

## Annex A

### Specific Questions of the CSA relating to the Proposed 81-102 Amendments

#### Annual Redemptions of Securities Based on NAV

1. Securities legislation defines a “mutual fund” as, among other things, an issuer whose securities entitle the holder to receive on demand, or within a specified period after demand, an amount computed by reference to the value of a proportionate interest of the net assets of the issuer.

The CSA have historically taken the view that “on demand, or within a specified period after demand” in the definition of “mutual fund” means that the securities of the fund entitle the holders to request that their securities be redeemed by the fund more frequently than once a year. This view has permitted investment funds to redeem their securities once a year based on their NAV and still be considered non-redeemable investment funds. We seek feedback on whether the CSA should reconsider its present view and consider an investment fund to be a mutual fund if it offers any redemptions based on NAV.

#### Investment Restrictions

##### *Concentration Restriction*

2. Do you agree with the 10% issuer concentration restriction for non-redeemable investment funds set out in proposed amended section 2.1 of NI 81-102? If not, please provide reasons why non-redeemable investment funds should be permitted to have a higher concentration limit, and how non-redeemable investment funds would benefit from a higher limit. Please also propose a higher limit and provide reasons for the limit.

If NI 81-102 provides for a concentration limit that is greater than 10% for non-redeemable investment funds, should NI 81-104 provide an even higher concentration limit for non-redeemable investment funds that are alternative funds subject to NI 81-104? Or should the concentration limits be the same for non-redeemable investment funds in both NI 81-102 and NI 81-104? We invite feedback on the appropriate balance of the concentration limit in NI 81-102 for non-redeemable investment funds and the concentration limit for non-redeemable investment funds under the alternative funds framework in NI 81-104.

##### *Investments in Illiquid Assets*

3. As non-redeemable investment funds do not redeem their securities regularly based on NAV, the CSA propose that they be permitted to purchase and hold more illiquid assets than the levels currently permitted by subsections 2.4(1) to (3) of NI 81-102. However, we are concerned that a portfolio containing a significant amount of illiquid assets could lead to difficulties in valuing the NAV of the fund. It is critical that the NAV

of an investment fund be accurately valued; for example, non-redeemable investment funds typically pay management and other fees based on the NAV of the fund, NAV is used to measure performance, and many non-redeemable investment funds offer annual redemptions based on NAV.

We have observed that many non-redeemable investment funds do not invest in a substantial amount of illiquid assets; in fact, the majority of non-redeemable investment funds, like mutual funds, hold minimal amounts of illiquid assets. Would the ability to purchase and hold more illiquid assets than the levels currently permitted by subsections 2.4(1) to (3) of NI 81-102 be beneficial for non-redeemable investment funds? What types of illiquid assets do non-redeemable investment funds wish to invest in, and why?

The CSA invite comment on the amount of illiquid assets that would be appropriate for non-redeemable investment funds to purchase and hold, and whether non-redeemable investment funds should be given more time than 90 days to divest illiquid assets (please refer to the mutual fund divestment requirements in subsections 2.4(2) and (3) of NI 81-102). Is there a minimum amount of liquid assets that non-redeemable investment funds should be required to hold to meet ongoing liquidity needs (e.g., to pay management fees and operational expenses)? Should the limit on illiquid asset investments be different for non-redeemable investment funds that do not offer any redemptions and non-redeemable investment funds that offer annual redemptions?

### ***Borrowing***

4. We seek comment on whether the proposed requirement for non-redeemable investment funds to borrow from a “Canadian financial institution” is appropriate. For example, if the majority of an investment fund’s assets are held outside Canada because it focuses on investing in foreign securities, should there be more flexibility to borrow from lenders other than those that are “Canadian financial institutions”? If so, what conditions should the other lenders have to meet?

### ***Investments in Mortgages***

5. We invite comment on the impact of the proposed restriction on investments in non-guaranteed mortgages for publicly offered non-redeemable investment funds. We also seek feedback on the transition period for the proposed restriction. If you consider that a transition period longer than 24 months is required, please explain why. Alternatively, if you think that a grandfathering provision is warranted to exempt these types of funds from the application of the proposed restriction on investments in non-guaranteed mortgages, please comment on the impact such a provision could have on fairness to new market participants and investor understanding.

### ***Fund-of-Fund Structures***

6. Certain non-redeemable investment funds (top funds) use a forward agreement to obtain exposure to an underlying mutual fund that is not subject to NI 81-102. The

underlying mutual fund in this fund-of-fund structure is established solely for the purpose of facilitating the investments of the top fund and it invests in accordance with the restrictions adopted by the top fund.

Under the Proposed 81-102 Amendments, an underlying mutual fund in a fund-of-fund structure would be required to be subject to NI 81-102. The investment restrictions in NI 81-102 applicable to mutual funds are generally more restrictive than the proposed investment restrictions for non-redeemable investment funds. The CSA are considering measures to enable top funds that are non-redeemable investment funds to continue to use the fund-of-fund structure described in the preceding paragraph, such that the underlying mutual fund may continue to invest in accordance with the investment restrictions applicable to the top fund. We seek comment on whether a carve-out from proposed paragraph 2.5(2)(a) of NI 81-102 would be effective for this purpose and if so, what conditions should attach to the use of the carve-out. Are there appropriate alternative measures to enable an underlying fund that is a mutual fund to follow the investment restrictions applicable to the top fund (a non-redeemable investment fund)?

7. Currently, many managers of non-redeemable investment funds that invest using the fund-of-fund structure described in question 6 have only filed prospectuses for the underlying fund in Ontario and/or Québec even though the prospectuses for the top fund (the non-redeemable investment fund) were filed in all of the jurisdictions of Canada.

Under proposed amended paragraph 2.5(2)(c) of NI 81-102, the underlying fund must be a reporting issuer in all the jurisdictions in which the non-redeemable investment fund is a reporting issuer. This is intended to prevent an indirect distribution of the securities of the underlying fund in jurisdictions where the underlying fund has not filed a prospectus and to ensure that the local jurisdiction has authority over both the top fund and the underlying fund. Should proposed amended paragraph 2.5(2)(c) apply to non-redeemable investment funds that use a fund-of-fund structure? If not, why not? What other parameters could be used to address the CSA's objectives?

### **Organizational Costs of New Non-Redeemable Investment Funds**

8. We seek comment on the impact and the benefits and costs of proposed subsection 3.3(3) of NI 81-102. Are there other parameters that could be developed that would achieve benefits similar to the benefits from proposed subsection 3.3(3)? Please also comment on whether the capital raising model followed by non-redeemable investment funds could support the payment of some of the organizational costs out of the proceeds of the initial public offering. Are there specific components of organizational costs that are more appropriately borne by the non-redeemable investment fund and components that are more appropriately borne by the manager? Please provide information about these cost components and what fraction each component typically constitutes of the total organizational costs for launching a new fund, and explain why it is appropriate for the fund or the manager to pay the specific cost components.

## **Dilutive Issuances of Securities**

9. The CSA propose to introduce subsection 9.3(2) to prevent issuances of securities that cause dilution to the NAV of other outstanding securities of a non-redeemable investment fund. Proposed subsection 9.3(3) recognizes that a non-redeemable investment fund that raises additional money from the public through a new issuance of securities must include the price of the securities in the prospectus. We invite comment on whether proposed subsections 9.3(2) and (3) achieve the purpose of preventing dilutive issuances while taking into account how new securities are distributed.

## **Naming Convention for Investment Funds**

10. Please see question 13 in Annex B.

## **Transition Period for Investment Restrictions in Proposed Amended NI 81-102 and Alternatives**

11. We are proposing that existing non-redeemable investment funds be required to comply with the investment restrictions in proposed amended sections 2.2, 2.3,<sup>1</sup> 2.4 and 2.5 of NI 81-102 18 months after the first coming-into-force date of the Proposed 81-102 Amendments pertaining to these sections. We invite feedback on whether the proposed transition period is sufficient. If not, please provide reasons for a longer transition period or provide alternatives to a transition period.

If you think that a grandfathering provision is warranted for existing non-redeemable investment funds, please comment on the scope of a grandfathering provision and explain why existing non-redeemable investment funds should not have to comply with specific sections in Part 2 of NI 81-102. Please also comment on the impact a grandfathering provision could have on fairness to new market participants and investor understanding.

## **Anticipated Costs of the Proposed Amendments and of Implementing the Alternative Funds Framework**

12. Do you agree or disagree that the costs of the Proposed Amendments and the proposals relating to NI 81-104 are proportionate to the benefits? We seek specific data from non-redeemable investment funds and commodity pools on the anticipated costs and benefits of complying with the regulatory framework set out in the proposed amendments to NI 81-102 and the alternative funds regulatory framework being contemplated in NI 81-104.

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<sup>1</sup> Other than proposed paragraph 2.3(2)(b). See question 5 above.