement” is defined in the Instrument to mean a sales communication that is published or designed for use on or through a “public medium”. The Canadian securities regulatory authorities interpret the term “public medium” to include print, television, radio, tape recordings, video tapes, computer disks, the Internet, displays, signs, billboards, motion pictures and telephones.

**2.13 “purchase”**

(1) The definition of a “purchase”, in connection with the acquisition of a portfolio asset by a mutual fund, means an acquisition that is the result of a decision made and action taken by the mutual fund.

(2) The Canadian securities regulatory authorities consider that the following types of transactions would generally be purchases of a security by a mutual fund under the definition:

1. The mutual fund effects an ordinary purchase of the security, or, at its option, exercises, converts or exchanges a convertible security held by it.
2. The mutual fund receives the security as consideration for a security tendered by the mutual fund into a take-over bid.
3. The mutual fund receives the security as the result of a merger, amalgamation, plan of arrangement or other reorganization for which the mutual fund voted in favour.
4. The mutual fund receives the security as a result of the automatic exercise of an exchange or conversion right attached to another security held by the mutual fund in accordance with the terms of that other security or the exercise of that exchange or conversion right at the option of the mutual fund.
5. (a) The mutual fund has become legally entitled to dispose of the collateral held by it under a securities loan or repurchase agreement and to apply proceeds of realization to satisfy the obligations of the counterparty of the mutual fund under the transaction, and  
(b) sufficient time has passed after the event described in paragraph (a) to enable the mutual fund to sell the collateral in a manner that maintains an orderly market and that permits the preservation of the best value for the mutual fund.

(3) The Canadian securities regulatory authorities consider that the following types of transactions would generally not be purchases of a security by a mutual fund under the definition:

1. The mutual fund receives the security as a result of a compulsory acquisition by an issuer following completion of a successful take-over bid.
2. The mutual fund receives the security as a result of a merger, amalgamation, plan of arrangement or other reorganization that the mutual fund voted against.
3. The mutual fund receives the security as the result of the exercise of an exchange or conversion right attached to a security held by the mutual fund made at the discretion of the issuer of the security held by the mutual fund.
4. The mutual fund declines to tender into an issuer bid, even though its decision is likely to result in an increase in its percentage holdings of a security beyond what the mutual fund would be permitted under the Instrument to purchase.

**2.14 “restricted security”** - A special warrant is a form of restricted security and, accordingly, the provisions of the Instrument applying to restricted securities apply to special warrants.

**2.15 “sales communication”**

- (1) The term “sales communication” refers to a communication to a securityholder of a mutual fund and to a person or company that is not a securityholder if the purpose of the communication is to induce the purchase of securities of the mutual fund. A sales communication therefore does not include a communication solely between a mutual fund or its promoter, manager, principal distributor or portfolio adviser and a participating dealer, or between the principal distributor or a participating dealer and its registered salespersons, that is indicated to be internal or confidential and that is not designed to be passed on by any principal distributor, participating dealer or registered salesperson to any securityholder of, or potential investor in, the mutual fund. In the view of the Canadian securities regulatory authorities, if a communication of that type were so passed on by the principal distributor, participating dealer or registered salesperson, the communication would be a sales communication made by the party passing on the communication if the recipient of the communication were a securityholder of the mutual fund or if the intent of the principal distributor, participating dealer or registered salesperson in passing on the communication were to induce the purchase of securities of the mutual fund.
- (2) The term “sales communication” is defined in the Instrument such that the communication need not be in writing and includes any oral communication. The Canadian securities regulatory authorities are of the view that the requirements in the Instrument pertaining to sales communications would apply to statements made at an investor conference to securityholders or to others to induce the purchase of securities of the mutual fund.
- (3) The Canadian securities regulatory authorities are of the view that image advertisements that are intended to promote a corporate identity or the expertise of a mutual fund manager fall outside the definition of “sales communication”. However, an advertisement or other communication that refers to a specific mutual fund or funds or promotes any particular investment portfolio or strategy would be a sales communication and therefore be required to include warnings of the type now described in section 15.4 of the Instrument.

- (4) Paragraph (b) of the definition of a “sales communication” in the Instrument excludes sales communications contained in certain documents that the mutual fund is required to prepare, including audited or unaudited financial statements, statements of account and confirmations of trade. The Canadian securities regulatory authorities are of the view that if information is contained in these types of documents that is not required to be included by securities legislation, any such additional material is not excluded by paragraph (b) of the definition of sales communication and may, therefore, constitute a sales communication if the additional material otherwise falls within the definition of that term in the Instrument.

## **2.16 “specified derivative”**

- (1) The term “specified derivative” is defined to mean an instrument, agreement or security, the market price, value or payment obligations of which are derived from, referenced to or based on an underlying interest. Certain instruments, agreements or securities that would otherwise be specified derivatives within the meaning of the definition are then excluded from the definition for purposes of the Instrument.
- (2) Because of the broad ambit of the lead-in language to the definition, it is impossible to list every instrument, agreement or security that might be caught by that lead-in language but that is not considered to be a derivative in any normal commercial sense of that term. The Canadian securities regulatory authorities consider conventional floating rate debt instruments, securities of a mutual fund or commodity pool, non-redeemable securities of an investment fund, American depositary receipts and instalment receipts generally to be within this category, and generally will not treat those instruments as specified derivatives in administering the Instrument.
- (3) However, the Canadian securities regulatory authorities note that these general exclusions may not be applicable in cases in which a mutual fund invests in one of the vehicles described in subsection (2) with the result that the mutual fund obtains or increases exposure to a particular underlying interest in excess of the limit set out in section 2.1 of the Instrument. In such circumstances, the Canadian securities regulatory authorities are likely to consider that instrument a specified derivative under the Instrument.

**2.17 “standardized future”** - The definition of “standardized future” refers to an agreement traded on a futures exchange. This type of agreement is called a “futures contract” in the legislation of some jurisdictions, and an “exchange contract” in the legislation of some other jurisdictions (such as British Columbia and Alberta). The term “standardized future” is used in the Instrument to refer to these types of contracts, to avoid conflict with existing local definitions.

**2.18 “swap”** - The Canadian securities regulatory authorities are of the view that the definition of a swap in the Instrument would include conventional interest rate and currency swaps, as well as equity swaps.

## **PART 3 INVESTMENTS**

### **3.1 Evidences of Indebtedness of Foreign Governments and Supranational Agencies**

- (1) Section 2.1 of the Instrument prohibits mutual funds from purchasing a security of an issuer, other than a government security or a security issued by a clearing corporation if, immediately after the purchase, more than 10 percent of the net assets of the mutual fund, taken at market value at the time of the purchase, would be invested in securities of that issuer. The term “government security” is defined in the Instrument as an evidence of indebtedness that is issued, or fully and unconditionally guaranteed as to principal and interest, by any of the government of Canada, the government of a jurisdiction or the government of the United States of America.
- (2) Before the Instrument came into force, the Canadian securities regulatory authorities granted relief from the predecessor provision of NP39 to a number of international bond funds in order to permit those mutual funds to pursue their fundamental investment objectives with greater flexibility.
- (3) The Canadian securities regulatory authorities will continue to consider applications for relief from section 2.1 of the Instrument if the mutual fund making the application demonstrates that the relief will better enable the mutual fund to meet its fundamental investment objectives. This relief will ordinarily be restricted to international bond funds.
- (4) The relief from paragraph 2.04(1)(a) of NP39, which is replaced by section 2.1 of the Instrument, that has been provided to a mutual fund has generally been limited to the following circumstances:
  1. The mutual fund has been permitted to invest up to 20 percent of its net assets, taken at market value at the time of purchase, in evidences of indebtedness of any one issuer if those evidences of indebtedness are issued, or guaranteed fully as to principal and interest, by supranational agencies or governments other than the government of Canada, the government of a jurisdiction or the government of the United States of America and are rated “AA” by Standard & Poor’s, or have an equivalent rating by one or more other approved credit rating organizations.
  2. The mutual fund has been permitted to invest up to 35 percent of its net assets, taken at market value at the time of purchase, in evidences of indebtedness of any one issuer, if those securities are issued by issuers described in paragraph 1 and are rated “AAA” by Standard & Poor’s, or have an equivalent rating by one or more other approved credit rating organizations.
- (5) It is noted that the relief described in paragraphs 3.1(4)1 and 2 cannot be combined for one issuer.
- (6) Despite subsection (4), the relief from paragraph 2.04(1)(a) of NP39, which is replaced by section 2.1 of the Instrument, provided to a mutual fund whose securities are a registered investment under the ITA or whose securities are not, and are described in the current prospectus or simplified prospectus of the mutual fund as not being foreign property under the ITA has generally been restricted to allowing the mutual fund to invest no more than 20 percent of its net assets, taken at market value at the time of purchase, in securities issued by issuers described in subsection (4) if the securities of those issuers are foreign property under the ITA.
- (7) In addition to the limitation described in subsection (6), the relief from paragraph 2.04(1)(a) of NP39, which is replaced by section 2.1 of the Instrument, has generally been provided only if

- (a) the securities that may be purchased under the relief referred to in subsections (4) and (6) are traded on a mature and liquid market;
- (b) the acquisition of the evidences of indebtedness by the mutual fund is consistent with its fundamental investment objectives;
- (c) the prospectus or simplified prospectus of the mutual fund disclosed the additional risks associated with the concentration of the net assets of the mutual fund in securities of fewer issuers, such as the potential additional exposure to the risk of default of the issuer in which the fund has so invested and the risks, including foreign exchange risks, of investing in the country in which that issuer is located; and
- (d) the prospectus or simplified prospectus of the mutual fund gave details of the relief provided by the Canadian securities regulatory authorities, including the conditions imposed and the type of securities covered by the exemption.

### **3.2 Index Mutual Funds**

- (1) An "index mutual fund" is defined in section 1.1 of the Instrument as a mutual fund that has adopted fundamental investment objectives that require it to
  - (a) hold the securities that are included in a permitted index or permitted indices of the mutual fund in substantially the same proportion as those securities are reflected in that permitted index or permitted indices; or
  - (b) invest in a manner that causes the mutual fund to replicate the performance of that permitted index or those permitted indices.
- (2) This definition includes only mutual funds whose entire portfolio is invested in accordance with one or more permitted indices. The CSA recognizes that there may be mutual funds that invest part of their portfolio in accordance with a permitted index or indices, with a remaining part of the portfolio being actively managed. Those mutual funds cannot avail themselves of the relief provided by subsection 2.1(5) of the Instrument, which provides relief from the "10 percent rule" contained in subsection 2.1(1) of the Instrument, because they are not "index mutual funds". The CSA acknowledge that there may be circumstances in which the principles behind the relief contained in subsection 2.1(5) of the Instrument is also applicable to "partially-indexed" mutual funds. Therefore, the CSA will consider applications from those types of mutual funds for relief analogous to that provided by subsection 2.1(5) of the Instrument.
- (3) It is noted that the manager of an index mutual fund may make a decision to base all or some of the investments of the mutual fund on a different permitted index than a permitted index previously used. This decision might be made for investment reasons or because that index no longer satisfies the definition of "permitted index" in the Instrument. It is noted that this decision by the manager will be considered by the Canadian securities regulatory authorities generally to constitute a change of fundamental investment objectives, thereby requiring securityholder approval under paragraph 5.1(c) of the Instrument. In addition, this decision would also constitute a material change for the mutual fund, thereby requiring an amendment to the simplified

prospectus of the mutual fund and the issuing of a press release under Part 11 of National Instrument 81-106 *Investment Fund Continuous Disclosure*.

**3.3 Special Warrants** - A mutual fund is required by subsection 2.2(3) of the Instrument to assume the conversion of each special warrant it holds. This requirement is imposed because the nature of a special warrant is such that there is a high degree of likelihood that its conversion feature will be exercised shortly after its issuance, once a prospectus relating to the underlying security has been filed.

### **3.4 Investment in Other Mutual Funds**

(1) Paragraph 2.5(2)(c) of the Instrument provides that a mutual fund may not invest in another mutual fund unless the securities of both mutual funds are qualified for distribution in the local jurisdiction. This requirement does not however preclude an investment by a mutual fund in an unqualified class or series of another mutual fund, provided this class or series is referable to the same portfolio of assets of a class or series that is qualified in the local jurisdiction.

(2) Subsection 2.5(7) of the Instrument provides that certain investment restrictions do not apply to investments in other mutual funds made in accordance with section 2.5. For greater certainty, the CSA note that subsection 2.5(7) applies only with respect to a mutual fund's investments in other mutual funds, and not for any other investment or transaction.

**3.5 Instalments of Purchase Price** - Paragraph 2.6(d) of the Instrument prohibits a mutual fund from purchasing a security, other than a specified derivative, that by its terms may require the mutual fund to make a contribution in addition to the payment of the purchase price. This prohibition does not extend to the purchase of securities that are paid for on an instalment basis in which the total purchase price and the amounts of all instalments are fixed at the time the first instalment is made.

**3.6 Purchase of Evidences of Indebtedness** - Paragraph 2.6(f) of the Instrument prohibits a mutual fund from lending either cash or a portfolio asset other than cash. The Canadian securities regulatory authorities are of the view that the purchase of an evidence of indebtedness, such as a bond or debenture, a loan participation or loan syndication as permitted by paragraph 2.3(i) of the Instrument, or the purchase of a preferred share that is treated as debt for accounting purposes, does not constitute the lending of cash or a portfolio asset.

### **3.7 Securities Lending, Repurchase and Reverse Repurchase Transactions**

(1) Section 2.12, 2.13 and 2.14 of the Instrument each contains a number of conditions that must be satisfied in order that a mutual fund may enter into a securities lending, repurchase or reverse repurchase transaction in compliance with the Instrument. It is expected that, in addition to satisfying these conditions, the manager on behalf of the mutual fund, in co-ordination with an agent, will ensure that the documentation evidencing these types of transactions contains customary provisions to protect the mutual fund and to document the transaction properly. Among other things, these provisions would normally include

(a) a definition of an "event of default" under the agreement, which would include failure to deliver cash or securities, or to promptly pay to the mutual fund amounts equal to

- dividends and interest paid, and distributions made, on loaned or sold securities, as required by the agreement;
- (b) provisions giving non-defaulting parties rights of termination, rights to sell the collateral, rights to purchase identical securities to replace the loaned securities and legal rights of set-off in connection with their obligations if an event of default occurs; and
  - (c) provisions that deal with, if an event of default occurs, how the value of collateral or securities held by the non-defaulting party that is in excess of the amount owed by the defaulting party will be treated.
- (2) Section 2.12, 2.13 and 2.14 of the Instrument each imposes a requirement that a mutual fund that has entered into a securities lending, repurchase or reverse repurchase transaction hold cash or securities of at least 102 percent of the market value of the securities or cash held by the mutual fund's counterparty under the transaction. It is noted that the 102 percent requirement is a minimum requirement, and that it may be appropriate for the manager of a mutual fund, or the agent acting on behalf of the mutual fund, to negotiate the holding of a greater amount of cash or securities if necessary to protect the interests of the mutual fund in a particular transaction, having regard to the level of risk for the mutual fund in the transaction. In addition, if the recognized best practices for a particular type of transaction in a particular market calls for a higher level of collateralization than 102 percent, it is expected that, absent special circumstances, the manager or the agent would ensure that its arrangements reflect the relevant best practices for that transaction.
- (3) Paragraph 3 of subsection 2.12(1) of the Instrument refers to securities lending transactions in terms of securities that are "loaned" by a mutual fund in exchange for collateral. Some securities lending transactions are documented so that title to the "loaned" securities is transferred from the "lender" to the "borrower". The Canadian securities regulatory authorities do not consider this fact as sufficient to disqualify those transactions as securities loan transactions within the meaning of the Instrument, so long as the transaction is in fact substantively a loan. References throughout the Instrument to "loaned" securities, and similar references, should be read to include securities "transferred" under a securities lending transaction.
- (4) Paragraph 6 of subsection 2.12(1) permits the use of irrevocable letters of credit as collateral in securities lending transactions. The Canadian securities regulatory authorities believe that, at a minimum, the prudent use of letters of credit will involve the following arrangements:
- (a) the mutual fund should be allowed to draw down any amount of the letter of credit at any time by presenting its sight draft and certifying that the borrower is in default of its obligations under the securities lending agreement, and the amount capable of being drawn down would represent the current market value of the outstanding loaned securities or the amount required to cure any other borrower default; and
  - (b) the letter of credit should be structured so that the lender may draw down, on the date immediately preceding its expiration date, an amount equal to the current market value of all outstanding loaned securities on that date.

- (5) Paragraph 9 of subsection 2.12(1) and paragraph 8 of subsection 2.13(1) of the Instrument each provides that the agreement under which a mutual fund enters into a securities lending or repurchase transaction include a provision requiring the mutual fund's counterparty to promptly pay to the mutual fund, among other things, distributions made on the securities loaned or sold in the transaction. In this context, the term "distributions" should be read broadly to include all payments or distributions of any type made on the underlying securities, including, without limitation, distributions of property, stock dividends, securities received as the result of splits, all rights to purchase additional securities and full or partial redemption proceeds. This extended meaning conforms to the meaning given the term "distributions" in several standard forms of securities loan agreements widely used in the securities lending and repurchase markets.
- (6) Section 2.12, 2.13 and 2.14 of the Instrument make reference to the "delivery" and "holding" of securities or collateral by the mutual fund. The Canadian securities regulatory authorities note that these terms will include the delivery or holding by an agent for a mutual fund. In addition, the Canadian securities regulatory authorities recognize that under ordinary market practice, agents pool collateral for securities lending/repurchase clients; this pooling of itself is not considered a violation of the Instrument.
- (7) Section 2.12, 2.13 and 2.14 of the Instrument require that the securities involved in a securities lending, repurchase or reverse repurchase transaction be marked to market daily and adjusted as required daily. It is recognized that market practice often involves an agent marking to market a portfolio at the end of a business day, and effecting the necessary adjustments to a portfolio on the next business day. So long as each action occurs on each business day, as required by the Instrument, this market practice is not a breach of the Instrument.
- (8) As noted in subsection (7), the Instrument requires the daily marking to market of the securities involved in a securities lending, repurchase or reverse repurchase transaction. The valuation principles used in this marking to market may be those generally used by the agent acting for the mutual fund, even if those principles deviate from the principles that are used by the mutual fund in valuing its portfolio assets for the purposes of calculating net asset value.
- (9) Paragraph 6 of subsection 2.13(1) of the Instrument imposes a requirement concerning the delivery of sales proceeds to the mutual fund equal to 102 per cent of the market value of the securities sold in the transaction. It is noted that accrued interest on the sold securities should be included in the calculation of the market value of those securities.
- (10) Section 2.15 of the Instrument imposes the obligation on a manager of a mutual fund to appoint an agent or agents to administer its securities lending and repurchase transactions, and makes optional the ability of a manager to appoint an agent or agents to administer its reverse repurchase transactions. A manager that appoints more than one agent to carry out these functions may allocate responsibility as it considers best. For instance, it may be appropriate that one agent be responsible for domestic transactions, with one or more agents responsible for offshore transactions. Managers should ensure that the various requirements of sections 2.15 and 2.16 of the Instrument are satisfied for all agents.
- (11) It is noted that the responsibilities of an agent appointed under section 2.15 of the Instrument include all aspects of acting on behalf of a mutual fund in connection with securities lending,

- repurchase or reverse repurchase agreements. This includes acting in connection with the reinvestment of collateral or securities held during the life of a transaction.
- (12) Subsection 2.15(3) of the Instrument requires that an agent appointed by a mutual fund to administer its securities lending, repurchase or reverse repurchase transactions shall be a custodian or sub-custodian of the mutual fund. It is noted that the provisions of Part 6 of the Instrument generally apply to the agent in connection with its activities relating to securities lending, repurchase or reverse repurchase transactions. The agent must have been appointed as custodian or sub-custodian in accordance with section 6.1, and must satisfy the other requirements of Part 6 in carrying out its responsibilities.
- (13) Subsection 2.15(5) of the Instrument provides that the manager of a mutual fund shall not authorize an agent to enter into securities lending, repurchase or, if applicable, reverse repurchase transactions on behalf of the mutual fund unless there is a written agreement between the agent, the manager and the mutual fund that deals with certain prescribed matters. Subsection (5) requires that the manager and the mutual fund, in the agreement, provide instructions to the agent on the parameters to be followed in entering into the type of transaction to which the agreement pertains. The parameters would normally include
- (a) details on the types of transactions that may be entered into by the mutual fund;
  - (b) types of portfolio assets of the mutual fund to be used in the transaction;
  - (c) specification of maximum transaction size, or aggregate amount of assets that may be committed to transactions at any one time;
  - (d) specification of permitted counterparties;
  - (e) any specific requirements regarding collateralization, including minimum requirements as to amount and diversification of collateralization, and details on the nature of the collateral that may be accepted by the mutual fund;
  - (f) directions and an outline of responsibilities for the reinvestment of cash collateral received by the mutual fund under the program to ensure that proper levels of liquidity are maintained at all times; and
  - (g) duties and obligations on the agent to take action to obtain payment by a borrower of any amounts owed by the borrower.
- (14) The definition of "cash cover" contained in section 1.1 of the Instrument requires that the portfolio assets used for cash cover not be "allocated for specific purposes". Securities loaned by a mutual fund in a securities lending transaction have been allocated for specific purposes and therefore cannot be used as cash cover by the mutual fund for its specified derivatives obligations.
- (15) A mutual fund sometimes needs to vote securities held by it in order to protect its interests in connection with corporate transactions or developments relating to the issuers of the securities. The manager and the portfolio adviser of a mutual fund, or the agent of the mutual fund

administering a securities lending program on behalf of the mutual fund, should monitor corporate developments relating to securities that are loaned by the mutual fund in securities lending transactions, and take all necessary steps to ensure that the mutual fund can exercise a right to vote the securities when necessary. This may be done by way of a termination of a securities lending transaction and recall of loaned securities, as described in paragraph 11 of subsection 2.12(1) of the Instrument.

- (16) As part of the prudent management of a securities lending, repurchase or reverse repurchase program, managers of mutual funds, together with their agents, should ensure that transfers of securities in connection with those programs are effected in a secure manner over an organized market or settlement system. For foreign securities, this may entail ensuring that securities are cleared through central depositories. Mutual funds and their agents should pay close attention to settlement arrangements when entering into securities lending, repurchase and reverse repurchase transactions.

### **3.8 Prohibited Investments**

- (1) Subsection 4.1(4) permits a dealer managed mutual fund to make an investment otherwise prohibited by subsection 4.1(1) and the corresponding provisions in securities legislation referred to in Appendix C to NI 81-102 if the independent review committee of the dealer managed mutual fund has approved the transaction under subsection 5.2(2) of NI 81-107. The CSA expect the independent review committee may contemplate giving its approval as a standing instruction, as contemplated in section 5.4 of NI 81-107.
- (2) Subsection 4.3(2) permits a mutual fund to purchase a class of debt securities from, or sell a class of debt securities to, another mutual fund managed by the same manager or an affiliate of the manager where the price payable for the security is not publicly available, if the independent review committee of the mutual fund has approved the transaction under subsection 5.2(2) of NI 81-107 and the requirements in section 6.1 of NI 81-107 have been met. The CSA expect the independent review committee may contemplate giving its approval as a standing instruction, as contemplated in section 5.4 of NI 81-107.
- (3) In providing its approval under paragraph 4.3(2), the CSA expect the independent review committee to have satisfied itself that the price of the security is fair. It may do this by considering the price quoted on a marketplace (e.g., CanPx or TRACE), or by obtaining a quote from an independent, arm's-length purchaser or seller, immediately before the purchase or sale.

## **PART 4 USE OF SPECIFIED DERIVATIVES**

- 4.1 Exercising Options on Futures** - Paragraphs 2.8(1)(d) and (e) of the Instrument prohibit a mutual fund from, among other things, opening and maintaining a position in a standardized future except under the conditions referred to in those paragraphs. Opening and maintaining a position in a standardized future could be effected through the exercise by a mutual fund of an option on futures. Therefore, it should be noted that a mutual fund cannot exercise an option on futures and assume a position in a standardized future unless the applicable provisions of paragraphs 2.8(1)(d) or (e) are satisfied.

**4.2 Registration Matters** - The Canadian securities regulatory authorities remind industry participants of the following requirements contained in securities legislation:

1. A mutual fund may only invest in or use clearing corporation options and over-the-counter options if the portfolio adviser advising with respect to these investments
  - (a) is permitted, either by virtue of registration as an adviser under the securities legislation or commodity futures legislation of the jurisdiction in which the portfolio adviser is providing the advice or an exemption from the requirement to be registered, to provide that advice to the mutual fund under the laws of that jurisdiction; and
  - (b) has satisfied all applicable option proficiency requirements of that jurisdiction which, ordinarily, will involve completion of the Canadian Options Course.
2. A mutual fund may invest in or use futures and options on futures only if the portfolio adviser advising with respect to these investments or uses is registered as an adviser under the securities or commodity futures legislation of the jurisdiction in which the portfolio adviser is providing the advice, if this registration is required in that jurisdiction, and meets the proficiency requirements for advising with respect to futures and options on futures in the jurisdiction.
3. A portfolio adviser of a mutual fund that receives advice from a non-resident sub-adviser as contemplated by section 2.10 of the Instrument is not relieved from the registration requirements described in paragraphs 1 and 2.
4. In Ontario, a non-resident sub-adviser is required, under the commodity futures legislation of Ontario, to be registered in Ontario if it provides advice to another portfolio adviser of a mutual fund in Ontario concerning the use of standardized futures by the mutual fund. Section 2.10 of the Instrument does not exempt the non-resident sub-adviser from this requirement. A non-resident sub-adviser should apply for an exemption in Ontario if it wishes to carry out the arrangements contemplated by section 2.10 without being registered in Ontario under that legislation.

**4.3 Leveraging** - The Instrument is designed to prevent the use of specified derivatives for the purpose of leveraging the assets of the mutual fund. The definition of “hedging” prohibits leveraging with specified derivatives used for hedging purposes. The provisions of subsection 2.8(1) of the Instrument restrict leveraging with specified derivatives used for non-hedging purposes.

**4.4 Cash Cover** - The definition of “cash cover” in the Instrument prescribes the securities or other portfolio assets that may be used to satisfy the cash cover requirements relating to specified derivatives positions of mutual funds required by Part 2 of the Instrument. The definition of “cash cover” includes various interest-bearing securities; the definition includes interest accrued on those securities, and so mutual funds are able to include accrued interest for purposes of cash cover calculations.

## **PART 5           LIABILITY AND INDEMNIFICATION**

### **5.1       Liability and Indemnification**

- (1)       Subsection 4.4(1) of the Instrument contains provisions that require that any agreement or declaration of trust under which a person or company acts as manager of a mutual fund provide that the manager is responsible for any loss that arises out of the failure of it, and of any person or company retained by it or the mutual fund to discharge any of the manager's responsibilities to the mutual fund, to satisfy the standard of care referred to in that section. Subsection 4.4(2) of the Instrument provides that a mutual fund shall not relieve the manager from that liability.
- (2)       The purpose of these provisions is to ensure that the manager remains responsible to the mutual fund and therefore indirectly to its securityholders for the duty of care that is imposed by the securities legislation of most jurisdictions, and to clarify that the manager is responsible to ensure that service providers perform to the level of that standard of care. The Instrument does not regulate the contractual relationships between the manager and service providers; whether a manager can seek indemnification from a service provider that fails to satisfy that standard of care is a contractual issue between those parties.
- (3)       Subsection 4.4(5) of the Instrument provides that section 4.4 does not apply to any losses to a mutual fund or securityholder arising out of an action or inaction by a custodian or subcustodian or by a director of a mutual fund. A separate liability regime is imposed, on custodians or sub-custodians by section 6.6 of the Instrument. Directors are subject to the liability regime imposed by the relevant corporate legislation.

### **5.2       Securities Lending, Repurchase and Reverse Repurchase Transactions**

- (1)       As described in section 5.1, section 4.4 of the Instrument is designed to ensure that the manager of a mutual fund is responsible for any loss that arises out of the failure of it, and of any person or company retained by it or the mutual fund to discharge any of the manager's responsibilities to the mutual fund, to satisfy the standard of care referred to in that section.
- (2)       The retention by a manager of an agent under section 2.15 of the Instrument to administer the mutual fund's securities lending, repurchase or reverse repurchase transactions does not relieve the manager from ultimate responsibility for the administration of those transactions in accordance with the Instrument and in conformity with the standard of care imposed on the manager by statute and required to be imposed on the agent in the relevant agreement by subsection 2.15(6) of the Instrument.
- (3)       Because the agent is required to be a custodian or sub-custodian of the mutual fund, its activities, as custodian or sub-custodian, are not within the responsibility of the manager of the mutual fund, as provided for in subsection 4.4(5) of the Instrument. However, the activities of the agent, in its role as administering the mutual funds' securities lending, repurchase or reverse repurchase transactions, are within the ultimate responsibility of the manager, as provided for in subsection 4.4(6) of the Instrument.

## **PART 6           SECURITYHOLDER MATTERS**

**6.1 Meetings of Securityholders** - Subsection 5.4(1) of the Instrument imposes a requirement that a meeting of securityholders of a mutual fund called for the purpose of considering any of the matters referred to in section 5.1 of the Instrument must be called on notice sent at least 21 days before the date of the meeting. Industry participants are reminded that the provisions of National Policy Statement No. 41, or a successor instrument, may apply to any meetings of securityholders of mutual funds and that those provisions may require that a longer period of notice be given.

## **6.2 Limited Liability**

- (1) Mutual funds generally are structured in a manner that ensures that investors are not exposed to the risk of loss of an amount more than their original investment. This is a very important and essential attribute of mutual funds.
- (2) Mutual funds that are structured as corporations do not raise pressing liability problems because of the limited liability regime of corporate statutes.
- (3) Mutual funds that are structured as limited partnerships may raise some concerns about the loss of limited liability if limited partners participate in the management or control of the partnership. The Canadian securities regulatory authorities encourage managers of mutual funds that are structured as limited partnerships to consider this issue in connection with the holding of meetings of securityholders, even if required under section 5.1 of the Instrument. In addition, all managers of mutual funds that are structured as limited partnerships should consider whether disclosure and discussion of this issue should be included as a risk factor in simplified prospectuses.

## **6.3 Calculation of Fees**

- (1) Paragraph 5.1(a) of the Instrument requires securityholder approval before the basis of the calculation of a fee or expense that is charged to a mutual fund is changed in a way that could result in an increase in charges to the mutual fund. The Canadian securities regulatory authorities note that the phrase “basis of the calculation” includes any increase in the rate at which a particular fee is charged to the mutual fund.
- (2) The CSA are of the view that the requirement of subsection 5.1(a) would not apply in instances where the change to the basis of the calculation is the result of separate individual agreements between the manager of the mutual fund and individual securityholders of the mutual fund, and the resulting increase in charges is payable directly or indirectly by those individual securityholders only.

## **PART 7 CHANGES**

### **7.1 Integrity and Competence of Mutual Fund Management Groups**

- (1) Paragraph 5.5(1)(a) of the Instrument requires that the approval of the securities regulatory authority be obtained before the manager of a mutual fund is changed.

Subsection 5.5(2) of the Instrument contemplates similar approval to a change in control of a manager.

- (2) In connection with each of these approvals, applicants are required by section 5.7 of the Instrument to provide information to the securities regulatory authority concerning the integrity and experience of the persons or companies that are proposed to be involved in, or control, the management of the mutual fund after the proposed transaction.
- (3) The Canadian securities regulatory authorities would generally consider it helpful in their assessment of the integrity and experience of the proposed new management group that will manage a mutual fund after a change in manager if the application set out, among any other information the applicant wishes to provide
  - (a) the name, registered address and principal business activity or the name, residential address and occupation or employment of
    - (i) if the proposed manager is not a public company, each beneficial owner of securities of each shareholder, partner or limited partner of the proposed manager, and
    - (ii) if the proposed manager is a public company, each beneficial owner of securities of each shareholder of the proposed manager that is the beneficial holder, directly or indirectly, of more than 10 percent of the outstanding securities of the proposed manager; and
  - (b) information concerning
    - (i) if the proposed manager is not a public company, each shareholder, partner or limited partner of the proposed manager,
    - (ii) if the proposed manager is a public company, each shareholder that is the beneficial holder, directly or indirectly, of more than 10 percent of the outstanding securities of the proposed manager,
    - (iii) each director and officer of the proposed manager, and
    - (iv) each proposed director, officer or individual trustee of the mutual fund.
- (4) The Canadian securities regulatory authorities would generally consider it helpful if the information relating to the persons and companies referred to in paragraph (3)(b) included
  - (a) for a company
    - (i) its name, registered address and principal business activity,
    - (ii) the number of securities or partnership units of the proposed manager beneficially owned, directly or indirectly, and

- (iii) particulars of any existing or potential conflicts of interest that may arise as a result of the activities of the company and its relationship with the management group of the mutual fund; and
  - (b) for an individual
    - (i) his or her name, birthdate and residential address,
    - (ii) his or her principal occupation or employment,
    - (iii) his or her principal occupations or employment during the five years before the date of the application, with a particular emphasis on the individual's experience in the financial services industry,
    - (iv) the individual's educational background, including information regarding courses successfully taken that relate to the financial services industry,
    - (v) his or her position and responsibilities with the proposed manager or the controlling shareholders of the proposed manager or the mutual fund,
    - (vi) whether he or she is, or within five years before the date of the application has been, a director, officer or promoter of any reporting issuer other than the mutual fund, and if so, disclosing the names of the reporting issuers and their business purpose, with a particular emphasis on relationships between the individual and other mutual funds,
    - (vii) the number of securities or partnership units of the proposed manager beneficially owned, directly or indirectly,
    - (viii) particulars of any existing or potential conflicts of interest that may arise as a result of the individual's outside business interests and his or her relationship with the management group of the mutual fund, and
    - (ix) a description of the individual's relationships to the proposed manager and other service providers to the mutual fund.
- (5) The Canadian securities regulatory authorities would generally consider it helpful in their assessment of the integrity and experience of the persons or companies that are proposed to manage a mutual fund after a change of control of the manager, if the application set out, among any other information that applicant wishes to provide, a description of
  - (a) the proposed corporate ownership of the manager of the mutual fund after the proposed transaction, indicating for each proposed direct or indirect shareholder of the manager of the mutual fund the information about that shareholder referred to in subsection (4);

- (b) the proposed officers and directors of the manager of the mutual fund, of the mutual fund and of each of the proposed controlling shareholders of the mutual fund, indicating for each individual, the information about that individual referred to in subsection (4);
- (c) any anticipated changes to be made to the officers and directors of the manager of the mutual fund, of the mutual fund and of each of the proposed controlling shareholders of the mutual fund that are not set out in paragraph (b); and
- (d) the relationship of the members of the proposed controlling shareholders and the other members of the management group to the manager and any other service provider to the mutual fund.

**7.2 Mergers and Conversions of Mutual Funds** - Subsection 5.6(1) of the Instrument provides that mergers or conversions of mutual funds may be carried out on the conditions described in that subsection without prior approval of the securities regulatory authority. The Canadian securities regulatory authorities consider that the types of transactions contemplated by subsection 5.6(1) of the Instrument when carried out in accordance with the conditions of that subsection address the fundamental regulatory concerns raised by mergers and conversions of mutual funds. Subsection 5.6(1) is designed to facilitate consolidations of mutual funds within fund families that have similar fundamental investment objectives and strategies and that are operated in a consistent and similar fashion. Since subsection 5.6(1) will be unavailable unless the mutual funds involved in the transaction have substantially similar fundamental investment objectives and strategies and are operated in a substantially similar fashion, the Canadian securities regulatory authorities do not expect that the portfolios of the consolidating funds will be required to be realigned to any great extent before a merger. If realignment is necessary, the Canadian securities regulatory authorities note that paragraph 5.6(1)(h) of the Instrument provides that none of the costs and expenses associated with the transaction may be borne by the mutual fund. Brokerage commissions payable as a result of any portfolio realignment necessary to carry out the transaction would, in the view of the Canadian securities regulatory authorities, be costs and expenses associated with the transaction.

### **7.3 Regulatory Approval for Reorganizations**

- (1) Paragraph 5.7(1)(b) of the Instrument requires certain details to be provided in respect of an application for regulatory approval required by paragraph 5.5(1)(b) that is not automatically approved under subsection 5.6(1). The Canadian securities regulatory authorities will be reviewing this type of proposed transaction, among other things, to ensure that adequate disclosure of the differences between the funds participating in the proposed transaction is given to securityholders of the mutual fund that will be merged, reorganized or amalgamated with another mutual fund.
- (2) If a mutual fund is proposed to be merged, amalgamated or reorganized with a mutual fund that has a net asset value that is smaller than the net asset value of the terminating mutual fund, the Canadian securities regulatory authorities will consider the implications of the proposed transaction on the smaller continuing mutual fund. The Canadian securities regulatory authorities believe that this type of transaction generally would constitute a material change for the smaller continuing mutual fund, thereby triggering the requirements of paragraph 5.1(g) of the Instrument and Part 11 of National Instrument 81-106 *Investment Fund Continuous Disclosure*.

**7.4 [Deleted]**

**7.5 Circumstances in Which Approval of Securityholders Not Required**

- (1) Subsection 5.3(2) of the Instrument provides that a mutual fund's reorganization with, or transfer of assets to, another mutual fund may be carried out on the conditions described in the subsection without the prior approval of the securityholders of the mutual fund.
- (2) If the manager refers the change contemplated in subsection 5.3(2) to the mutual fund's independent review committee, and subsequently seeks the approval of the securityholders of the mutual fund, the CSA expect the manager to include a description of the independent review committee's determination in the written notice to securityholders referred to in section 5.4 of this Instrument.

**7.6 Change of Auditor** – Section 5.3.1 of the Instrument requires that the independent review committee of the mutual fund give its prior approval to the manager before the auditor of the mutual fund may be changed.

**7.7 Connection to NI 81-107** – There may be matters under section 5.1 that may also be a conflict of interest matter as defined in NI 81-107. The CSA expect any matter under section 5.1 subject to review by the independent review committee to be referred by the manager to the independent review committee before seeking the approval of securityholders of the mutual fund. The CSA further expect the manager to include a description of the independent review committee's determination in the written notice to securityholders referred to in subsection 5.4(2) of this Instrument.

**PART 8 CUSTODIANSHIP OF PORTFOLIO ASSETS**

**8.1 Standard of Care** - The standard of care prescribed by section 6.6 of the Instrument is a minimum standard only. Similarly, the provisions of section 6.5 of the Instrument, designed to protect a mutual fund from loss in the event of the insolvency of those holding its portfolio assets, are minimum requirements. The Canadian securities regulatory authorities are of the view that the requirements set out in section 6.5 may require custodians and sub-custodians to take such additional steps as may be necessary or desirable properly to protect the portfolio assets of the mutual fund in a foreign jurisdiction and to ensure that those portfolio assets are unavailable to satisfy the claims of creditors of the custodian or sub-custodian, having regard to creditor protection and bankruptcy legislation of any foreign jurisdiction in which portfolio assets of a mutual fund may be located.

**8.2 Book-Based System**

- (1) Subsection 6.5(3) of the Instrument provides that a custodian or sub-custodian of a mutual fund may arrange for the deposit of portfolio assets of the mutual fund with a depository, or clearing agency, that operates a book-based system. Such depositories or clearing agencies include The Canadian Depository For Securities Limited, the Depository Trust Company or any other domestic or foreign depository or clearing

agency that is incorporated or organized under the laws of a country or a political subdivision of a country and operates a book-based system in that country or political subdivision or operates a transnational book-based system.

- (2) A depository or clearing agency that operates a book-based system used by a mutual fund is not considered to be a custodian or sub-custodian of the mutual fund.

**8.3 Compliance** - Paragraph 6.7(1)(c) of the Instrument requires the custodian of a mutual fund to make any changes periodically that may be necessary to ensure that the custodian and sub-custodian agreements comply with Part 6, and that there is no sub-custodian of the mutual fund that does not satisfy the applicable requirements of sections 6.2 or 6.3. The Canadian securities regulatory authorities note that necessary changes to ensure this compliance could include a change of sub-custodian.

## **PART 9 CONTRACTUAL PLANS**

**9.1 Contractual Plans** - Industry participants are reminded that the term “contractual plan” used in Part 8 of the Instrument is a defined term in the securities legislation of most jurisdictions, and that contractual plans as so defined are not the same as automatic or periodic investment plans. The distinguishing feature of a contractual plan is that sales charges are not deducted at a constant rate as investments in mutual fund securities are made under the plan; rather, proportionately higher sales charges are deducted from the investments made during the first year, or in some plans the first two years.

## **PART 10 SALES AND REDEMPTIONS OF SECURITIES**

**10.1 General** - Parts 9, 10 and 11 of the Instrument are intended to ensure that

- (a) investors’ cash is received by a mutual fund promptly;
- (b) the opportunity for loss of an investors’ cash before investment in the mutual fund is minimized; and
- (c) the mutual fund or the appropriate investor receives all interest that accrues on cash during the periods between delivery of the cash by an investor until investment in the mutual fund, in the case of the purchase of mutual fund securities, or between payment of the cash by the mutual fund until receipt by the investor, in the case of redemptions.

### **10.2 Interpretation**

- (1) The Instrument refers to “securityholders” of a mutual fund in several provisions, most notably in Parts 9 and 10 when referring to purchase and redemption orders received by a mutual fund or a participating dealer or principal distributor from “securityholders”.
- (2) Mutual funds must keep a record of the holders of their securities. A mutual fund registers a holder of its securities on this record as requested by the person or company placing a purchase order or as subsequently requested by that registered securityholder. The Canadian securities

regulatory authorities are of the view that a mutual fund is entitled to rely on its register of holders of securities to determine the names of such holders and in its determination as to whom it is to take instructions from.

- (3) Accordingly, when the Instrument refers to “securityholder” of a mutual fund, it is referring to the securityholder registered as a holder of securities on the records of the mutual fund. If that registered securityholder is a participating dealer acting for its client, the mutual fund deals with and takes instructions from that participating dealer. The Instrument does not regulate the relationship between the participating dealer and its client for whom the participating dealer is acting as agent. The Canadian securities regulatory authorities note however, that the participating dealer should, as a matter of prudent business practice, obtain appropriate instructions, in writing, from its client when dealing with the client’s beneficial holdings in a mutual fund.

### **10.3 Receipt of Orders**

- (1) A principal distributor or participating dealer of a mutual fund should endeavour, to the extent possible, to receive cash to be invested in the mutual fund at the time the order to which they pertain is placed.
- (2) A dealer receiving an order for redemption should, at the time of receipt of the investor’s order, obtain from the investor all relevant documentation required by the mutual fund in respect of the redemption including, without limitation, any written request for redemption that may be required by the mutual fund, duly completed and executed, and any certificates representing the mutual fund securities to be redeemed, so that all required documentation is available at the time the redemption order is transmitted to the mutual fund or to its principal distributor for transmittal to the mutual fund.

**10.4 Backward Pricing** - Sections 9.3 and 10.3 of the Instrument provide that the issue price or the redemption price of a security of a mutual fund to which a purchase order or redemption order pertains shall be the net asset value per security, next determined after the receipt by the mutual fund of the relevant order. For clarification, the Canadian securities regulatory authorities emphasize that the issue price and redemption price cannot be based upon any net asset value per security calculated before receipt by the mutual fund of the relevant order.

### **10.5 Coverage of Losses**

- (1) Subsection 9.4(6) of the Instrument provides that certain participating dealers may be required to compensate a mutual fund for a loss suffered as the result of a failed settlement of a purchase of securities of the mutual fund. Similarly, subsection 10.5(3) of the Instrument provides that certain participating dealers may be required to compensate a mutual fund for a loss suffered as the result of a redemption that could not be completed due to the failure to satisfy the requirements of the mutual fund concerning redemptions.
- (2) The Canadian securities regulatory authorities have not carried forward into the Instrument the provisions contained in NP39 relating to a participating dealer’s ability to recover from their clients or other participating dealers any amounts that they were required to pay to a mutual fund. If participating dealers wish to provide for such rights they should make the appropriate

provisions in the contractual arrangements that they enter into with their clients or other participating dealers.

## **PART 11      COMMINGLING OF CASH**

### **11.1      Commingling of Cash**

- (1) Part 11 of the Instrument requires principal distributors and participating dealers to account separately for cash they may receive for the purchase of, or upon the redemption of, mutual fund securities. Those principal distributors and participating dealers are prohibited from commingling any cash so received with their other assets or with cash held for the purchase or upon the sale of securities of other types of securities. The Canadian securities regulatory authorities are of the view that this means that dealers may not deposit into the trust accounts established under Part 11 cash obtained from the purchase or sale of other types of securities such as guaranteed investment certificates, government treasury bills, segregated funds or bonds.
- (2) Subsections 11.1(2) and 11.2(2) of the Instrument state that principal distributors and participating dealers, respectively, may not use any cash received for the investment in mutual fund securities to finance their own operations. The Canadian securities regulatory authorities are of the view that any costs associated with returned client cheques that did not have sufficient funds to cover a trade (“NSF cheques”) are a cost of doing business and should be borne by the applicable principal distributor or participating dealer and should not be offset by interest income earned on the trust accounts established under Part 11 of the Instrument.
- (3) No overdraft positions should arise in these trust accounts.
- (4) Subsections 11.1(3) and 11.2(3) of the Instrument prescribe the circumstances under which a principal distributor or participating dealer, respectively, may withdraw funds from the trust accounts established under Part 11 of the Instrument. This would prevent the practice of “lapping”. Lapping occurs as a result of the timing differences between trade date and settlement date, when cash of a mutual fund client held for a trade which has not yet settled is used to settle a trade for another mutual fund client who has not provided adequate cash to cover the settlement of that other trade on the settlement date. The Canadian securities regulatory authorities view this practice as a violation of subsections 11.1(3) and 11.2(3) of the Instrument.
- (5) Subsections 11.1(4) and 11.2(4) of the Instrument require that interest earned on cash held in the trust accounts established under Part 11 of the Instrument be paid to the applicable mutual fund or its securityholders “pro rata based on cash flow”. The Canadian securities regulatory authorities are of the view that this requirement means, in effect, that the applicable mutual fund or securityholder should be paid the amount of interest that the mutual fund or securityholder would have received had the cash held in trust for that mutual fund or securityholder been the only cash held in that trust account.
- (6) Paragraph 11.3(b) of the Instrument requires that trust accounts maintained in accordance with sections 11.1 or 11.2 of the Instrument bear interest “at rates equivalent to comparable accounts of the financial institution”. A type of account that ordinarily pays zero interest may be used for

trust accounts under sections 11.1 or 11.2 of the Instrument so long as zero interest is the rate of interest paid on that type of account for all depositors other than trust accounts.

**PART 12 [Deleted]**

**PART 13 PROHIBITED REPRESENTATIONS AND SALES COMMUNICATIONS**

**13.1 Misleading Sales Communications**

- (1) Part 15 of the Instrument prohibits misleading sales communications relating to mutual funds and asset allocation services. Whether a particular description, representation, illustration or other statement in a sales communication is misleading depends upon an evaluation of the context in which it is made. The following list sets out some of the circumstances, in the view of the Canadian securities regulatory authorities, in which a sales communication would be misleading. No attempt has been made to enumerate all such circumstances since each sales communication must be assessed individually.
1. A statement would be misleading if it lacks explanations, qualifications, limitations or other statements necessary or appropriate to make the statement not misleading.
  2. A representation about past or future investment performance would be misleading if it is
    - (a) a portrayal of past income, gain or growth of assets that conveys an impression of the net investment results achieved by an actual or hypothetical investment that is not justified under the circumstances;
    - (b) a representation about security of capital or expenses associated with an investment that is not justified under the circumstances or a representation about possible future gains or income; or
    - (c) a representation or presentation of past investment performance that implies that future gains or income may be inferred from or predicted based on past investment performance or portrayals of past performance.
  3. A statement about the characteristics or attributes of a mutual fund or an asset allocation service would be misleading if
    - (a) it concerns possible benefits connected with or resulting from services to be provided or methods of operation and does not give equal prominence to discussion of any risks or associated limitations;
    - (b) it makes exaggerated or unsubstantiated claims about management skill or techniques; characteristics of the mutual fund or asset allocation service; an investment in securities issued by the fund or recommended by the service; services offered by the fund, the service or their respective manager; or effects of government supervision; or

- (c) it makes unwarranted or incompletely explained comparisons to other investment vehicles or indices.
- 4. A sales communication that quoted a third party source would be misleading if the quote were out of context and proper attribution of the source were not given.
- (2) Performance data information may be misleading even if it complies technically with the requirements of the Instrument. For instance, subsections 15.8(1) and (2) of the Instrument contain requirements that the standard performance data for mutual funds given in sales communications be for prescribed periods falling within prescribed amounts of time before the date of the appearance or use of the advertisement or first date of publication of any other sales communication. That standard performance data may be misleading if it does not adequately reflect intervening events occurring after the prescribed period. An example of such an intervening event would be, in the case of money market funds, a substantial decline in interest rates after the prescribed period.
- (3) An advertisement that presents information in a manner that distorts information contained in the preliminary prospectus or prospectus, or preliminary simplified prospectus and annual information form, of a mutual fund or that includes a visual image that provides a misleading impression will be considered to be misleading.
- (4) Any discussion of the income tax implications of an investment in a mutual fund security should be balanced with a discussion of any other material aspects of the offering.
- (5) Paragraph 15.2(1)(b) of the Instrument provides that sales communications may not include any statement that conflicts with information that is contained in, among other things, a simplified prospectus. The Canadian securities regulatory authorities are of the view that a sales communication that provides performance data in compliance with the requirements of Part 15 of the Instrument for time periods that differ from the time periods for which performance data is required to be provided in a simplified prospectus under National Instrument 81-101 is not thereby in violation of the requirements of paragraph 15.2(1)(b) of the Instrument.
- (6) Subsection 15.3(1) of the Instrument permits a mutual fund or asset allocation service to compare its performance to, among other things, other types of investments or benchmarks on certain conditions. Examples of such other types of investments or benchmarks to which the performance of a mutual fund or asset allocation service may be compared include consumer price indices; stock, bond or other types of indices; averages; returns payable on guaranteed investment certificates or other certificates of deposit; and returns from an investment in real estate.
- (7) Paragraph 15.3(1)(c) of the Instrument requires that if the performance of a mutual fund or asset allocation service is compared to that of another investment or benchmark, the comparison sets out clearly any factors necessary to ensure that the comparison is fair and not misleading. Such factors would include an explanation of any relevant differences between the mutual fund or asset allocation service and the investment or benchmark to which it is compared. Examples of such differences include any relevant differences in the guarantees of, or insurance on, the principal of or return from the investment or benchmark; fluctuations in principal, income or total return; any differing tax treatment; and, for a comparison to an index or average, any differences between the

composition or calculation of the index or average and the investment portfolio of the mutual fund or asset allocation service.

### 13.2 Other Provisions

- (1) Subsection 15.9(1) of the Instrument imposes certain disclosure requirements for sales communications in circumstances in which there was a change in the business, operations or affairs of a mutual fund or asset allocation service during or after a performance measurement period of performance data contained in the sales communication that could have materially affected the performance of the mutual fund or asset allocation service. Examples of these changes are changes in the management, investment objectives, portfolio adviser, ownership of the manager, fees and charges, or of policies concerning the waiving or absorbing of fees and charges, of the mutual fund or asset allocation service; or of a change in the characterization of the mutual fund as a money market fund.
- (2) Paragraph 15.11(1)5 of the Instrument requires that no non-recurring fees and charges that are payable by some or all securityholders and no recurring fees and charges that are payable by some but not all securityholders be assumed in calculating standard performance data. Examples of non-recurring types of fees and charges are front-end sales commissions and contingent deferred sales charges, and examples of recurring types of fees and charges are the annual fees paid by purchasers who purchased on a contingent deferred charge basis.
- (3) Paragraphs 15.11(1)2 and 15.11(2)2 of the Instrument require that no fees and charges related to optional services be assumed in calculating standard performance data. Examples of these fees and charges include transfer fees, except in the case of an asset allocation service, and fees and charges for registered retirement savings plans, registered retirement income funds, registered education savings plans, pre-authorized investment plans and systematic withdrawal plans.
- (4) The Canadian securities regulatory authorities are of the view that it is inappropriate and misleading for a mutual fund that is continuing following a merger to prepare and use *pro forma* performance information or financial statements that purport to show the combined performance of the two funds during a period before their actual merger. The Canadian securities regulatory authorities are of the view that such *pro forma* information is hypothetical, involving the making of many assumptions that could affect the results.
- (5) Subsections 15.8(2) and (3) of the Instrument require disclosure of standard performance data of a mutual fund, in some circumstances, from "the inception of the mutual fund". It is noted that paragraph 15.6(d) generally prohibits disclosure of performance data for a period that is before the time when the mutual fund offered its securities under a simplified prospectus or before an asset allocation service commenced operation. Also, Instruction (1) to Item 5 of Part B of Form 81-101F1 Contents of Simplified Prospectus requires disclosure of the date on which a mutual fund's securities first became available to the public as the date on which the mutual fund "started". Therefore, consistent with these provisions, the words "inception of the mutual fund" in subsections 15.8(2) and (3) should be read as referring to the beginning of the distribution of the securities of the mutual fund under a simplified prospectus of the mutual fund, and not from any previous time in which the mutual fund may have existed but did not offer its securities under a simplified prospectus.

- (6) Paragraph 15.6(a) of the Instrument contains a prohibition against the inclusion of performance data for a mutual fund that has been distributing securities for less than 12 consecutive months. The creation of a new class or series of security of an existing mutual fund does not constitute the creation of a new mutual fund and therefore does not subject the mutual fund to the restrictions of paragraph 15.6(a) unless the new class or series is referable to a new portfolio of assets.
- (7) Section 15.14 of the Instrument contains the rules relating to sales communications for multi-class mutual funds. Those rules are applicable to a mutual fund that has more than one class of securities that are referable to the same portfolio of assets. Section 15.14 does not deal directly with asset allocation services. It is possible that asset allocation services could offer multiple "classes"; the Canadian securities regulatory authorities recommend that any sales communications for those services generally respect the principles of section 15.14 in order to ensure that those sales communications not be misleading.
- (8) The Canadian securities regulatory authorities believe that the use of hypothetical or *pro forma* performance data for new classes of securities of a multi-class mutual fund would generally be misleading.

#### **PART 14 [Deleted]**

#### **PART 15 SECURITYHOLDER RECORDS**

- 15.1 Securityholder Records** - Section 18.1 of the Instrument requires the maintenance of securityholder records, including past records, relating to the issue and redemption of securities and distributions of the mutual fund. Section 18.1 does not require that these records need be held indefinitely. It is up to the particular mutual fund, having regard to prudent business practice and any applicable statutory limitation periods, to decide how long it wishes to retain old records.

#### **PART 16 EXEMPTIONS AND APPROVALS**

- 16.1 Need for Multiple or Separate Applications** - The Canadian securities regulatory authorities note that a person or company that obtains an exemption from a provision of the Instrument need not apply again for the same exemption at the time of each prospectus or simplified prospectus refiling unless there has been some change in an important fact relating to the granting of the exemption. This also applies to exemptions from NP39 granted before the Instrument; as provided in section 19.2 of the Instrument, it is not necessary to obtain an exemption from the corresponding provision of the Instrument.

#### **16.2 Exemptions under Prior Policies**

- (1) Subsection 19.2(1) of the Instrument provides that a mutual fund that has obtained, from the regulatory or securities regulatory authority, an exemption from a provision of NP 39 before the Instrument came into force is granted an exemption from any substantially similar provision of the Instrument, if any, on the same conditions, if any, contained in the earlier exemption.

- (2) The Canadian securities regulatory authorities are of the view that the fact that a number of small amendments have been made to many of the provisions of the Instrument from the corresponding provision of NP39 should not lead to the conclusion that the provisions are not “substantially similar”, if the general purpose of the provisions remain the same. For instance, even though some changes have been made in the Instrument, the Canadian securities regulatory authorities consider paragraph 2.2(1)(a) of the Instrument to be substantially similar to paragraph 2.04(1)(b) of NP39, in that the primary purpose of both provisions is to prohibit mutual funds from acquiring securities of an issuer sufficient to permit the mutual fund to control or significantly influence the control of that issuer.
- (3) The CSA are of the view that the new provisions of the Instrument relating to mutual funds investing in other mutual funds introduced on December 31, 2003 are not “substantially similar” to those of the Instrument which they replace.

### **16.3 Waivers and Orders concerning “Fund of Funds”**

- (1) The CSA in a number of jurisdictions have provided waivers and orders from NP39 and securities legislation to permit “fund of funds” to exist and carry on investment activities not otherwise permitted by NP39 or securities legislation. Some of those waivers and orders contained “sunset” provisions that provided that they expired when legislation or a CSA policy or rule came into force that effectively provided for a new “fund of funds” regime. For greater certainty, the Canadian securities regulatory authorities note that the coming into force of the Instrument will not trigger the “sunset” of those waivers and orders.
- (2) For greater certainty, note that the coming into force of National Instrument 81-102 did not trigger the “sunset” of those waivers and orders. However, the coming into force of section 19.3 of the Instrument will effectively cause those waivers and orders to expire one year after its coming into force.