

2006 BCSECCOM 718

September 28, 2006

Headnote

Mutual Reliance Review System for Exemptive Relief Applications - National Instrument 81-106 *Investment Fund Continuous Disclosure*, s. 14.2 – Calculation of Net Asset Value - Investment funds require relief from the requirement in section 14.2 of NI 81-106 *Investment Fund Continuous Disclosure* to calculate net asset value in accordance with Canadian GAAP - Canadian GAAP, as outlined in the Handbook changed through the CICA's adoption of section 3855 of the Handbook; as a result of this change, investment funds must use the bid and ask prices of listed securities to value them, rather than the closing price; because the change will affect different funds at different times, this change in the valuation method could result in different funds and different investors in the same fund being treated differently; this inconsistent treatment is contrary to the intent of section 14.2 of NI 81-106, and could have an adverse effect on the value of an investor's investment in an investment fund; the objective of section 14.2 of NI 81-106 is to ensure all investment funds calculated their net asset value consistently, resulting in a fair and consistent valuation for investors; an investment fund will continue to price its securities for purchase and redemption using the close price, and will use the bid and ask prices to report its net asset value in its annual and interim financial statements; an investment fund must reconcile the two different net asset values in the notes to its financial statements; an investment fund will otherwise comply with Canadian GAAP as required by NI 81-106; the exemption is for a limited time period to permit investment funds to fully assess the impact of this change in Canadian GAAP to their operations

Applicable British Columbia Provisions

National Instrument 81-106 *Investment Fund Continuous Disclosure*, s. 14.2

In the Matter of
the Securities Legislation of
British Columbia, Alberta, Saskatchewan, Manitoba, Ontario, Quebec, New
Brunswick, Nova Scotia, Newfoundland and
Labrador, the Northwest Territories, Nunavut, and Yukon
(the Jurisdictions)

and

In the Matter of
the Mutual Reliance Review System for Exemptive Relief Applications

and

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In the Matter of
AGF Funds Inc., Accumulus Management Ltd., AIC Limited, Aim Funds
Management Inc., Betapro Management Inc., BMO Harris Investment
Management Inc., BMO Investments Inc., BMO Nesbitt Burns Inc., Canadian
Imperial Bank of Commerce, CIBC Asset Management Inc., CI Investments Inc.,
Counsel Group of Funds Inc., Excel Funds Management Inc., Fédération des
Caisses Desjardins du Québec, Fidelity Investments Canada Limited, Franklin
Templeton Investments Corp., Goodman & Company, Investment Counsel Ltd.,
Guardian Group of Funds Ltd., Horizons Funds Inc., I.G. Investment
Management, Ltd., IA Clarington Investments Inc., Impax Funds Management
Inc., Investors Group Investment Management (Quebec) Ltd., Mackenzie
Financial Corporation, Medical Discovery Management Corporation, Northwest
Mutual Funds Inc., PFSL Investments Canada Ltd., RBC Asset Management Inc.,
Russell Investments Canada Limited, TD Asset Management Inc., and United
Financial Corporation, on Behalf of the Investment Funds Under Their
Management (the Funds)
(the Filers)

MRRS Decision Document

Background

The local securities regulatory authority or regulator (the Decision Maker) in each of the Jurisdictions has received an application from the Filers for a decision under National Instrument 81-106 *Investment Fund Continuous Disclosure* (NI 81-106) exempting the Funds, whether under the management of the Filers currently or in the future, and each investment fund which is now or becomes subject to section 14.2 of NI 81-106 which is managed by a manager other than the Applicants (the Affected Funds) from the requirements of section 14.2 of NI 81-106 insofar as it relates to:

- (a) calculating net asset value for any purpose (including for greater certainty, for purchases and redemptions of securities of a mutual fund as required by Parts 9 and 10 of National Instrument 81-102 *Mutual Funds* (NI 81-102)), other than for purposes of the financial statements required of a Fund or Affected Fund under Part 2 of NI 81-106; or
- (b) providing net asset value of a Fund or Affected Fund or information based on net asset value of a Fund or Affected Fund, in any report, marketing material, any other document or any other commentary (including arranging for publication of net asset value pursuant to section 14.2(7) of NI 81-106), other than in the financial statements of the Fund or Affected Fund.

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The relief from section 14.2 of NI 81-106 contemplated by paragraphs (a) and (b) is herein referred to as the Requested Relief.

Under the Mutual Reliance Review System for Exemptive Relief Applications:

- (a) the Ontario Securities Commission is the principal regulator for this application; and
- (b) this MRRS decision document evidences the decision of each Decision Maker.

Interpretation

Defined terms contained in National Instrument 14-101 Definitions have the same meaning in this decision unless they are defined in this decision.

Representations

This decision is based on the following facts represented by the Filers:

1. The Filers are the managers of the Funds under their management. They are responsible for ensuring that the Funds meet the requirements of applicable securities legislation, regulations and rules, including NI 81-106.
2. Each of the existing Funds is a reporting issuer and is subject, amongst others, to the requirements of NI 81-106.
3. Each existing Fund calculates its net asset value, as of the date of this application, as required by section 14.2 of NI 81-106 as currently in effect. Section 14.2 of NI 81-106 requires the Funds and Affected Funds to calculate their net asset value in accordance with Canadian GAAP. Canadian GAAP is modified by the introduction of section 3855 *Financial Instruments – Recognition and Measurement* of the Handbook (section 3855) which applies to financial years beginning on or after October 1, 2006 (the Initial Date).
4. Funds in the industry have different year ends, typically March, June, September or December. As a result, the Initial Date is as early as October 1, 2006 for some Funds, but could theoretically be as late as September 30, 2007 for others.
5. The Filers believe that complying with the requirements of section 3855 will result in a change to net asset value which will vary by type of fund and the holdings of such fund. That change will result from or depend on various factors, including the requirement to use bid price for securities purchased

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long and ask for securities purchased short, instead of closing price for active securities and the interpretation of “active market”.

6. The Filers believe that further study is required of whether the calculation and use of net asset value in accordance with Canadian GAAP for purposes other than financial statements is appropriate before proceeding with the implementation of such change. This will also allow an opportunity for the Filers and regulators to consider international standards which are still developing in this regard.
7. Canadian GAAP is meant to define suitable approaches for financial reporting purposes and those who establish such requirements are concerned with financial reporting. Indeed, section 3855 is not a provision specifically targeted at investment funds and would not have been considered from the perspective of the best interests of investors in such funds, the industry’s perspective or perspectives other than financial reporting. Investors would be subjected to a reduction in the value of their investment funds not from any change in the portfolio securities held by the fund but as a result of the first day change in valuation methodology as a result of Canadian GAAP changes.
8. As is clear from the previous paragraphs, this is not a typical application which results in a benefit for a fund group; rather it is about the consequence arising from the introduction of section 3855 of the CICA Handbook, an event which occurred beyond the industry’s control. It is for this reason that constating documents of Funds have not historically defined, and continue not to define, net asset value for purchases and redemptions by cross reference to Canadian GAAP.
9. The Filers do not believe that it is in the best interests of investors to make any change to begin with, let alone to make such a change as early as October 1, 2006, when most investors and even many of their advisors are relatively unfamiliar with the proposed changes. If a Fund complies with Canadian GAAP as modified by the introduction of section 3855, the net asset value of the Fund will change from the last day of the financial year to the first day of the next year by dint of compliance with section 3855. Investors are generally not aware of this consequence, which sets up the possibility of allowing some investors to engage in arbitrage thereby taking value from other investors. This arbitrage opportunity is in fact one of the issues of concern to the industry. In short, two of the prerequisites for investing, being clarity and quality of communication, clearly do not exist with respect to this issue at this point in time. The Filers do not believe that such a change is in the best interests of investors in the Funds, is prejudicial to existing and future investors and is not necessary for the fair operation of a Fund.

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10. As noted above, the introduction of the proposed change in the way net asset value is calculated for purchases and redemptions and other non-financial statement purposes would apply at different times for different Funds. The Filers believe that such a status would cause further confusion to investors and is also prejudicial to Filers whose Funds would be required to be priced differently than those of their direct competitors in a particular fund category for a period of time.
11. The Filers also note that the change, if implemented, would result in further unfairness due to the fact that the brunt of the time and effort would fall unfairly on those whose Initial Date occurs first. The change would require cost, time and effort with regards to systems, operations and other matters, both directly on the Filers and on third party service providers serving many members of the industry.
12. If the Requested Relief is not granted, the valuation procedures described in the current prospectus and/or annual information form of a Fund would be inaccurate and each Fund would have to amend such offering documents in order to explain the valuation requirements of section 3855 for pricing purposes, including for example, that the bid price must be used for a security in an active market rather than the closing price.
13. Additional time for dialogue between the industry and the Decision Makers will be required to clarify various matters relating to the use of net asset value, including but not limited to, presentation of performance information, quarterly reports, management report of fund performance, and percentages that portfolio investments represent of a fund.

Decision

Each of the Decision Makers is satisfied that the test contained in NI 81-106 that provides the Decision Maker with the jurisdiction to make the decision has been met. The decision of the Decision Makers under NI 81-106 is that the Requested Relief is granted to each Fund and Affected Fund provided that:

1. each Fund and Affected Fund continues to calculate its net asset value for purposes other than its financial statements in accordance with Canadian GAAP without giving effect to section 3855;
2. the notes to the financial statements of a Fund or Affected Fund required under Part 2 of NI 81-106 include a reconciliation of the net asset value in the financial statements to the net asset value calculated in accordance with 1 above and used for other purposes; and

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3. this decision shall terminate on the earlier of (i) September 30, 2007, or (ii) the date on which changes to Part 14 of NI 81-106 come into effect with respect to calculating net asset value for purposes other than the financial statements and providing net asset value of a Fund or Affected Fund or information based on net asset value of a Fund or Affected Fund, in any report, marketing material, any other document or any other commentary.

Susan Silma
Director, Investment Funds Branch
Ontario Securities Commission