Annex B

Summary of Public Comments and CSA Responses

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Part I – Background
Summary of Comments On March 27, 2013, the Canadian Securities Administrators (CSA) published proposals relating to the second phase of the Modernization of Investment Fund Product Regulation Project (the Modernization Project). The proposals include amendments to National Instrument 81-102 *Mutual Funds* (NI 81-102), changes to Companion Policy 81-102CP (81-102CP), related consequential amendments, and proposals relating to National Instrument 81-104 *Commodity Pools* (NI 81-104) and securities lending, repurchases and reverse repurchases by investment funds (collectively, the Proposals). On June 25, 2013, the CSA published CSA Staff Notice 11-324 *Extension of Comment Period* (CSA Staff Notice 11-324) to extend the closing of the comment period on the Proposals from June 25, 2013 to August 23, 2013. The Proposals aim to (i) introduce core investment restrictions and operational requirements for publicly offered non-redeemable investment funds, other than scholarship plans, (ii) enhance the disclosure requirements relating to securities lending, repurchases and reverse repurchases by investment funds (the Securities Lending Disclosure Proposals), and (iii) create a more comprehensive alternative fund framework to be effected through amendments to NI 81-104 (the Alternative Funds Proposals). As stated in CSA Staff Notice 11-324, we are finalizing certain aspects of the Proposals in advance of others. In particular, we are first focusing on finalizing the proposed amendments that introduce core investment restrictions and operational requirements for non-redeemable

investment funds and certain of the Securities Lending Disclosure Proposals. The Alternative Funds Proposals will be considered in conjunction with certain of the investment restrictions included in the Proposals, which include provisions regarding investments in physical commodities, borrowing cash, short selling and use of derivatives (the Interrelated Investment Restrictions), and will come into force at a later date.

We received submissions from 49 commenters, which are listed in Part V. We have considered the comments received and have made some changes in response to the comments. We wish to thank all those who took the time to comment.

While we appreciate all comments received in relation to the Proposals, we have not provided a summary of the comments in respect of the Alternative Funds Proposals and the Interrelated Investment Restrictions, as they are not being finalized at this time. As we move forward with the implementation of the Alternative Funds Proposals and the Interrelated Investment Restrictions, the CSA will continue to consider all comments received.

Part II - Comments on proposed amendments to NI 81-102

Issue	**Comments**	**Responses**
General comments	Most commenters generally supported the proposed amendments to NI 81-102 (the Proposed Amendments), other than those relating to Part 2 (the Investment Restriction Proposals) and Part 3 (the Organizational Cost Proposals) of NI 81-102. Commenters had differing views with respect to the various provisions of the Investment Restriction Proposals, which are summarized below. A majority of commenters strongly disagreed with the Organizational Cost Proposals. The extensive feedback we received with respect to the Organizational Cost Proposals is summarized below.	We thank all commenters for their feedback. Other than the Investment Restriction Proposals and the Organizational Cost Proposals, the CSA are finalizing the Proposed Amendments subject to certain minor changes discussed in Annex A (the 81-102 Amendments). We are also introducing certain of the Securities Lending Disclosure Proposals as discussed in the CSA Notice of Amendments (the Notice) and in Part III of this Annex B (the Securities Lending Disclosure Requirements, and together with the 81-102 Amendments, the Amendments). After reviewing the comments received, the CSA are

		deferring the implementation of the proposed amendments to sections 2.1 (the issuer concentration restriction) and 2.4 (the illiquid asset restrictions) of NI 81-102, among others, until such time as the Alternative Funds Proposals and the Interrelated Investment Restrictions are finalized. Moreover, the CSA will continue to consider how best to proceed on the Organizational Cost Proposals. Accordingly, the issuer concentration restriction and the illiquid asset restrictions, as well as proposed amendments regarding organizational costs, may be republished for comment concurrently with the publication for comment of the Alternative Funds Proposals and the Interrelated Investment Restrictions.
Concentration restriction (s. 2.1)	Most commenters disagreed with the issuer concentration restriction, which would require non-redeemable investment funds to limit their investment in an issuer to an amount equal to 10% of net asset value (NAV) at the time of purchase. Several commenters submitted that, unlike conventional mutual funds, non-redeemable investment funds are not meant to be used as an investor's sole or primary investment vehicle, but are intended to achieve a particular investment strategy within a broader overall portfolio. One of these commenters explained that the diversification benefits of a concentration restriction, which allow investors to benefit from investing in a	After considering the comments received, the CSA have decided not to finalize the issuer concentration restriction at this time. While the CSA recognize that non-redeemable investment funds have different diversification and liquidity requirements than mutual funds, the CSA continue to think that these differences do not support the absence of any concentration limit for non-redeemable investment funds. Given that the majority of non-redeemable investment funds adopt an issuer concentration limit, the CSA continue to be of the view that retail investors generally expect that all publicly offered investment funds provide some level of diversification.

	fund as compared to investing on an individual account basis, do not apply to investors of non-redeemable investment funds. These investors generally invest in non-redeemable investment funds through an individual account at a dealer member of the Investment Industry Regulatory Organization of Canada (IIROC), which account would include other investments such as stocks and bonds. Therefore, diversification for non-redeemable investment fund investors is achieved at the portfolio level rather than at the product level, as is done by many mutual fund investors. Several commenters submitted that, in the process of structuring a new non-redeemable investment fund, the appropriate level of diversification is determined by the theme and objectives of the product only, and not by investor expectation or industry practice. Many commenters underscored that non-redeemable investment funds are niche products designed around particular investment themes, objectives and techniques, and to propose that all non-redeemable investment funds achieve the same diversification objective has the potential to stifle innovation and investor choice. According to these commenters, a concentration restriction will unnecessarily limit the range of investment strategies available to portfolio managers. Many commenters also submitted that the concentration limit exists for mutual funds as a rudimentary protection to ensure that the fund preserves a level of liquidity to meet redemptions.	The CSA also recognize that non-redeemable investment funds may use a broad range of investment strategies and investment restrictions to achieve the particular investment objectives of each fund. The CSA note that some of these investment objectives may require higher concentration limits than others. While the CSA consider it important for non-redeemable investment funds to retain sufficient flexibility to pursue diverse investment strategies, the CSA also think there should be appropriate differentiation between the concentrated exposure of non-redeemable investment funds using conventional strategies and those using more alternative strategies. Accordingly, the CSA think that any concentration limit applicable to non-redeemable investment funds should provide for a sufficient level of portfolio diversification while providing managers with the flexibility to pursue certain strategies. Also, while the CSA agree that due diligence and scrutiny of potential offerings of non-redeemable investment funds by multiple parties is beneficial, in our view such due diligence does not completely obviate the need for guidelines and restrictions around the activities of non-redeemable investment funds, particularly in respect of a non-redeemable investment fund's ongoing activities after the initial public offering. In the notice accompanying the Proposals published on March 27, 2013 (the Request for Comments), the CSA indicated that we will consider whether there should be

	Unlike mutual funds, non-redeemable investment funds are not constrained by the need to maintain certain levels of liquidity, as they generally only offer annual redemptions and have redemption notice periods of up to 60 days. Further, since most non-redeemable investment funds are listed on an exchange, investors have a source of liquidity that does not impact the fund's investment portfolio. While several commenters acknowledged that the majority of currently existing non-redeemable investment funds adopt a 10% concentration restriction, they also disagreed that it reflects an industry best practice. We were told that certain non-redeemable investment funds impose a 10% concentration restriction to satisfy one of the conditions necessary to qualify as a "mutual fund trust" for purposes of the *Income Tax Act*, while others may impose a concentration restriction to reflect a diversification objective, such as for risk management or for investment reasons. Other commenters emphasized that new regulation should not be introduced simply because most non-redeemable investment funds at this point in time have adopted similar parameters. We were told that such an approach to regulation would be careless because it does not allow for changing needs and demands of investors, or changing economic and financial conditions. Several commenters noted that many existing non-redeemable investment funds have investment theses	different concentration limits for non-redeemable funds in NI 81-102 and non-redeemable funds subject to the alternative funds framework in NI 81-104. Accordingly, the CSA will continue to consider the appropriate concentration limit for non-redeemable investment funds in conjunction with considering the Alternative Funds Proposals. When considering the appropriate concentration limit for non-redeemable investment funds, the CSA will consider the different investment strategies currently used by non-redeemable investment funds, including, among other things, whether non-redeemable investment funds whose investment objectives or strategies require concentrated portfolios should be regulated under the alternative fund framework or whether there should be exemptions similar to the fixed portfolio carve-out for exchange-traded funds.

	that permit the fund to hold securities of a small number of issuers. For example, many funds provide exposure to certain industries and sectors, such as the Canadian banking, insurance or wireless industries, that are highly concentrated and provide fewer than ten investment positions. These funds, which have been long accepted in the marketplace, would not comply with the 10% concentration restriction and may not fall under the proposed carve-out for fixed portfolio funds. In these commenters' view, investors should not be restricted from buying a non-redeemable investment fund that provides exposure to such a limited number of issuers, given that these investors would not be restricted from buying the underlying companies. We were told that buying the securities directly would not permit investors to benefit from the overlay strategies used by a non-redeemable investment fund to reduce risk or increase cash income. One commenter also noted that the level of risk and innovation provided by industry-specific funds would make their designation as alternative funds inappropriate. We were told that, other than industry-specific funds, existing non-redeemable investment funds structured to provide concentrated exposure above the proposed 10% concentration restriction include funds with subsidiaries, split share corporations that may have 100% exposure to one underlying issuer, fund-of-fund structures where a top fund may have exposure to a single counterparty under a derivative, and funds that	

	invest in flow-through shares of resource issuers (flow-through funds). In respect of flow-through funds, two commenters noted that a concentration restriction would not be relevant, as the securities of such funds are not redeemable. Accordingly, there is no direct correlation between liquidity risk to investors and the operational liquidity required for flow-through funds. One commenter added that the imposition of a concentration restriction would lead to unintentional consequences for existing non-redeemable investment funds that obtain exposure to underlying funds through forward agreements. These non-redeemable investment funds would find themselves offside the concentration restriction and would be required to terminate their forward arrangements prematurely, thereby triggering unnecessary tax consequences for investors. One commenter also noted that there are some non-redeemable investment funds that use indices as benchmarks and that it is not uncommon for indices to have components with a greater than 10% weighting. Several commenters suggested that a concentration restriction is unnecessary in light of the extensive disclosure provided about a non-redeemable investment fund's investment strategies and restrictions in the long form prospectus. With this disclosure, investors and advisors can make an informed judgment on whether the fund's strategy is appropriate.	

	A few commenters also submitted that non-redeemable investment funds coming to market under a long form prospectus are thoroughly scrutinized and subject to vetting and due diligence by many registered investment dealers who have liability for the prospectus disclosure. This vetting process involves the issuer, the issuer's counsel, the lead investment dealer acting as agent and its counsel, as well as the entire syndicate of investment dealers, and results in a dynamic set of restrictions designed specifically for the particular investment objective, strategy and asset class of the fund. In addition, fund securities are only distributed by registered investment dealers who are subject to Know Your Client, suitability and other obligations. These commenters believed that this multi-layered approval process allows the market to impose its own discipline such that a concentration restriction is not necessary. One commenter suggested that regulations should be focused on the manager to ensure that the manager has the expertise to manage the strategies and objectives of the fund, rather than restricting investment strategies. Of those commenters who agreed with the introduction of a concentration restriction for non-redeemable investment funds, a few recommended concentration limits of 15% to 20% of NAV. Some of these commenters felt that this threshold would provide for a sufficient level of portfolio diversification while providing managers with the flexibility to pursue certain strategies. Other commenters submitted that these would be acceptable thresholds only if the fixed	

	portfolio fund exemption was broadened to provide for rules-based or formulaic portfolios (that would permit rebalancing or portfolio substitutions) and subject to a look-through for fund-of-fund investments. Another commenter suggested that a concentration limit of 25% to 30% of NAV would achieve the appropriate balance for providing non-redeemable investment funds with investment flexibility while at the same time providing for reasonable diversification. One commenter submitted that an appropriate concentration limit for flow-through funds would be 20% of NAV. This commenter felt that such a restriction would continue to permit managers to purchase a higher concentration of higher quality investments. One commenter thought that there should be no concentration limit if non-redeemable investment funds are no longer permitted to offer redemptions of their securities with reference to NAV. When considering an appropriate limit for non-redeemable investment funds, many commenters were of the view that this investment restriction is interrelated with the Alternative Funds Proposals and should be considered concurrently with amendments to NI 81-104. One commenter suggested, for example, that it would not be opposed to a 10% concentration limit for non-redeemable investment funds if there were no limit for	

	alternative funds.	
Control restriction (s. 2.2)	One commenter questioned the interpretation of proposed section 2.2 of NI 81-102 in section 3.2.1 of 81-102CP, which would, in this commenter's view, bring into question the activities of fund managers who take a more activist approach in managing mutual funds. This commenter thought that the CSA should engage in more consultation before finalizing this policy pronouncement.	No change. Section 3.2.1 of 81-102CP is consistent with the CSA's view that investment funds should not be operating businesses or take active control over the management of issuers in which they invest. However, we have made minor amendments to the language in section 3.2.1 of 81-102CP to clarify that the discussion of "control" in section 3.2.1 is only with respect to section 2.2 of NI 81-102 and may not be applicable to "control" as used in other provisions of securities legislation.
Investments in non-guaranteed mortgages (s. 2.3(2)(b))	Many commenters questioned the CSA's proposal to prohibit non-redeemable investment funds from investing in mortgages others than guaranteed mortgages (the non-guaranteed mortgage restriction). Some commenters noted that there has been recent discussion by the CSA regarding whether investment funds that invest all or substantially all of their assets in mortgages (MIEs) are investment funds or whether they should be regulated under the securities law regime for issuers that are not investment funds. A few commenters urged the CSA to clarify their current position about whether an MIE satisfies the definition of an investment fund. Along this line, one commenter conveyed that MIEs should not be able to choose whether to be regulated as investment funds or corporate issuers, and further suggested that uniform rules should apply across Canada.	No change. The CSA are of the view that, generally, non-guaranteed mortgages are not appropriate investments for publicly offered non-redeemable investment funds. Given that investing in non-guaranteed mortgages can be akin to engaging in a lending business, we think such an investment is contrary to the nature of an investment fund. Moreover, investments in non-guaranteed mortgages may, in the event of borrower default, require the MIE to exercise and enforce its rights as a mortgagee, which includes managing the real property underlying the mortgage until such time as the MIE is able to dispose of the property. The CSA are of the view that such activities require certain business expertise and are generally outside the scope of portfolio management typically engaged in by investment funds. Further, given the CSA's view that the mortgage lending activities engaged in by many MIEs are akin to

	If the CSA are of the view that it is more appropriate to regulate MIEs as non-investment fund issuers, a few commenters questioned how MIEs transitioning from the regulatory regime for investment funds to the regulatory regime for issuers that are not investment funds would alleviate any concerns regarding investor protection. One such commenter noted that the benefits of being invested in an investment fund, including redemptions, the publication of NAV, the imposition of investment restrictions and the presence of a registered investment fund manager, would be lost if MIEs are no longer subject to the regulatory regime for investment funds.	a lending business, we think the prospectus disclosure and continuous disclosure requirements applicable to investment funds are not designed to provide information regarding operating businesses. Accordingly, better disclosure regarding an operating business can be provided to investors by complying with the disclosure requirements applicable to non-investment fund issuers. The CSA also note that the non-guaranteed mortgage restriction will apply equally in every jurisdiction of Canada. Despite the above, in order to provide time for MIEs subject to NI 81-102 to consider divesting their non-guaranteed mortgages or transitioning to the regulatory regime applicable to reporting issuers that are not investment funds, the CSA are grandfathering existing non-redeemable investment funds that have adopted fundamental investment objectives to permit them to invest in mortgages, such that the non-guaranteed mortgage restriction will not apply to them. See new subsection 20.4(2) of NI 81-102 and "Transitioning and grandfathering of existing funds" below.
	One commenter suggested that CSA staff engage with investors so that they may understand why MIEs may be transitioning from investment funds to non-investment funds, what impact a change in regulatory regime will have on the value of their investments and whether there will be grandfathering provisions. On the other hand, if MIEs may be structured as non-	The CSA are of the view that it is up to each MIE to determine how to respond to paragraph 2.3(2)(b) of NI 81-102. Some MIEs may decide to divest their non-guaranteed mortgages, while others may decide to transition to the regulatory regime applicable to reporting issuers that are not investment funds. As discussed above, investments in non-guaranteed

	redeemable investment funds, certain commenters felt that the non-guaranteed mortgage restriction inappropriately restricts non-redeemable investment fund investment in non-guaranteed mortgages.	mortgages introduce certain potential issues not found with guaranteed mortgages such as the possible need to seize, manage and dispose of the real property underlying the mortgage in the event of borrower default.
	A few commenters suggested that one reason for the proposed non-guaranteed mortgage restriction may be the illiquid nature of mortgage investments. These commenters submitted that illiquidity is not a sufficient reason to preclude non-redeemable investment funds from investing in non-guaranteed mortgages, as non-redeemable investment funds are able to match their redemption rights to the liquidity of their investment portfolio through other means, such as limiting annual redemptions of their securities and providing for a lengthy notice and payment time period for redemptions.	While the illiquidity of, and difficulty of valuing, mortgages are concerns for the CSA, the additional concern addressed by the non-guaranteed mortgage restriction is that investments in non-guaranteed mortgages are generally inappropriate for publicly offered non-redeemable investment funds. See the reasons provided above.
	We were also told that a portfolio of mortgages provides monthly income to a non-redeemable investment fund that covers ongoing liquidity needs, such as management fees and operational expenses, and thus, liquidity for a MIE is not wholly dependent on the ability to sell the fund's assets.	See response above.
	Some commenters suggested that another reason for the proposed non-guaranteed mortgage restriction may be concerns regarding the ability to accurately value mortgage investments. These commenters noted that valuation is not an issue, given that accounting guidelines in Canada specifically address the valuation of mortgages.	See response above.

	One commenter suggested that the reasoning behind the non-guaranteed mortgage restriction may stem from sub-prime non-guaranteed mortgages becoming a contributing factor to the 2008 financial crisis. This commenter told us that the Canadian mortgage market differs fundamentally from the market in the United States and did not experience the same outcomes in 2008. A few commenters thought that it was not clear from the Request for Comments or CSA Staff Notice 31-323 *Guidance Relating to the Registration Obligations of Mortgage Investment Entities* why the CSA are making a distinction between guaranteed and non-guaranteed mortgages. A few commenters were of the view that investments in mortgages should not be restricted to guaranteed mortgages, in the same way that bond investors should not be restricted to only holding guaranteed government bonds. One of these commenters told us that the non-guaranteed mortgage restriction seems to put mortgage investments in an unfair competitive position versus other investment alternatives such as corporate bonds and equities with which an investor is at risk for loss of capital. One commenter questioned why non-redeemable investment funds would be prohibited from holding non-guaranteed mortgages while mutual funds may do	The CSA are not of the view that entities should not invest in non-guaranteed mortgages nor do we take issue with MIEs in general. The non-guaranteed mortgage restriction is not intended to impede investments in non-guaranteed mortgages altogether, and only restricts non-redeemable investment funds that are reporting issuers from purchasing non-guaranteed mortgages. Accordingly, the non-guaranteed mortgage restriction is unrelated to the 2008 financial crisis. See responses above regarding the CSA's concerns associated with non-guaranteed mortgage investments. The distinction between guaranteed and non-guaranteed mortgages has always been recognized by NI 81-102 in respect of mutual funds by virtue of what is now paragraph 2.3(1)(b) of NI 81-102. As stated above, the CSA do not have a view with respect to whether entities should invest in non-guaranteed mortgages nor do we take issue with MIEs in general. The non-guaranteed mortgage restriction only applies to publicly offered non-redeemable investment funds. Issuers that are not investment funds may continue to invest in non-guaranteed mortgages. Mutual funds are generally not permitted to invest in non-guaranteed mortgages by virtue of paragraph 2.3(1)(b) of NI 81-102. The exception to this restriction

	so subject only to compliance with the provisions of National Policy Statement 29 *Mutual Funds Investing in Mortgages* (NP 29). In this commenter's view, if it is acceptable to sell MIEs as low-risk investments through the mutual fund dealer channel, they should be acceptable in the IIROC channel as well. This commenter questioned whether the CSA is also planning to abolish NP 29.	is currently provided by section 20.4 of NI 81-102 for mutual funds which existed prior to the coming into force of NI 81-102, and which comply with NP 29. Please note that under the Amendments, section 20.4 is renumbered as subsection 20.4(1).
	One commenter suggested amending the non-guaranteed mortgage restriction to mirror the restriction in NP 29, whereby only mortgages that exceed a specified loan to value ratio require insurance, and only applying this rule to those non-redeemable investment funds whose primary objective is not mortgage investing.	No change made. The CSA are not imposing an insurance requirement on mortgages. Rather, the non-guaranteed mortgage restriction simply restricts the types of mortgages that publicly offered non-redeemable investment funds may purchase.
	Another commenter suggested that the loan to value ratio is the correct determinant of whether mortgage insurance should be required, rather than the particular legal or listing structure of the lender.	No change made. See response immediately above.
	Certain commenters told us that mortgages are not an asset class that investors can participate in individually and therefore, the non-guaranteed mortgage restriction would preclude Canadian investors from the opportunity to invest in this asset class, which has generated attractive returns in the past on a basis uncorrelated with the capital markets. Accordingly, investors should be allowed to make an informed investment decision based on prospectus disclosure and continuous disclosure.	Investors may continue to invest in non-guaranteed mortgages through MIEs that are not investment funds. The CSA note that there are currently a number of such MIEs which are reporting issuers, and a reporting issuer that wishes to invest its assets in non-guaranteed mortgages may do so as an issuer that is not an investment fund.

	One commenter told us that mortgages can form part of a well-diversified portfolio and a non-redeemable investment fund which invests in mortgages may be appropriate for some investors. However, this commenter recommended that rules be imposed to require the non-redeemable investment fund's manager to be at arm's-length from the mortgagor and any of the parties to the real estate transaction. Another commenter noted that MIEs provide an alternative source of financing in mortgages. In this commenter's view, restricting MIEs to only holding guaranteed mortgages will limit their ability to target markets, will restrict competition and could result in some types of mortgage loans disappearing from the marketplace. One commenter also asked whether the MIE entity analysis would apply to issuers who hold collateralized debt obligations (CDOs) as they have many similarities with mortgage investment entities. This commenter indicated that it would be helpful to understand what the CSA's regulatory response will be, as many CDO offerings are being done on a private placement basis and it is inevitable that this structure will enter the public fund space. A number of commenters noted that, currently, no non-redeemable investment funds have investment objectives to invest in guaranteed mortgages. Therefore, according to these commenters, the non-guaranteed mortgage restriction would effectively eliminate MIEs from the investment fund category.	See the responses above. Despite the non-guaranteed mortgage restriction, the CSA are not expressing a view with respect to the role that mortgages may play in a portfolio or their appropriateness for investors. See the responses above. A discussion of issuers who hold CDOs is beyond the scope of the Modernization Project. See responses above. For the reasons provided above, the CSA are of the view that MIEs generally engage in activities inconsistent with the nature of an investment fund and should be regulated under the regulatory regime for non-investment fund issuers.

	One commenter told us that some MIEs will have to change their investment objectives to comply with the non-guaranteed mortgage restriction, which may make them uneconomic and will drastically change their return profile.	The CSA have introduced new subsection 20.4(2) of NI 81-102, such that the non-guaranteed mortgage restriction will not apply to certain existing MIEs. Therefore, there is no requirement for such MIEs to amend their investment restrictions at this time. See "Transitioning and grandfathering of existing funds" below.
	A few commenters were of the view that the effect of the non-guaranteed mortgage restriction will be that MIEs will not meet the listing requirements of the Toronto Stock Exchange (the TSX). As one commenter noted, one of the reasons for an issuer to elect to be regulated as an investment fund is that the listing requirements of the TSX are able to be met.	In our view, being able to meet the listing requirements of an exchange does not provide a sufficient policy basis for permitting non-redeemable investment funds to engage in activity which may be inconsistent with their nature.
	According to these commenters, a new MIE would first need to raise funds in the exempt market in order to have the appropriate financial performance to meet the TSX listing requirements as a corporate issuer. Some of these commenters felt that the CSA should engage in a dialogue with the TSX prior to finalizing the proposed restrictions since they could severely hamper new entrants and investor choice. One commenter also added that the CSA cannot properly conduct a cost-benefit analysis of the non-guaranteed mortgage restriction without understanding whether the TSX intends to delist existing MIEs.	See the response immediately above.
	One commenter requested further clarity on the definition of a non-guaranteed mortgage. According to this commenter, certain mortgages are not guaranteed	"Guaranteed mortgage" is a defined term in NI 81-102. For the purposes of the Notice and this Annex B, a "non-guaranteed mortgage" refers to a mortgage that is

	but have sufficient collateral to support the mortgage value and present less risk. One commenter noted that the definition of "mortgage" is very broad and covers any debt obligation that is charged on real property (such as corporate issue bonds and other loans) and may result in a restriction that is broader than intended. Many commenters were in favour of grandfathering existing non-redeemable investment funds that invest in non-guaranteed mortgages. These comments are summarized in Part IV of this Annex B, along with other comments regarding grandfathering and transition periods.	not a guaranteed mortgage. We note that, to date, mutual funds have not had difficulty with the definition of "mortgage" in NI 81-102 in connection with complying with their investment restrictions. The CSA have introduced new subsection 20.4(2) of NI 81-102 such that the non-guaranteed mortgage restriction will not apply to certain existing non-redeemable investment funds. See "Transitioning and grandfathering of existing funds".
Investments in illiquid assets (s. 2.4)	Most commenters were of the view that the illiquid asset restrictions should not apply to non-redeemable investment funds. Many commenters told us that the definition of "illiquid asset" in NI 81-102 is problematic and that the illiquid asset restrictions cannot be fully considered or commented on until the definition is modernized. Several commenters expressed that the "illiquid asset" definition needs to be updated to reflect the current market environment, as the definition unintentionally captures highly liquid securities. These commenters thought that the current definition does not address the purpose of the illiquid asset restriction because some securities that are considered liquid, such as certain equity securities and fixed income securities, are very	After considering the comments received, the CSA have decided not to finalize, at this time, the illiquid asset restrictions. In conjunction with considering the Alternative Funds Proposals, the CSA will continue to consider what requirements concerning illiquid assets, including a maximum limit and related divestiture requirement, are appropriate for non-redeemable investment funds. In conjunction with considering the appropriate illiquid asset limits for non-redeemable investment funds, the CSA will also revisit the definition of "illiquid asset" in NI 81-102 and consider whether it continues to keep pace with industry investment standards. While the CSA recognize that non-redeemable investment funds have different liquidity requirements

	thinly traded, whereas certain non-public securities that actively trade in the grey market or over-the-counter (OTC), and for which independent market pricing is relatively easy to obtain, are considered illiquid. These include high yield bonds, senior loans, mutual funds redeemable daily at NAV, and OTC derivatives. A few other commenters expressed that certain elements of the "illiquid asset" definition are difficult to interpret and apply. For example, it is not clear whether "public quotations" is intended to capture securities or instruments that are not listed on conventional exchanges. Further, it is unclear whether the definition is intended to exclude mortgages or securities whose resale is restricted by law. Many commenters submitted that the purpose of the illiquid asset restrictions in NI 81-102 is to ensure that there is not a mismatch between requests for redemptions of a mutual fund's securities by securityholders and the ability of the fund to meet those redemptions. According to these commenters, non-redeemable investment funds do not need to maintain the same levels of liquidity as mutual funds because they generally only offer redemptions once per year, they have redemption notice periods of up to 60 days, and liquidity is primarily obtained through trading on an exchange. Further, there is a lengthy timeline for the payment of redemption proceeds. Therefore, these commenters felt that cash flow needs are different for non-redeemable investment funds than for mutual funds.	than mutual funds, the CSA continue to think that these differences do not support the absence of any illiquid asset limit for non-redeemable investment funds, especially given that the majority of non-redeemable investment funds offer an annual redemption at NAV, which requires a non-redeemable investment fund to maintain a certain level of liquidity in its portfolio to fund redemptions (and to pay ongoing expenses). We note that the majority of non-redeemable investment funds already adopt an internal limit for illiquid assets equal to 10% of NAV. Moreover, illiquid assets are generally more difficult to value and, therefore, may raise questions regarding fees calculated in relation to the NAV of a non-redeemable investment fund which invests a large portion of its assets in illiquid assets. These valuation problems are, in the CSA's view, not sufficiently mitigated by disclosure. The CSA recognize that the ability to invest in illiquid assets has historically been a distinguishing feature of non-redeemable investment funds. While the CSA consider it beneficial for non-redeemable investment funds to retain some flexibility to invest in illiquid assets, we think a maximum limit would mitigate the liquidity and valuation concerns associated with investing substantial portions of an investment fund's assets in illiquid assets. The CSA consider that disclosure of illiquid asset investments and their associated risks in a non-redeemable investment fund's prospectus may not sufficiently address these concerns.

	Several commenters noted that managers already endeavour to structure funds that are able to meet annual redemptions. For example, many non-redeemable investment funds hold minimal amounts of illiquid assets because investors generally desire annual redemptions. At the same time, where an investment mandate contemplates significant amounts of illiquid assets, redemption rights are either capped or not offered at all. It was submitted that this demonstrates market discipline is working effectively. One commenter emphasized that the manager is in the best position to evaluate a non-redeemable investment fund's liquidity needs, which will be determined by factors such as the frequency of redemptions, other cash flow needs, the fund's investment mandate, overall market conditions and outlook for different asset classes. Many commenters strongly believed that non-redeemable investment funds should be afforded more flexibility to invest in illiquid assets. It was submitted that, historically, the unique investment objectives and strategies offered by the ability to invest in illiquid assets was one of the primary benefits of the non-redeemable investment fund structure over the mutual fund structure. One commenter submitted that illiquid investments, such as securities issued by private companies, OTC and thinly traded securities and OTC options, can be undervalued by the market as a result of their illiquid nature, which provides an opportunity for a non-	While the CSA note that managers do generally set illiquid asset levels with a view to a given non-redeemable investment fund's structure, the CSA think that a baseline level applicable to all non-redeemable investment funds is important for the reasons stated above. To address the CSA's concerns in the meantime, the CSA have introduced section 3.3.1 of 81-102CP, which sets out some of the CSA's expectations concerning a non-redeemable investment fund's practices with respect to investing in illiquid assets. The CSA agree that an appropriate illiquid asset limit would provide non-redeemable investment funds with sufficient flexibility to pursue a range of investment strategies, while not posing significant challenges to valuation or creating substantial risk of liquidity problems. The CSA will therefore consider, when determining the appropriate illiquid asset restrictions for non-redeemable investment funds, the different investment strategies and asset classes used by non-redeemable investment funds that may require higher levels of illiquid assets. Furthermore, the CSA will consider, when proposing the illiquid asset restrictions for non-redeemable investment funds, whether different illiquid asset limits should apply to non-redeemable investment funds whose securities do not permit securityholders to request that the fund redeem their securities (for example, non-redeemable investment funds which invest in flow-through shares of resources issuers).

	redeemable investment fund to earn a higher return, particularly over the longer term. Some commenters were concerned that the illiquid asset restrictions would limit or prohibit investments in flow-through securities of junior exploration companies, public-private infrastructure partnerships, venture capital opportunities, mortgages and other investments that could benefit investors as well as the economy. A few commenters noted in particular that investments in securities that are subject to hold periods should not be restricted if the hold period is to expire before the next redemption date. For example, one commenter submitted that flow-through securities purchased via private placements and other privately sourced opportunities often have four-month hold periods and would be considered illiquid assets. We were told that quality issuers are increasingly choosing to remain private and, further, that good quality flow-through investments are difficult to find. Accordingly, restricting investments that have hold periods may severely impact non-redeemable investment funds that actively participate in private placements of publicly traded issuers, such as flow-through funds. Several commenters emphasized that imposing a limit for illiquid asset investments will stifle product innovation and the availability of diverse investment products, and reduce investor choice. While a few commenters acknowledged that many existing non-redeemable investment funds adopt an illiquid asset	In formulating the Alternative Funds Proposals, the CSA will also consider whether different illiquid asset limits should apply to investment funds that are subject to NI 81-104. Finally, while several commenters suggested that mortgages be carved out of any illiquid asset restriction, the CSA note that under subsection 2.3(2)(b) of NI 81-102, non-redeemable investment funds will no longer be permitted to purchase non-guaranteed mortgages. The CSA do not think there are any policy reasons to treat guaranteed mortgages differently than other assets in respect of liquidity requirements of a non-redeemable investment fund.

	restriction, and any proposed restriction may not have a significant impact on these existing funds, a limit may nonetheless inhibit potentially valuable product development and innovation going forward. Many commenters felt that appropriate disclosure would eliminate the need for an illiquidity restriction. These commenters recommended that the CSA ensure a non-redeemable investment fund's prospectus provides comprehensive disclosure about the fund's ability to invest in illiquid assets with reference to the fund's investment objectives and strategies, as well as the associated risks of investing in illiquid assets. One commenter noted that investors in non-redeemable investment funds are already provided with sufficient disclosure about the non-redeemable investment fund's investments in illiquid assets, and the management of those risks, in the notes to the fund's financial statements, which enables an investor to evaluate a non-redeemable investment fund's liquidity risk. When considering an appropriate illiquid asset limit for non-redeemable investment funds, many commenters were of the view that any such investment restriction is interrelated with the Alternative Funds Proposals and should be considered concurrently with amendments to NI 81-104. Commenters had differing views about whether to apply different illiquidity restrictions for non-redeemable investment funds that offer annual redemptions of their securities and non-redeemable	

	investment funds that do not offer any redemptions. Some commenters were of the view that the two types of non-redeemable investment funds have different liquidity needs and, therefore, should be subject to different limits. These commenters suggested that non-redeemable investment funds that do not offer any redemptions of their securities should be permitted to invest a higher proportion of their NAV in illiquid assets. In particular, one commenter recommended that flow-through funds not be caught by the illiquid asset restrictions since their securities are not redeemable. Another commenter submitted that there is little practical difference between non-redeemable investment funds that offer annual redemptions of their securities and open-end mutual funds, in that both need to generate liquidity to satisfy redemption requests. We were urged to consider whether a difference in the frequency of redemption requests is a sufficient basis on which to apply different illiquid asset restrictions. One commenter suggested that restricting investment in illiquid assets to an amount equal to 20% of a non-redeemable investment fund's NAV would be appropriate, as it would provide non-redeemable investment funds with sufficient investment flexibility to engage in their investment strategies, while not posing significant challenges to valuation or creating substantial risk of liquidity problems. Two commenters suggested that a limit of 25% to 30% would provide this appropriate balance while another commenter believed that 50% would be a reasonable limit.	

	One commenter expressed that it would support an illiquidity limit of 25% of NAV only if the definition of “illiquid assets” were updated. This commenter also suggested that non-redeemable investment funds have the ability to seek exemptive relief in cases where an investment strategy may call for higher levels of investment in illiquid assets. A few commenters were of the view that non-redeemable investment funds should have a longer timeline for divesting illiquid assets, which are in excess of the permitted limit, than the 90 days provided to mutual funds in NI 81-102, especially in light of the fact that such funds only offer annual redemptions of their securities and have lengthy notice periods for redemptions. For example, two commenters submitted that non-redeemable investment funds should not be required to adjust their portfolios where increased market valuations are the cause of exceeding the illiquid asset restrictions. It was submitted that if a non-redeemable investment fund’s position in a private company grew to such a size that it exceeded the illiquid asset restrictions, the fund would be required to sell down the position even though the portfolio manager considered the investment to be successful and would have recommended that such investment be permitted to realize its full value or that the fund invest in other private companies as part of its investment strategy. We were told that applying a divestiture requirement under these circumstances would adversely affect	

	securityholders. Another commenter submitted that, if the illiquid asset limit was increased to a higher level, such as 25% to 30% of NAV, then the 90-day divestiture requirement applicable to mutual funds should also apply to non-redeemable investment funds. One commenter expressed concern that 90 days is an insufficient period to sell illiquid assets in a responsible manner that ensures the preservation of NAV, given that divesting a portfolio of assets such as mortgages and private real estate interests at fair market value is a time consuming process and is affected by a variety of asset-specific and macroeconomic factors. Several commenters believed that a non-redeemable investment fund holding illiquid assets would not lead to difficulty in valuing the NAV of the fund. These commenters felt that properly disclosed valuation principles together with accounting and auditing valuation methodologies for illiquid assets are sufficient to address the CSA's concerns. A few commenters submitted that non-redeemable investment funds have established procedures for valuing illiquid assets, which are typically carried out by third-party valuation agents. Further, the valuation must be conducted in a manner that is consistent with accounting standards and the detailed valuation policies and procedures disclosed to investors in the prospectus. One commenter emphasized that the accounting and	

	auditing profession has made great strides in determining appropriate valuation methodologies for illiquid assets, which are relied upon by bank and securities industry regulators around the world. Another commenter emphasized that non-redeemable investment fund managers are subject to a variety of rules in respect of calculating NAV, including National Instrument 81-107 *Independent Review Committee for Investment Funds* (NI 81-107) and, in Ontario, a statutory standard of care and fiduciary duty. Two commenters also referred to discussions at the international level regarding liquidity risk management. These commenters agreed with the view that valuation concerns are more appropriately dealt with through effective and robust valuation governance arrangements (including a fund having formal valuation policies, procedures and controls and that valuation be outsourced to third parties), rather than limitations on investing in illiquid assets.	
Investments in other investment funds (s. 2.5)	Although several commenters expected the number and frequency of fund-of-fund structures to diminish significantly as a result of recent changes to tax legislation regarding character conversion transactions, they believed that non-redeemable investment funds should continue to have the ability to invest in or obtain exposure to other investment funds to carry out their investment objectives. These commenters suggested that there will be other circumstances where this investment strategy is appropriate.	As a result of the 81-102 Amendments, non-redeemable investment funds will be subject to section 2.5 of NI 81-102, which will permit a non-redeemable investment fund to invest in other investment funds if the prescribed criteria are met.

	Many commenters submitted that a non-redeemable investment fund should not be restricted to investing in mutual funds that are subject to the investment restrictions in NI 81-102 applicable to conventional mutual funds, especially where the underlying fund has no investors other than the top fund. These commenters believed that the top and underlying funds should be required to have consistent investment restrictions and strategies, which could be achieved through a carve-out from proposed paragraph 2.5(2)(a) of NI 81-102.	Change made. We have added paragraph 2.5(2)(a.1) of NI 81-102, which states that any investment fund in which a non-redeemable investment fund invests must either be subject to NI 81-102 or must comply with the provisions of NI 81-102 applicable to a non-redeemable investment fund. The CSA are of the view that the investment restrictions and other requirements of the top and underlying fund should be consistent.
	Further, a few commenters suggested that such a carve-out from proposed paragraph 2.5(2)(a) of NI 81-102 should be subject to certain conditions. For example, we were told that the carve-out could be conditional on the underlying fund adopting investment objectives and restrictions designed to achieve, either directly or through specified derivatives, the investment objectives of the top fund. These commenters noted that the investment objectives and restrictions of the underlying fund will not always be identical to those of the top fund because the objectives or restrictions of the top fund may relate to the payment of distributions, tax issues or the use of specified derivatives to obtain exposure to the underlying fund.	See response above.
	Another commenter suggested that the carve-out be conditional on the fund-of-fund structure not leading to an increase in net fees for the investor and that the structure not be used to get around the intent of the investment restrictions of the top fund.	See response above. The Amendments also include requirements that non-redeemable investment funds that invest in other investment funds comply with paragraphs 2.5(2)(d), (e) and (f) of NI 81-102, which prohibit the duplication of fees.
	One commenter added that the securities of an	No change. We expect managers to consider, among

	underlying fund should be redeemable concurrently with its corresponding top fund.	other things, the redemption rights of the securities of the underlying fund at the time of making a purchase of those securities.
	One commenter submitted that there should be no requirement for the underlying fund to have the same investment restrictions as the top fund. This commenter noted that there are examples of non-redeemable investment funds that currently do not satisfy this requirement in respect of their fund-of-fund investments.	The CSA recognize that there are a limited number of non-redeemable investment funds that invest in foreign investment funds which may not have the same operational requirements and investment restrictions as the non-redeemable investment fund. The CSA will consider applications for exemptive relief for non-redeemable investment funds to invest in such underlying funds on a case-by-case basis.
	One commenter expressed that any carve-out from paragraph 2.5(2)(a) of NI 81-102 that would permit a non-redeemable investment fund to invest in an underlying mutual fund that is not subject to NI 81-102 should also be available to mutual funds.	No change at this time. We will continue to consider requests for exemptive relief on a case-by-case basis. However, the CSA remain concerned about an investment fund doing indirectly (i.e., through an investment in another investment fund) what NI 81-102 would not permit it to do directly. As mutual funds are currently subject to more extensive investment restrictions under NI 81-102 than non-redeemable investment funds, the CSA are of the view that additional considerations apply to a mutual fund investing in other investment funds.
	A few commenters disagreed with the proposed restriction on non-redeemable investment funds investing in other non-redeemable investment funds. One of these commenters submitted that it may be appropriate for a non-redeemable investment fund to invest in another non-redeemable investment fund when securities of the underlying fund are trading at a	At this time, we are not finalizing the restriction on non-redeemable investment funds investing in other non-redeemable investment funds. We will continue to consider any benefits of such fund-of-fund structures and whether there should be further restrictions on these investments. As indicated in the Request for Comments, the restriction on investing in non-redeemable investment funds was based on the concern

	price that is significantly less than NAV and subsequently sold when the difference between the trading price and NAV narrows. We were told this strategy will result in a greater return for the top non-redeemable investment fund. Another commenter submitted a restriction on a non-redeemable investment fund investing in another non-redeemable investment fund would prohibit non-redeemable investment funds from investing in a subsidiary if that entity were considered to be a non-redeemable investment fund. This commenter noted that this restriction would be inappropriate, as investments in subsidiaries and other investee entities are expressly contemplated by Form 41-101F2 (i.e., General Instruction 8).	that a non-redeemable investment fund could circumvent the proposed leverage limit by investing in another non-redeemable investment fund. Since we are not moving forward with several of the proposed investment restrictions on non-redeemable investment funds at this time, including limits on leverage, we will revisit any restriction on a non-redeemable investment fund investing in another non-redeemable investment fund when we consider the investment restrictions applicable to non-redeemable investment funds concurrently with the Alternative Funds Proposals.
	Some of these commenters thought that the CSA's concern, that fund-of-fund structures involving non-redeemable investment funds would indirectly permit the top fund to employ more leverage than the amount permitted in the Proposed Amendments, could be addressed by requiring the top fund's leverage to be calculated on an aggregate basis taking into account the leverage of the underlying non-redeemable investment fund.	See response above.
	One other commenter did not think that the concern with overall maximum leverage achieved through a fund-of-fund structure involving non-redeemable investment funds should be addressed through an investment restriction imposed at the top fund level, but instead left to the judgment of the portfolio	See response above.

	manager. Another commenter suggested that the restriction on non-redeemable investment funds investing in other non-redeemable investment funds be deferred and considered in conjunction with other proposed restrictions on bank borrowings and leverage, since the rationale of the proposed fund-of-fund restriction is to avoid the fund indirectly employing a greater amount of leverage than the fund is permitted to employ directly. One commenter urged us to focus on ensuring adequate disclosure rather than restricting the type of investment fund whose securities a non-redeemable investment fund may purchase. This commenter noted that continuous disclosure can be provided on a look-through basis in accordance with applicable securities law and accounting principles under IFRS. This approach would be consistent with the CSA's approach under National Policy 41-201 *Income Trusts and Other Indirect Offerings.* One commenter asked us to clarify the type of underlying funds the Proposed Amendments would restrict a non-redeemable investment fund from investing in. This commenter was of the view that the Proposed Amendments appear to only prohibit investments in funds subject to NI 81-104, which would allow a top fund to invest in other types of funds that would cause the top fund to have substantial exposure to leverage.	 See response above. As discussed above, the CSA are not proposing to restrict the type of underlying fund in which a non-redeemable fund may invest at this time. Paragraph 2.5(2)(a) has been revised so that it no longer applies to non-redeemable investment funds. Paragraph 2.5(2)(a.1), which does apply to non-redeemable investment funds, has been added. A non-redeemable investment fund may invest in another investment fund provided the investment satisfies the criteria of subsection 2.5(2) of NI 81-102. See response above.

	While one commenter agreed with the proposed restriction in 2.5(2)(c), which would restrict non-redeemable investment funds from investing in foreign investment funds, another commenter felt that it is not appropriate to limit investments in underlying funds to the domestic market.	The CSA recognize that there are a limited number of non-redeemable investment funds that invest in foreign investment funds which are not reporting issuers in Canada. The CSA will consider exemptive relief to permit non-redeemable investment funds to invest in such underlying funds on a case-by-case basis.
	This commenter submitted that some non-redeemable investment funds have global investment strategies and may need to invest in foreign investment funds to achieve their investment objectives. This commenter further suggested that investments in foreign investment funds not be restricted to mutual funds. Since non-redeemable investment funds do not require significant levels of liquidity to fund regular redemptions, a portion of the investment portfolio being invested in other non-redeemable investment funds is not a significant risk.	See responses above.
	All of the comments we received in response to the CSA's question about the proposed requirement for an underlying fund to be a reporting issuer in all of the jurisdictions in which the top non-redeemable investment fund is a reporting issuer expressed that this requirement would not enhance investor protection, and would only pass on unnecessary and ongoing costs to investors.	Change made. We have removed the requirement that a non-redeemable investment fund and the underlying fund in which it invests be reporting issuers in the same jurisdictions. Instead, we have added paragraph 2.5(2)(c.1) of NI 81-102, which requires that the underlying fund be a reporting issuer in at least one jurisdiction in which the non-redeemable investment fund is a reporting issuer.
	One commenter urged us to further investigate the reasons behind any requirement for underlying funds to become reporting issuers in every jurisdiction. This commenter questioned whether the current requirements create opportunities for regulatory or cost	See response above.

	arbitrage, and suggested that new requirements may only be warranted if the current structure allows issuers to avoid providing investor protections in some jurisdictions and not others.	
	Many commenters believed that the current requirements are sufficient in addressing the CSA's objectives. These commenters noted that underlying funds currently only file a non-offering prospectus in Quebec (because of the AMF's policy position that providing exposure to an underlying fund would constitute an indirect offering in Canada) and occasionally in Ontario (to benefit from the limited liability provisions under the *Trust Beneficiaries Liability Act, 2004* (Ontario)). We were told that requiring an underlying fund to become a reporting issuer in at least one jurisdiction would meet the CSA's policy objectives because it will subject the underlying fund to National Instrument 81-106 *Investment Fund Continuous Disclosure* (NI 81-106) and continuous disclosure relating to the underlying fund would be made publicly available to investors on SEDAR. It was also suggested that requiring the fund to become a reporting issuer in all jurisdictions would be inconsistent with the CSA's principal regulator concept.	See response above. The CSA do not expect that the new requirement in paragraph 2.5(2)(c.1) of NI 81-102 will have an impact on current industry practices. Accordingly, investment funds should continue to consider whether any indirect offering issues arise which may require the underlying fund to file a prospectus in more than one jurisdiction.
	One commenter added that it would not be necessary for an underlying fund to become a reporting issuer in all jurisdictions, provided that the underlying fund does not offer securities in a jurisdiction in which the top fund is not a reporting issuer.	See response above. Although paragraph 2.5(2)(c.1) of NI 81-102 requires the underlying fund to be a reporting issuer in only one local jurisdiction, that jurisdiction must be one in which the top fund is a reporting issuer.

	Another commenter added that many underlying funds are single purpose funds which are not directly available for purchase by investors, and full disclosure about the underlying fund is usually made in the prospectus of the top fund. This commenter suggested that the disclosure provided in the top fund prospectus, combined with the ongoing continuous disclosure provided by the underlying fund as a reporting issuer in one jurisdiction would provide sufficient information and protection for investors.	See response above.
	A few commenters questioned the need for an underlying fund to become a reporting issuer in the first place. We were told that this is unnecessary if the top fund undertakes to include look-through disclosure of the detailed holdings of the underlying fund in its prospectus and continuous disclosure. One commenter expressed that the current requirement for an underlying fund to file a prospectus in Quebec and/or Ontario to become a reporting issuer is too rigid and does not provide investors with enhanced disclosure, but instead imposes additional costs and burdens. This commenter believed that the requirement to file a prospectus for an underlying fund should be examined on a case-by-case basis in light of the substantive elements and economics of the fund-of-fund structure.	No change. The CSA believe that requiring the underlying fund to be a reporting issuer in at least one Canadian jurisdiction ensures that the underlying fund is subject to the CSA's continuous disclosure regime in NI 81-106 and permits securityholders to readily access information about the underlying fund. The CSA also appreciate the opportunity to review the underlying fund's prospectus in order to fully review each specific fund-of-fund structure proposed to be offered to the public.
	Another commenter questioned the need for an underlying fund to become a reporting issuer given the CSA's broad public interest powers to intervene in activities related to the Canadian capital markets. This	See response above.

	commenter noted that the CSA's broad jurisdiction does not depend on reporting issuer status and in most cases an underlying fund would have a sufficient nexus to a CSA jurisdiction.	
	Several commenters also submitted that there should not be a requirement for the prospectus of an underlying fund to be delivered to securityholders of the top fund. These commenters questioned the utility of such a requirement, given that the top fund's prospectus is required to provide full, true and plain disclosure in respect of the securities acquired by investors. It was also emphasized that the delivery of the prospectus of the underlying fund would impose additional cost without adding any legitimate benefit.	The CSA are not adding any requirements to NI 81-102 that would require a non-redeemable investment fund to deliver the prospectus of any underlying fund in which it invests to its securityholders.
	One commenter asked us to consider whether a carve-out from the concentration and control investment restrictions is required to permit a non-redeemable investment fund to use fund-of-fund structures. This commenter also requested that we clarify in 81-102CP that such a carve-out would be available in the case of compliance with the requirements of section 2.5, and any exemptions therefrom if the terms of the exemption are complied with.	At this time, the issuer concentration restriction does not apply to non-redeemable investments funds. Please see paragraph 2.2(1.1)(a) of NI 81-102, which states that the control restriction in section 2.2 does not apply to the purchase of a security of an investment fund, if the purchase is made in accordance with section 2.5 of NI 81-102. We are not making further changes at this time.
	One commenter urged us to undertake a study of the fees charged in fund-of-fund structures in order to determine whether they provide substantial benefits to investors in performance or risk and the extent of the detriment to investors in terms of increased fees. Absent this research, this commenter believed there is no compelling reason to permit a non-redeemable	No change at this time. The CSA believe that fund-of-fund structures should be permitted subject to the conditions in section 2.5 of NI 81-102. Section 2.5 continues to prohibit duplication of fees in fund-of-fund structures.

	investment fund to invest in other investment funds.	
Securities lending, repurchases and reverse repurchases (ss. 2.12 to 2.14)	Commenters differed on the extent to which the securities lending, repurchase and reverse repurchase provisions of NI 81-102 should apply to non-redeemable investment funds. One commenter supported extending the securities lending, repurchase and reverse repurchase provisions of Part 2 of NI 81-102 to non-redeemable investment funds. On the other hand, a few commenters did not agree that there should be limits on securities lending, repurchase and reverse repurchase activities by non-redeemable investment funds, but stated that they would support certain additional disclosure requirements. These commenters felt that securities lending or repurchases can be a valuable source of income for investors in a non-redeemable investment fund and were concerned that these activities would be unduly limited based on assumptions regarding a prudent investment standard. A few of these commenters felt that the focus of regulation in this sphere should be on the quality of collateral and on ensuring that there is full disclosure. These commenters also questioned how restricting the percentage of an investment fund's assets that may be loaned protects (or mitigates risk to) the investment fund.	No change. The CSA consider the framework for securities lending, repurchases and reverse repurchases contained in NI 81-102 to represent prudent practices, which are also in line with international proposals and discussions regarding guidelines for these types of activities by investment funds. In addition to the application of sections 2.12 to 2.17 of NI 81-102 to non-redeemable investment funds, the CSA are also amending NI 81-106, Form 41-101F2, Form 81-101F1 and Form 81-101F2 to mandate additional disclosure regarding an investment fund's securities lending activities. See Part III of this Annex B. NI 81-102 currently includes requirements with respect to the type and amount of collateral to be delivered to an investment fund with respect to securities lending and repurchases, and also restricts what an investment fund may do with that collateral. NI 81-102 also restricts the percentage of an investment fund's assets that may be loaned to mitigate the potential risk of loss to the investment fund. As a result of the 81-102 Amendments, these requirements will also apply to non-redeemable investment funds.

	According to one of these commenters, using repurchases to create leverage should not be impeded in favour of the requirements that apply to conventional mutual fund management, to the extent that this would increase costs or reduce incremental returns for no material net investor benefit. One commenter was of the view that there should be significant financial benefit to a non-redeemable investment fund from securities lending; otherwise, it should not be permitted.	No change made. As stated above, the CSA consider the securities lending, repurchase and reverse repurchase requirements of NI 81-102 to represent prudent practices which should apply to all publicly offered investment funds. We do not think that non-redeemable investment funds should be treated differently than mutual funds in respect of these types of activities. No change made. The CSA do not generally take issue with a non-redeemable investment fund engaging in securities lending provided it is done in compliance with the requirements of NI 81-102 and with appropriate disclosure to securityholders.
Organizational costs (s. 3.3(3))	Most commenters disagreed with the CSA's proposal to restrict a non-redeemable investment fund from paying the costs of its incorporation, formation or initial organization (the organizational costs). Many commenters told us that the organizational costs of a non-redeemable investment fund are largely imposed by regulation and, to that extent, are not discretionary. These commenters noted that the costs involved in bringing a non-redeemable investment fund to market are much higher than those associated with launching a mutual fund, and include preparing, filing, translating and printing a preliminary and final long form prospectus, the involvement of investment dealers, two sets of legal counsel, an auditor, external due diligence processes and a more extensive regulatory approval process including obtaining TSX	After reviewing the extensive comments received, we have decided not to proceed with the Organizational Cost Proposals at this time. However, the CSA remain concerned about the different treatment of mutual funds and non-redeemable investment funds with respect to the payment of organizational costs, particularly as this different treatment permits a manager to circumvent the restriction on a mutual fund paying its organizational costs by launching an investment fund in the form of a non-redeemable investment fund, and then converting the fund into a mutual fund after a short period of time. While several commenters suggested that the CSA focus on disclosure to ensure that the costs of

	listing. As a result of the non-discretionary nature of many of the organizational costs, some commenters conveyed that organizational costs are either fixed or relatively fixed and would be unlikely to change substantially in the event that they were paid by the manager instead of the non-redeemable investment fund. One such commenter added that managers already aim to minimize the organizational costs that are borne by their non-redeemable investment funds because the investment funds industry is highly competitive and managers who are unable to do so are at a competitive disadvantage. Many commenters focused on the “investor protection” elements of the activities that comprise a non-redeemable investment fund’s organizational costs, such as the involvement of the investment dealers in conducting a thorough due diligence review and the extensive regulatory approval process. A few of these commenters told us that, while the organizational costs of a mutual fund are lower than for a non-redeemable investment fund, mutual funds do not provide investors with the benefit of due diligence conducted by independent investment dealers. Further, we were told that the costs of certain activities, such as meeting with advisors to explain the non-redeemable investment fund, provide investor benefit by increasing the size of a fund (which reduces the fund’s MER and increases trading liquidity for the fund). Accordingly, these commenters suggested that it	establishing a non-redeemable investment fund, as well as the entity who bears those costs, are clearly disclosed, the CSA are of the view that disclosure may not be adequate to deal with the potential for regulatory arbitrage created by the different treatment of non-redeemable investment funds and mutual funds with respect to the payment of their organizational costs. The CSA will continue to consider how to best address the potential for regulatory arbitrage. We may publish for comment, concurrently with the Alternative Funds Proposals, proposed amendments to NI 81-102 which would require the manager of a non-redeemable investment fund to reimburse the fund for its organizational costs if the non-redeemable investment fund converts to a mutual fund within a specified period of time after its initial public offering. In order to address the potential for regulatory arbitrage in the meantime, the CSA are moving forward with introducing subsection 5.1(2) of NI 81-102, which restricts an investment fund from bearing any of the costs or expenses associated with, among other things, a conversion from a non-redeemable investment to a mutual fund. Furthermore, although it was suggested by one commenter that the CSA codify a carve-out from the restriction on a mutual fund bearing its own organization costs for the first prospectus of a mutual fund in connection with the conversion of a non-redeemable investment fund, the CSA are not introducing such a carve-out.

	is reasonable for the related organizational costs to be indirectly borne by investors through payment out of the offering proceeds. A few commenters suggested that the primary reason behind the prohibition on a mutual fund bearing its own organizational costs is that the mutual fund's start-up costs can be a substantial proportion of the mutual fund's initial NAV. Non-redeemable investment funds do not have this problem, as the minimum sizes of their public offerings are sufficiently large to bear the organizational costs. Similarly, other commenters told us that the rationale for the prohibition on mutual funds paying organizational costs is that investors invest in mutual funds over time and, therefore, it would be inequitable for the first investors in a mutual fund to effectively pay for the organizational costs of the mutual fund. Since non-redeemable investment funds are distributed in one offering, these commenters suggested that investors are on an equal footing and no particular group is prejudiced by a non-redeemable investment fund paying the organizational costs from its offering proceeds. Some commenters noted that requiring the manager to bear the organizational costs constitutes a significant departure from the position adopted in the past on offering expenses on the launch of exchange-traded mutual funds that are not in continuous distribution, a position that was determined based on the rationale noted above.	

	A few commenters noted that mutual fund managers recoup their much lower organizational costs over time through the continuous distribution process. Non-redeemable investment fund managers, however, have limited opportunity to grow their investor base over time. Many commenters conveyed that shifting organizational costs to the manager will cause these costs to be borne by the non-redeemable investment fund in other ways, which will not result in cost savings for investors, but may instead result in an increase to the aggregate costs borne by investors. For example, many commenters were of the view that managers would begin charging higher management fees to recoup the organizational costs, which fees will likely never be reduced once the organizational costs have been recouped. These commenters felt that, over time, an investor will almost certainly pay more through increased management fees than under the current model where the organizational costs payable by a non-redeemable investment fund are capped at 1.5% of the gross proceeds of the offering. As evidence of this, some of these commenters noted that management fees of a mutual fund are generally higher than for a non-redeemable investment fund, which means that non-redeemable investment fund investors are compensated for the upfront absorption of the organizational costs.	

	A few commenters took the position that another consequence of the Organizational Cost Proposals is that, as a manager will seek financing to cover the organizational costs, the costs associated with this financing will also be recouped through a higher management fee. Some of these commenters noted that the manager may also charge a form of risk premium to ensure that the manager would receive, over time, at least the organizational costs expended. Certain commenters were also of the view that the Organizational Cost Proposals may result in the introduction of redemption fees to ensure recovery of organizational costs or that redemption rights may be delayed or reduced in order for the manager to ensure that assets are retained long enough to earn back the capital the manager invested in launching the non-redeemable investment fund. A few of these commenters noted that redemption fees create misleading NAVs, since the investor will have to pay a fee to redeem out at NAV and the market price will be reduced to reflect this additional fee. Many commenters were of the view that shifting organizational costs to the manager will not create incentives to reduce these costs, as the interest of managers with respect to organizational costs is already aligned with those of investors. In particular, managers of non-redeemable investment funds already seek to minimize organizational costs, as they are responsible for these costs in the event that the non-redeemable investment fund's offering is not successful.	

	In addition, many commenters told us that, for the last several years, market practice has required that organizational costs borne by a non-redeemable investment fund be capped at 1.5% of the gross proceeds of the fund's offering size. As a result, managers are also responsible for the organizational costs that exceed this cap and are already incentivised to seek cost efficiencies to minimize organizational costs beyond this cap. A few commenters noted that industry practice is to have a non-redeemable investment fund raise a minimum amount of money (generally $20 million) before proceeding with its offering. In this way, organizational costs do not make up a large proportion of a non-redeemable investment fund's initial NAV. A few commenters also told us that organizational costs of non-redeemable investment funds have decreased significantly over time. According to these commenters, many material agreements and much of the required prospectus disclosure have become standardized and, while costs will necessarily be higher for novel and complex products that require additional structuring and diligence, many significant aspects of these offerings require less legal involvement than previously. Many commenters were of the view that the Organizational Cost Proposals would act as a barrier to entry, having a material detrimental impact on competition and stifling new entrants to the market and	

	reducing the incentive to launch new funds. According to these commenters, the Organizational Cost Proposals would favour managers with significant capital resources and would therefore contribute to a non-redeemable investment fund market dominated by a few very large players, which these commenters did not believe to be in the best interests of Canadian retail investors or capital markets generally. We were told this would result in a reduction of diverse and innovative products in the marketplace and it would be unlikely that investors would have an alternative means to access these strategies. A few commenters submitted that the effect of the Organizational Cost Proposals is that the securities regulators may end up regulating the quantum of fees and prices, something that they have not historically done. On this point, certain commenters were of the view that the market should continue to determine the allocation of organizational costs and that regulators should focus on disclosure (such as ensuring disclosure is provided on management compensation, the costs of establishing the fund and who bears the costs), rather than regulating the commercial practice of how to charge fees. A few commenters noted that the long form prospectus for a non-redeemable investment fund prominently discloses that the organizational costs of the non-redeemable investment fund are paid by the fund.	

	These fees, along with the ongoing fees of the fund, can be scrutinized and compared by investment dealers and their clients prior to any investment decision being made. According to these commenters, the organizational costs are part of the initial bargain made between the investors and the issuer. Further, some commenters told us that the payment of organizational costs by a non-redeemable investment fund reflects investor expectations and is reflected in each non-redeemable investment fund's opening NAV. One commenter noted that the largest part of the start-up costs of a non-redeemable investment fund are the agents' fees, which are not caught by the proposed subsection 3.3(3) of NI 81-102. Many commenters focused on the CSA's objective of addressing the regulatory arbitrage created by launching an investment fund structured as a non-redeemable investment fund and then converting it into a mutual fund a short time after completion of the initial public offering. Many of these commenters were of the view that regulatory arbitrage can be addressed by requiring investment fund managers to refund the organizational costs borne by a non-redeemable investment fund if it converts within a prescribed period following the closing of its initial public offering or if the intention to convert is not disclosed in the fund's initial prospectus. In the alternative, these commenters suggested that the CSA consider prohibiting non-redeemable investment	

	funds from converting to mutual funds altogether. One commenter suggested that managers be required to bear the portion of the organizational costs for a converting non-redeemable investment fund that would approximate the costs of launching the fund as a mutual fund. Certain commenters felt that there is no need to level the playing field between mutual funds and non-redeemable investment funds, as a mutual fund manager is free to launch non-redeemable investment funds, and several have done so. A few commenters noted that the costs and risk of a failed launch for a non-redeemable investment fund are far greater than for a mutual fund, eliminating any benefit to preferring the non-redeemable investment fund space to the mutual fund one. Another commenter suggested that the CSA codify a carve-out from the restriction on a mutual fund bearing its own organizational costs for the first prospectus of a mutual fund filed in connection with the conversion of a non-redeemable investment fund. One commenter was of the view that there should be no difference between similar issuers that are not investment funds, such as real estate investment trusts or MIEs, who bear their own organizational costs, and non-redeemable investment funds. A few commenters supported some sort of restriction on a non-redeemable investment fund bearing all of its	

	organizational costs. One commenter did support the Organizational Cost Proposals and was of the view that these proposals would achieve the benefits cited in the Request for Comments. This commenter also noted that, for mutual funds, managers currently pay the organizational costs and recoup such costs through ongoing management fees. According to this commenter, investors should not pay the organizational costs when they pay ongoing management fees for non-redeemable investment funds. This commenter felt that the Organizational Cost Proposals would also prevent managers launching non-redeemable investment funds that convert to mutual funds within a short period of time after the launch. One commenter told us that investors purchase investment fund securities with the expectation that they will profit from the investment and it is only fair that they should bear a portion of the organizational costs of such fund. However, this commenter also suggested that discretionary costs associated with the launch or maintenance of a fund should be borne by the manager. Similarly, one commenter noted that the different capital raising model followed by non-redeemable investment funds could support the agent's fee being paid by the fund and other flat fees being borne by the manager. One commenter conveyed that, if the CSA intend to	

	regulate organizational costs, it would support a codification of the market practice that caps the amount of organizational costs payable by the non-redeemable investment fund at 1.5% of the gross proceeds of the offering.	
Conflicts of interest provisions (Part 4)	The majority of commenters agreed with the Proposed Amendments to extend the application of the conflicts of interest provisions in Part 4 of NI 81-102 to non-redeemable investment funds. Some commenters further suggested that the provisions in NI 81-102 should be harmonized with the conflicts of interest provisions in National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* (NI 31-103), NI 81-107 and the applicable securities legislation of the provinces and territories of Canada. One commenter agreed with applying conflicts of interest rules to non-redeemable investment funds, but disagreed with the exemptions provided where approval is given by the independent review committee of a fund. This commenter urged us to reconsider the independent review committee model for dealing with conflicts of interest of investment funds.	We thank commenters for their feedback. The CSA do not propose to amend any of the conflicts of interest requirements in NI 31-103 or NI 81-107 at this time. We will consider harmonizing the conflicts of interest provisions in the various instruments in the context of future amendments to NI 81-107. The review of the independent review committee model under NI 81-107 is not within the scope of the Modernization Project.
Securityholder and regulatory approval requirements (ss. 5.1 to 5.6)	Many commenters agreed with the proposed securityholder and regulatory approval requirements for fundamental changes to non-redeemable investment funds and their management, including new securityholder requirements in connection with conversions and mergers of non-redeemable	We thank commenters for their feedback.

	investment funds.	
	A few of these commenters, however, submitted that while they agreed with the new securityholder approval requirement for changes to the nature of a non-redeemable investment fund, they disagreed with the proposed requirement that managers pay for the expenses associated with implementing that change. These commenters did not agree with the assumption that conversions and mergers are for the benefit of the manager. It was submitted that such changes are sometimes made as a result of regulatory changes or are proposed by the manager and viewed by the independent review committee of the fund as beneficial to securityholders.	No change. The CSA believe that the restriction on an investment fund bearing the costs of changing the nature of the fund is consistent with the requirements for fundamental changes to investment funds by way of merger or reorganization. Since restructuring an investment fund offers managers the benefit of retaining fund assets under management, whether the restructuring is done through a merger or conversion, the CSA continue to be of the view that the costs of these transactions should not be borne by the investment fund. Given that the CSA are not moving forward with the proposals to restrict a non-redeemable investment fund from paying its organizational costs, the CSA think that a manager paying for the conversion of a fund from a non-redeemable investment fund into a mutual fund will discourage any potential arbitrage opportunities where managers may launch mutual funds without paying the organizational costs (i.e., by creating a non-redeemable investment fund and then converting it into a mutual fund after a short period of time).
	Two commenters further emphasized that changes to the investment objectives, nature or structure of a non-redeemable investment fund are often necessary over the life of a fund due to regulatory, tax or market conditions, and are only proposed and approved on the basis that they benefit securityholders. These commenters submitted that the net benefits provided to securityholders justify the fund bearing the costs of	Under the Amendments, only the costs related to a change contemplated by paragraph 5.1(1)(h) of NI 81-102 may not be borne by the investment fund. See response above.

	these changes. One commenter suggested that costs for fundamental changes be permitted to be borne by the fund if independent review committee approval is obtained. Alternatively, this commenter suggested that the CSA provide a list of changes that would not be deemed to be for the benefit of securityholders.	
	One commenter suggested that changes to the nature of an investment fund are so fundamental that approval of two-thirds of securityholders should be required for such a change. This commenter also expressed support for the proposed requirement that funds not bear the costs for these changes.	The CSA have not made any changes to the securityholder approval requirements in section 5.2 of NI 81-102 in connection with a change to the nature of an investment fund. We think the requirement for securityholder approval, and the restriction on an investment fund bearing the costs, of such a change adequately address the CSA's concerns.
	A few commenters expressed support for the codified exemptions from the proposed securityholder approval requirements for certain transactions, including (i) conversions of non-redeemable investment funds that are structured from inception to convert to a mutual fund upon the occurrence of a specified event, (ii) mergers involving specialized non-redeemable investment funds that have a limited life and that do not list or trade their securities on a secondary market (commonly referred to as flow-through funds), and (iii) mergers of non-redeemable investment funds with other funds where investors can redeem their securities of the fund at NAV prior to the merger. One commenter suggested that the limited exemption from the securityholder approval requirement for a non-redeemable investment fund that is structured from inception to convert to a mutual fund, provided that the	After considering the comments received, the CSA have decided not to move forward with adding an exemption from the securityholder approval requirements for conversions of non-redeemable investment funds that are structured from inception to convert to a mutual fund upon the occurrence of a specified event. As discussed above, the CSA are not moving forward with the proposals to restrict a non-redeemable investment fund from paying its organizational costs. Accordingly, the CSA think the requirement to obtain securityholder approval prior to a conversion from a non-redeemable investment fund to a mutual fund will mitigate the potential arbitrage of launching an investment fund in the form of a non-redeemable investment fund and then converting it to a mutual fund shortly after launch, and will help ensure that the

	conversion is disclosed, be broadened to include other fundamental changes to a non-redeemable investment fund where the change is disclosed in the fund's offering documents. For example, this commenter suggested that the exemption may include changes to the method of investing, leverage or other investment restrictions when certain targets, events or dates are met.	decision to convert will be in the best interests of securityholders, who will also have the opportunity to make an informed decision about the conversion. In addition, the CSA consider a change to the nature of an investment fund to be a fundamental change that requires securityholder approval. The CSA are generally of the view that the investor benefit provided by the securityholder approval requirements in section 5.1 of NI 81-102 cannot be replaced with disclosure in the prospectus.
	One commenter, in addition to expressing support for the exemption from the securityholder and regulatory approval requirement for mergers involving flow-through funds, asked us to expressly state that these transactions are exempt from the prohibition on inter-fund trades in paragraph 13.5(2)(b) of NI 31-103. This commenter noted that this would be consistent with market and administrative practice.	No change made. See subsection 5.9(2) of NI 81-102, which, among other things, exempts transactions described in section 5.6 of NI 81-102 from the investment fund conflict of interest investment restrictions (as defined in NI 81-102).
	Another commenter disagreed with the exemption from regulatory approval for mergers involving flow-through funds and felt that such transactions could benefit from the review of regulatory authorities. This commenter suggested, however, that if any exemption from regulatory approval is provided for mergers involving flow-through funds, or if any exemption from securityholder approval is provided for non-redeemable investment funds that are structured from inception to convert to mutual funds upon a specified event, such an exemption should be conditional on prominent plain language disclosure in the prospectus	We have not made any changes with respect to the exemption from regulatory approval for mergers involving flow-through funds. The CSA expect the disclosure provided in connection with subparagraph 5.3(2)(b)(v) to be presented in an easy-to-read format and comply with plain language principles, as required by Form 41-101F2. See also the response above. We have removed the exemption from securityholder approval for non-redeemable investment funds that are structured from inception to convert to mutual funds upon a specified event.

	and any sales communication materials of the applicable investment fund. A few commenters expressed support for the CSA's proposal to redraft the requirement to obtain regulatory approval for a change in control of the manager.	 Acknowledged.
Termination of non-redeemable investment funds (s. 5.8.1)	Two commenters agreed with the proposed requirement that a non-redeemable investment fund terminate no earlier than 15 days and no later than 30 days after filing a press release to disclose the intended termination. Several other commenters, however, were concerned that the 30-day limit for a non-redeemable investment fund to terminate upon issuing a news release may not be a sufficient period of time to wind up the affairs of the fund in an orderly manner and may result in unnecessary loss of investor assets. One commenter noted that the time required to wind up a non-redeemable investment fund is often beyond the control of the manager and will depend on such factors as the nature of the portfolio, the manager's ability to maximize securityholder value and the provision for the liabilities of the fund, which are also all dependent on prevailing market conditions. Another commenter added that the 30-day time limit is operationally problematic because winding up a fund requires various regulatory, listing and other service providers to complete a number of tasks in a set order. This commenter submitted that it may not be possible	After considering the comments received, we have decided to extend the time period for which a non-redeemable investment fund may terminate after filing a press release disclosing the intended termination. See revised subsection 5.8.1(2) of NI 81-102, which requires that a non-redeemable investment fund terminate no earlier than 15 days and no later than 90 days after the filing of the news release. The CSA continue to be of the view that this requirement ensures that securityholders of a non-redeemable investment fund have sufficient time to consider the consequences of the termination of the non-redeemable investment fund and, at the same time, ensures that the assets of the terminating fund are distributed to securityholders in a timely manner.

	to meet this timing. One commenter also submitted that it is particularly difficult to terminate a fund if the fund holds illiquid assets because those assets are more difficult to dispose of. This commenter suggested that the CSA consider allowing a manager to hold illiquid assets in trust on the wind-up of a fund as a principled and practical solution for disposing of assets with nominal value. We were told that this provision would also require a carve-out from the self-dealing provisions. One commenter recommended a limit of 90 days to terminate a non-redeemable investment fund, which would allow sufficient time for a non-redeemable investment fund to liquidate its portfolio in an orderly manner and to wind up its affairs. Another commenter suggested that it would be appropriate to permit the manager of a non-redeemable investment fund to set the final termination date, which would allow the manager to consider matters including the orderly liquidation of the portfolio, the termination of contractual consents and any external approvals that may be required.	
Custodianship of portfolio assets (Part 6)	The majority of commenters agreed with the Proposed Amendments to update the custodian requirements in NI 81-102 and apply the updated NI 81-102 requirements to all non-redeemable investment funds that are reporting issuers (the Custodial Amendments), and not only those that file a prospectus under National Instrument 41-101 *General Prospectus Requirements*	We thank commenters for their feedback.

	(NI 41-101).	
	One commenter questioned the CSA's view that the Custodial Amendments would not result in substantive changes to the custodian requirements for any investment funds, given that the requirements will apply to all investment funds, and not only those that file a prospectus under NI 41-101. This commenter submitted that pooled funds are not subject to NI 41-101 or NI 81-102 and would not be aware of the Custodial Amendments. It was recommended that, if we intend to require all non-redeemable investment funds to comply with the custodian requirements, we publish a separate notice specifically for the hedge fund industry.	The Amendments in respect of Part 6 of NI 81-102 do not apply to non-redeemable investment funds that are not reporting issuers. Prior to the Amendments coming into force, the custodianship requirements for non-redeemable investment funds are provided in Part 14 of NI 41-101. As a result, non-redeemable investment funds that filed a prospectus before NI 41-101 came into force are not subject to those requirements. In the Request for Comments, the CSA conveyed that the consequence of moving the custodianship requirements for non-redeemable investment funds from NI 41-101 to NI 81-102 is that the custodianship requirements will now apply to all non-redeemable investment funds that are reporting issuers, regardless of whether they became a reporting issuer prior to NI 41-101 coming into force.
	One commenter expressed that a consequence of the Custodial Amendments will be that MIEs in Alberta, which qualify as non-redeemable investment funds, would not be able to hold their mortgage investments directly, but will have to use a custodian. This commenter noted that Alberta and some other jurisdictions have a government-operated land titles registry, which means that the government has custody of all original titles, documents and plans and has legal responsibility for the validity and security of all registered land title information. We were told that a custodian in such circumstances would only add costs without any additional benefits, since the government operated land titles registry already secures the MIE	As a result of paragraph 2.3(2)(b) of NI 81-102**,** non-redeemable investment funds that are reporting issuers will no longer be permitted to purchase non-guaranteed mortgages. We encourage issuers to consult with staff of the local jurisdiction should any questions arise in respect of compliance with these requirements**.**

	and the MIE's investors. As a result, this commenter recommended that an exception from the custodian rules be provided for mortgages held in government land titles systems.	
Issue price of securities (ss. 9.3(2) and (3))	Many commenters expressed support for the proposed requirements that non-redeemable investment funds not issue securities at a price that would be dilutive to the NAV of the fund. Two commenters, however, expressed concern that subsection 9.3(2) as drafted, would introduce uncertainty in the pricing of a new issue offering of a non-redeemable investment fund. These commenters suggested that we amend the rule to permit the price of the offering to be fixed based on the most recent determined NAV prior to the pricing of the offering.	We thank commenters for their feedback. Change made. We recognize that compliance with proposed subsections 9.3(2) and (3) of NI 81-102 may not have been practicable in certain offerings of non-redeemable investment funds. In particular, for some new offerings, such as private placement offerings or offerings made under a PREP prospectus, the pricing date may be different than "one business day before the date of the prospectus." Accordingly, we have replaced proposed subsections 9.3(2) and (3) with subsection 9.3(2) of NI 81-102, which requires that the issue price of a security of a non-redeemable investment fund not be, as far as reasonably practical, a price that causes dilution of the NAV of other outstanding securities of the investment fund at the time the security is issued, or, a price that is less than the most recent NAV per security calculated prior to the pricing of the offering. See also section 10.6 of 81-102CP, which provides guidance on how the CSA will interpret subsection 9.3(2) and sets out practices regarding the pricing of non-redeemable investment fund securities that the CSA do not consider to be dilutive to existing securityholders.

	Another commenter asked us to consider also implementing a rule that would require a non-redeemable investment fund issuing new securities to its manager as payment of management fees to disclose the price of those new securities. This commenter noted that the disclosure would be particularly helpful in the case of funds holding illiquid assets.	Given subsection 9.3(2) of NI 81-102, the CSA expect that any issuances of new securities to the non-redeemable investment fund's manager as payment of management fees be issued at a price that is not less than the NAV per security on the date of issuance. See section 10.6 of 81-102CP. At this time, the CSA are not introducing disclosure requirements with respect to this issue.
Warrant offerings (Part 9.1)	A few commenters agreed with the prohibition on warrant offerings for the policy reasons cited by the CSA in the Request for Comments. However, many commenters were of the view that a blanket prohibition on warrant offerings would be unduly prohibitive and would remove one of the least costly methods of raising additional capital for non-redeemable investment funds. Several commenters submitted that the assets of a non-redeemable investment fund typically deplete over time as a result of the annual redemption feature and any purchases under a normal course issuer bid. These commenters suggested that, unless a non-redeemable investment fund replenishes its assets and increases the number of outstanding securities, securityholders will be negatively impacted by increases to the fund's MER and decreases to the fund's trading liquidity. It was emphasized that maintaining or lowering the fund's MER preserves or increases the fund's NAV, which ultimately influences the fund's yield and trading price on the exchange.	We thank commenters for their feedback. No change. While the CSA recognize that warrant offerings may offer certain benefits to an investment fund, we continue to think the potential dilution faced by existing securityholders often outweigh any potential benefit. In order to ensure that existing securityholders of a non-redeemable investment fund are not coerced into investing additional capital into the investment fund or paying additional fees to raise additional capital for the fund, the CSA continue to be of the view that investment funds should be restricted from issuing warrants or rights, or from entering into a position in a specified derivative the underlying interest of which is a security of the investment fund. In limited and exceptional circumstances, if a non-redeemable investment fund can demonstrate market necessity and where steps are taken to mitigate any potential dilution and conflicts of interest for the non-redeemable investment fund so that the benefits of the warrant offering outweigh any costs of dilution, the

	In addition to lowering the MER and increasing the trading liquidity of a non-redeemable investment fund, several commenters submitted that warrant offerings offer benefits such as providing a non-redeemable investment fund with additional capital that can be used to take advantage of attractive investment opportunities and increasing diversification and investment options for a fund's portfolio.	CSA may consider applications for exemptive relief.
	We were told that filing a prospectus to issue new units or shares is not always an appropriate substitute for warrant offerings to raise additional capital for a non-redeemable investment fund. These commenters submitted that issuing new units or shares is often not viable because a non-redeemable investment fund's securities would have to trade at a price that is at least 4.5% to 6% higher than their NAV in order to incentivise investors to purchase securities from the new offering and to justify the costs of the offering. Since most non-redeemable investment funds trade at a price that is less than their NAV, there are relatively few funds that can effectively raise money under such circumstances. Further, we were told that the offering expenses of new share or unit issues typically exceed 4% of the issue price, whereas the costs related to warrant offerings, including the preparation of the prospectus, are generally lower.	See response above.
	Some commenters thought that concerns about dilution are lessened if warrants have exercise prices that would not be dilutive to the NAV of the non-redeemable investment fund at the time the exercise price is determined. Further, it was submitted that warrant	While the CSA recognize that warrants with short term exercise periods raise fewer concerns in respect of dilution, the CSA are not satisfied that the risks of dilution to existing securityholders are sufficiently mitigated. As discussed above, the CSA may consider

	offerings would only cause minor dilution if the exercise period is short. One commenter suggested, therefore, that only long-dated warrants be prohibited. One commenter, while noting that industry practice has moved away from the use of warrant offerings to raise capital for a non-redeemable investment fund, agreed with other commenters that there may be certain circumstances where the benefits of a warrant offering would outweigh the costs of moderate dilution to the fund. A few commenters were of the view that a prohibition on warrant offerings ignores the fundamental aspects of non-redeemable investment funds that distinguish them from mutual funds. Since securityholders of non-redeemable investment funds generally obtain liquidity by trading the fund's securities on an exchange, these commenters suggested that NAV dilution is less relevant for a non-redeemable investment fund than it is for a mutual fund. These commenters emphasized that the key benchmark by which investors measure the value of a non-redeemable investment fund is the market price of the fund's securities, which is affected by factors other than NAV, such as yield, liquidity, fees, performance, and term to maturity. As a result, it was submitted that warrant offerings must be evaluated for their positive effects on the trading price of a non-redeemable investment fund's securities in addition to any dilutive effects on NAV.	exemptive relief in exceptional circumstances. See response above. While the CSA recognize that factors in addition to NAV are significant for investors of non-redeemable investment funds, the CSA continue to have concerns about the potential dilution to NAV resulting from warrant offerings. It appears to the CSA that NAV is a significant consideration for investors when measuring the value of a non-redeemable investment fund. The CSA note, for example, that the majority of non-redeemable investment funds are structured with an annual redemption feature to permit redemptions of their securities at NAV, which supports the trading price of the fund's securities such that the securities trade at a price that is close to NAV.

	A few commenters also submitted that securities of a non-redeemable investment fund are more analogous to common shares of a corporate listed issuer than to units of a mutual fund, and, accordingly, warrant offerings by non-redeemable investment funds are analogous to rights offerings by corporate issuers. Some commenters noted that even though rights offerings are frequently conducted at a discount to market price (similar to warrant offerings), there are no equivalent restrictions on public companies based on the same concerns regarding dilution or coercion. One commenter submitted that the mere fact that an investment fund is able to calculate NAV, while a public company cannot, is not sufficient to justify different regulation. Several commenters also disagreed with the view that warrant offerings may be coercive to securityholders who are obligated to make an additional investment in the fund or face the risk of dilution. Some commenters emphasized that warrants are not prejudicial to investors when they are listed on an exchange because securityholders are able to realize their value if they choose not to exercise their warrants. We were told by one commenter that warrant offerings can even be profitable to investors who sell their warrants on the exchange, regardless of whether any of the warrants are exercised. A few commenters submitted that warrant offerings are fair to existing securityholders because they provide them with an equal opportunity to participate in the offering and the ability to preserve their proportionate share in the non-redeemable investment fund. One	The CSA consider the concept of NAV to be a fundamental distinguishing feature between an investment fund and an issuer that is not an investment fund. Accordingly, the CSA continue to have concerns about the potential dilution to NAV resulting from warrant offerings by investment funds. While the CSA recognize that warrants which are listed on an exchange may mitigate some of the concerns in respect of coercive warrant issuances, the CSA are not satisfied that such listings will always be effective or sufficient to compensate investors who do not exercise their warrants for the loss of the value of their securities. See responses above.

	commenter believed that by virtue of their current ownership, existing securityholders are presumably satisfied with their investment and are more knowledgeable and favourably predisposed to buy additional securities of the non-redeemable investment fund. This commenter also noted that securityholders purchasing additional securities through warrants may incur lower commission costs than purchasing them on the secondary market, and they may be able to purchase larger quantities of securities without increasing the market price of those securities.	
	One commenter suggested that, rather than prohibiting warrant or rights offerings, the CSA could stipulate a maximum discount to the trading price that could be utilized in any such offering.	No change.
	A few commenters also disagreed that investors of non-redeemable investment funds may not expect the fund they invest in to seek additional capital from them after their initial investment. These commenters submitted that warrant offerings are not uncommon in the non-redeemable investment fund market and investors are aware of them. To address the CSA's concerns, some commenters suggested that non-redeemable investment funds be permitted to issue warrants and rights if this ability is disclosed in the fund's prospectus, or with securityholder approval if not disclosed in the prospectus. Such prospectus disclosure would include the risks associated with warrant offerings and the conditions under which warrants may be issued.	The CSA have observed that, over the last few years, non-redeemable investment funds have generally moved away from the use of warrant offerings as a way to raise capital for a non-redeemable investment fund. We are of the view that disclosure will not address the CSA's concerns outlined in the Request for Comments and discussed above.
	Several commenters were of the view that the decision	See responses above.

	to issue warrants should be left to market practice and the discretion of managers, who would assess whether the warrant offering would be in the best interest of securityholders in light of the potential benefits to the non-redeemable investment fund and the potential dilution to the NAV of the fund's securities. These commenters submitted that, since warrant offerings raise potential conflicts of interest issues for the manager, proposed offerings are often referred to the independent review committee of the fund for its review in accordance with NI 81-107 prior to the manager proceeding with the offering. Two commenters noted that the securities rules in the United Kingdom and the United States permit non-redeemable investment funds to issue warrants and rights to existing securityholders with an exercise price that is below NAV. These commenters suggested that there is no policy rationale for the CSA to differ from those jurisdictions.	 See responses above.
Redemption of securities (Part 10)	Several commenters generally agreed with the proposed amendments in connection with redemptions by non-redeemable investment funds, including the requirements that (i) a fund pay redemption proceeds within 15 business days of the redemption date, (ii) redemptions not be effected at prices that are greater than NAV, and (iii) a fund be permitted to suspend redemptions in certain circumstances. Some commenters expressed support for the proposed requirement that non-redeemable investment funds send an annual reminder to investors regarding the	We thank commenters for their feedback. The Amendments include these provisions. Subsection 10.1(4) of NI 81-102 provides that the requirement that non-redeemable investment funds send investors an annual reminder of the procedures for

	procedure for exercising redemptions, while others disagreed with the requirement or sought clarification of what would be acceptable in meeting those requirements. A few commenters questioned whether the annual reminder must be in the form of a separate mailing, from which securityholders may not opt out, or whether the requirement could be satisfied by including disclosure in the non-redeemable investment fund's annual information form or management report of fund performance (MRFP), or in the bulletins issued by CDS Clearing and Depository Services Inc. (CDS). Some commenters submitted that a separate mailing would add unnecessary costs to investors.	exercising redemptions does not necessarily require that the reminder be in the form of a separate mailing to securityholders, as long as the requirements are described in any document that is sent to all securityholders in that year. This is intended to ensure securityholders will be informed on an annual basis of their redemption rights.
	One commenter noted that any requirement to send investors an annual reminder of redemption procedures would have to be completed by dealers, and many dealers already send annual reminders of redemption dates to their clients. This commenter suggested that these reminders are sometimes confusing and the use of a standard form should be required so that it is clear to investors that the right to redeem is optional.	Non-redeemable investment funds will have the flexibility to determine the form of the annual reminder of the fund's procedures for exercising redemptions. This includes flexibility for a non-redeemable investment fund to include disclosure in the annual reminders that redeeming securities of the fund is optional.
	One commenter questioned the need to regulate the timing of the payment of redemption proceeds by non-redeemable investment funds.	The CSA consider a timeline for investors to receive their redemption proceeds to be a basic investor protection. We continue to think 15 days is a practicable timeline for non-redeemable investment funds.
	One commenter disagreed with the proposed requirement that the redemption price of a non-	No change at this time.

	redeemable investment fund's security not be a price that is more than the NAV of the security (the redemption price requirement). This commenter submitted that redeeming securities at a price that is more than the NAV of those securities does not always dilute remaining securityholders. For example, where a non-redeemable investment fund is invested in a credit default swap, there may be instances where the fund unwinds a portion of the credit default swap agreement to fund annual redemptions, and the fair value of the amount released by the counterparty to fund redemptions is greater than the proportionate share of the NAV invested in the swap. We were told that this excess amount paid to securityholders is borne by the counterparty to the swap agreement and not by the fund, and, therefore, does not dilute the other securityholders of the fund. As a result, it was suggested that the redemption price requirement only apply in circumstances where remaining securityholders would be diluted.	
	This commenter also submitted that the redemption price requirement may prohibit existing non-redeemable investment funds that offer quarterly redemptions based on the market price of the fund's securities from fulfilling their obligations when the fund's securities are trading at a price that is higher than NAV.	No change at this time. Redeeming securities of a non-redeemable investment fund at a price higher than the net asset value of those securities causes a reduction in the net asset value of the other securities of the non-redeemable investment fund. In the CSA's view, preventing this type of dilution is a core protection for investors.
	One commenter recommended that non-redeemable investment funds also be required to publicly disclose details of the annual redemption through a press release. This commenter suggested that such annual	No change at this time. Under Item 15.1 of Form 41-101F2, non-redeemable investment funds will be required to disclose the amounts that may be deducted from the net asset value per security from the

	disclosure include: • the number of securities tendered for redemption; • the number of securities taken up for annual redemption, if the amount of redemptions are capped; • the NAV applicable on the redemption date; • the actual amount of proceeds payable to redeeming investors after deducting redemption costs, charges and other deductions; • the redemption charges and any penalties deducted from NAV in order to calculate redemption proceeds; and, • any other relevant matters that affect the calculation or payment of redemption proceeds. This commenter was of the view that redemption charges are typically not adequately disclosed in prospectuses or continuous disclosure documents and that information regarding the historical practices of the manager with respect to redemptions is useful for investors.	redemption proceeds payable to redeeming securityholders. At this time, we consider this additional disclosure requirement, along with the required disclosure in the financial statements of the aggregate amounts paid on redemptions of securities of the non-redeemable investment fund, to be adequate. The CSA will continue to consider whether additional disclosure requirements related to redemptions by non-redeemable investment funds will be beneficial.
Commingling of cash (Part 11)	A few commenters expressed support for the Proposed Amendments that would apply the provisions relating to the holding of monies from sales and redemptions in a trust account to non-redeemable investment funds. However, several commenters noted that, unlike mutual funds, non-redeemable investment funds are held on a non-certificated basis through the book-entry only system of CDS. We were told that net sales proceeds from an offering of non-redeemable investment fund securities are transferred directly from	We thank commenters for their feedback. See new subsection 11.4(1.3) of NI 81-102, which states that section 11.1 of NI 81-102 does not apply to CDS. We have not included transfer agents or registrars of an investment fund in the exemption from section 11.1 of NI 81-102. The CSA note that there is currently no exemption from section 11.1 of NI 81-102

	the lead agent to the fund's custodial account and distributions and redemptions are typically transferred from the custodial account through certain qualified transfer agents to be effected through CDS. As a result, these commenters submitted that there is no opportunity for commingling of cash and the trust account requirements should not apply to such qualified transfer agents or CDS. It was recommended that we define a "qualified transfer agent" as an "entity appointed as transfer agent or registrar of an investment fund that satisfies the requirements of section 6.2", and that we include an exemption from sections 11.1 and 11.2 of NI 81-102 for CDS or qualified transfer agents in subsection 11.4(1) of NI 81-102.	for transfer agents of mutual funds, and we are not aware of any issues with mutual funds complying with this requirement.
Record dates (Part 14)	Many commenters agreed with the Proposed Amendments to apply the record date requirements of NI 81-102 to non-redeemable investment funds. Several of these commenters also submitted that the proposed record date requirements should not apply to mutual fund rollover transactions by flow-through funds. It was suggested that an exemption be provided in section 14.1 of NI 81-102 or that guidance be added to 81-102CP to clarify that the requirements for setting record dates do not apply to these transactions.	We thank commenters for their feedback. After considering the comments received, the CSA have decided not to apply Part 14 of NI 81-102 to non-redeemable investment funds. The CSA recognize that the majority of non-redeemable investments funds list their securities on an exchange and are already subject to the requirements of the exchange in respect of setting record dates. The CSA also note that the remaining non-redeemable investment funds that do not list their securities on an exchange are primarily flow-through limited partnerships, which must comply with applicable limited partnership legislation for setting record dates that may conflict with the proposed amendments to NI 81-102. Accordingly, Part 14 of NI 81-102 will not apply to non-redeemable investment funds.

Sales communications (Part 15)	Many commenters supported the extension of the sales communications requirements in Part 15 of NI 81-102 to non-redeemable investment funds, so long as the requirements recognize the differences between mutual funds and non-redeemable investment funds. In particular, two commenters expressed support for the proposed requirement that a mutual fund which has previously existed as a non-redeemable investment fund present past performance data for the period that it existed as a non-redeemable investment fund. One commenter submitted that the proposed sales communications requirements would not permit the presentation of after tax returns, which is relevant for investors holding certain funds, such as flow-through funds. This commenter expressed that, due to the unique features of non-redeemable investment funds, sales communication requirements need to be sufficiently flexible to allow for presentation of information that permits investors to properly assess the performance of their investment.	The CSA consider that the sales communications requirements in the Amendments appropriately recognize the differences between mutual funds and non-redeemable investment funds. We thank commenters for their feedback. The purpose of the sales communications requirements in Part 15 of NI 81-102 is to ensure that sales communications of non-redeemable investment funds contain relevant information and are not misleading. Non-redeemable investment funds are encouraged to contact staff of the local jurisdiction should questions arise on whether proposed sales communications comply with Part 15 of NI 81-102.
Securityholder records (Part 18)	A few commenters expressed support for the application of securityholder record requirements in Part 18 of NI 81-102 to non-redeemable investment funds. One commenter suggested, however, that section 18.1 should not apply to limited partnerships.	We thank commenters for their feedback. No change. The CSA are of the view that limited partnerships can comply with both NI 81-102 and the rules in respect of securityholder records under applicable limited partnership legislation.

	Several commenters submitted that, unlike mutual funds, non-redeemable investment funds are book-entry only through the facilities of CDS and, accordingly, CDS is the sole registered securityholder. As such, a non-redeemable investment fund's securityholder records are necessarily more limited than a mutual fund's. These commenters sought confirmation that this is acceptable to the CSA.	The CSA recognize that CDS is the sole registered securityholder for many non-redeemable investment funds. See subsection 15.1(2) of 81-102CP.

Part III - Comments on securities lending, repurchases and reverse repurchases by investment funds		
Questions	**Comments**	**Responses**
1. Are there other costs of conducting securities lending, other than the fee paid to the lending agent?	Some commenters told us that, generally, all securities lending costs incurred by investment funds are paid by the securities lending agent, who receives a fee from the fund (that is taken out of the securities lending revenue) for its services. Another commenter submitted that the only costs of conducting securities lending, other than the lending agent's fee, are the customary legal and administrative costs associated with entering into the securities lending arrangement itself. However, one commenter told us that certain funds may pay certain transaction-related costs directly, which include custodial charges, transaction fees, market fees and service provider charges. Furthermore, this commenter indicated that some	We thank commenters for their feedback.

	managers charge a fee for overseeing the securities lending program, and investment funds that invest the cash collateral they receive in a money market fund may also incur a management fee for that investment. A few commenters emphasized that, as investment funds only receive securities lending revenue net of the lending agent's share, a fund does not pay for the agent's share and, therefore, there is no "cost" to securities lending.	
2. What approaches could the CSA consider to ensure that the financial statements of an investment fund disclose the revenue from securities lending inclusive of the share paid to the agent? What approaches could the CSA consider to ensure that the financial statements of an investment fund disclose the costs of securities lending?	Commenters had different views regarding disclosure of gross revenue from securities lending in an investment fund's financial statements. A few commenters suggested that disclosure of gross revenue from securities lending could be addressed through a requirement for additional note disclosure in the financial statements, such as a tabular reconciliation of gross lending income and payment amounts for the reporting period to the securities lending income amount presented in the statement of operations. One such commenter also submitted that the notes to the financial statements could also disclose the material terms of lending agent compensation, including disclosure of any fees incurred by the fund in connection with securities lending. One commenter suggested requiring a presentation of gross securities lending amounts for income and any offsetting payments within the revenue category of the statement of operations.	We thank commenters for their feedback. The CSA agree with the approach of requiring additional note disclosure in the financial statements of an investment fund. See new subsections 3.8(4) and (5) of NI 81-106. We believe these new subsections will result in clearer and more transparent disclosure regarding the costs of securities lending by investment funds. The CSA are of the view that subsections 3.8(4) and (5) of NI 81-106 are adequate to achieve our objective of requiring an investment fund's financial statements to disclose the revenue from securities lending inclusive of the share paid to the securities lending

	Another commenter was of the view that the CSA should ensure that securities lending revenue is disclosed inclusive of the share paid to the securities lending agent by requiring that funds only be permitted to lend under agreements that specify that agents will provide full and complete disclosure of lending revenue received by the agent and any associated party, with a detailed breakdown of associated costs. According to this commenter, managers should be required to include costs that are expenses paid to third parties, and in addition, any cost of its own expended for securities lending.	agent. Accordingly, we are not proceeding with other proposals relating to the disclosure of revenue and costs of securities lending by investment funds at this time.
	A few commenters were of the view that the revenue sharing arrangement between an investment fund and its lending agent is proprietary or may be subject to non-disclosure agreements because of competitive concerns. According to these commenters, mandated disclosure of this information will impact the competitive landscape of the securities lending industry and may result in service providers being less likely to provide concessions on terms and fees while providing little to no added benefit. One such commenter told us that it would support additional disclosure regarding revenue sharing arrangements between the fund and the lending agent where the manager is acting as the securities lending agent or where the agent is someone other than the custodian of the fund. Some commenters were of the view that it is not meaningful for an investment fund's financial	While the CSA recognize that managers and securities lending agents may wish to keep information regarding revenue sharing arrangements confidential, we are of the view that this information is important for investors, especially in light of the potential conflicts of interests that may arise in cases where the securities lending agent of an investment fund is an affiliate of the manager. The disclosure required by subsections 3.8(4) and (5) of NI 81-106 is intended to provide information regarding the revenue sharing arrangement between an investment fund and its securities lending agent so that investors will be better able to understand the total costs and returns of the investment fund's securities lending activities. Currently, investors do not have information concerning what amounts, if any, are received by the securities lending agent out of the amount generated from an investment fund's securities lending activities. The CSA are of the view that such

	statements to disclose the revenue from securities lending, inclusive of the share paid to the securities lending agent, and then show the agent's share as an additional cost. As investment funds using lending agents can never earn 100% of the lending revenue, these commenters thought that disclosing gross revenue will only inflate the income while providing no additional benefit to the reader of the financial statements. According to one of these commenters, disclosure of gross revenue, and the share of the agent's revenue as a cost to the fund, does not appear to match the cash flow of the transaction. One commenter noted that, as the revenue generated from securities lending, repurchases and reverse repurchases for an investment fund is minimal, and the portion paid to the lending agent is generally *de minimis*, additional disclosure regarding the revenue sharing arrangement should not be required. This commenter felt that the preferable approach is for the independent review committee to review and approve securities lending, repurchase and reverse repurchase arrangements.	information is relevant to investment fund securityholders, particularly where the securities lending agent is an affiliate of the manager or where it provides other services to the investment fund (e.g., custodial services), as the fees otherwise charged to the fund by the manager or the service provider may be reduced as a result of receiving a portion of the amount generated from the securities lending activities. As a result, the true cost of owning securities of the investment fund would not be transparent to securityholders. The CSA also think that, by requiring all investment funds to provide disclosure about their revenue sharing arrangements, whether or not the securities lending agent is related to the manager, investors will also have the benefit of comparing this information across different investment funds and fund families. See responses above. The CSA do not consider the disclosure required by subsections 3.8(4) and (5) of NI 81-106 to be onerous and we think that the costs of providing such disclosure are outweighed by the benefits.
3. What approaches could the CSA consider	Most commenters agreed that, from an accounting standpoint, the fees paid to the securities lending agent are not a cost of engaging in securities lending	After reviewing the comments received, the CSA are not proceeding with a requirement to include the fees paid to the securities lending agent in an investment

to ensure that the costs of securities lending are included in either the management expense ratio or the trading expense ratio of the investment fund?	activities, and therefore, these fees should not be included in the calculation of an investment fund's MER or trading expense ratio (TER). One such commenter told us that it would be more accurate and meaningful to disclose the costs of securities lending as a reduction in the gross return from securities lending (i.e., as an offset against revenue). A few commenters suggested that the CSA take into consideration the views of applicable professional accounting bodies in any proposed revisions to the rules governing the preparation of financial statements and MRFPs, as the disclosure of the securities lending agent's share of the securities lending revenue as an expense may be inconsistent with accepted accounting treatment of securities lending revenue, given that the agent is entitled to its share before remitting net revenue to the investment fund. One commenter suggested that the costs of securities lending and repurchases do not need to be disclosed given their *de minimis* levels and the competitive landscape. One commenter submitted that requiring inclusion of the fees paid to the securities lending agent in an investment fund's MER may prompt funds to discontinue their securities lending activities, which the commenter felt was not in a fund's best interests.	fund's MER or TER. We think that the disclosure required by subsections 3.8(4) and (5) of NI 81-106 adequately addresses the CSA's concerns that investors receive continuous disclosure regarding the amount of the securities lending revenue generated by their investment fund that is retained by the securities lending agent. The CSA have considered applicable accounting rules in drafting the Securities Lending Disclosure Requirements. While the CSA accept the view that the costs of securities lending by an investment fund, particularly the fees paid to the securities lending agent, may not technically be considered an "expense" from an accounting standpoint, the CSA are of the view that the costs of securities lending by an investment fund are relevant for investors. As a result, while the disclosure required by subsections 3.8(4) and (5) of NI 81-106 will provide information about such costs, we also think this disclosure will not impact the MER disclosed by investment funds.
4. We think that the disclosure of the returns and	Commenters who responded to this question agreed that disclosure regarding the returns and costs of securities lending and repurchases should be disclosed	After reviewing the comments received, the CSA are not requiring that disclosure regarding securities lending and repurchases by investment funds be

the costs of repurchases should be the same as the disclosure of securities lending, since both activities are substantively similar. Should the same type of disclosure for reverse repurchases be provided? Should the returns and costs of securities lending and repurchases be aggregated, rather than disclosed separately?	separately, as they represent different activities and are not substantially similar. A few of these commenters told us that the fee arrangements for securities lending and repurchases are different, as are the underlying drivers for these activities. According to these commenters, securities lending is an ancillary activity designed to provide incremental returns and generate additional income for an investment fund, and is not a primary component of achieving a fund's investment objective. Further, securities lending arrangements are typically managed by an agent and are subject to an additional fee. On the other hand, reverse repurchase transactions are normally managed by the fund's portfolio manager without an incremental fee, as the management of these activities forms part of the portfolio manager's investment management services and is covered by the management fee. As an example of reverse repurchases forming part of an investment fund's investment strategy, one commenter noted that reverse repurchases are employed to generate a cash-like return similar to commercial paper issued by the same counterparty.	aggregated, given that they are different activities with different underlying drivers. New subsections 3.8(4) and (5) of NI 81-106 only apply to securities lending by investment funds.
5. In order to provide investors with transparency on the profitability and scope of an investment fund's	One commenter felt that disclosure of the average daily aggregate dollar value of securities lent (average on-loan) and the maximum amount of securities lent expressed in dollars (maximum on-loan) could be misleading or confusing for investors. Given the potentially wide range of underlying fund sizes that engage in securities lending, this commenter felt that	After reviewing the comments received, the CSA are not introducing any of these additional disclosure requirements at this time. However, we will continue to monitor securities lending, repurchases and reverse repurchases by investment funds, as well as international developments in this area, and may introduce new quantitative disclosure items in the

securities lending and repurchase activities, the CSA are considering requiring certain additional disclosure, in the investment fund's management reports of fund performance regarding such activities. **Do you agree that these disclosure items are useful in increasing transparency regarding the profitability and scope of a fund's securities lending and repurchases? Are any of these items less useful to investors, in light of the costs to the investment fund of calculating and disclosing them?**	the most meaningful disclosure would be the average and maximum on-loan as a percentage of NAV. Some commenters were of the view that, while the proposed disclosure measures would provide investors with a significant amount of data about securities lending, this information may not be useful to investors. Reasons that were provided include the following: • the information regarding securities lending would be more extensive than the information investors receive about the primary investment strategies of a fund, which could divert their focus from the latter even though that information is far more material; • securities lending revenue is driven by market demands and corporate events, which may vary significantly year to year, and which make comparisons of securities lending data between funds or over a period of time impossible; and • the information would likely be confusing to investors and would require substantial costs to be borne by the fund. Some commenters emphasized the importance of a balanced and proportionate disclosure framework and thought that it is important to consider the benefits provided by disclosure as well as the administrative and compliance costs of providing the disclosure. These commenters told us that the revenues generated from securities lending may not justify the cost of	future.

	collecting and disclosing such information. One commenter supported additional disclosure with regard to securities lending, but was less convinced of the benefits of such disclosure for repurchases. One commenter supported the CSA's effort to enhance investors' understanding of the benefits, costs and risks of securities lending, repurchases and reverse repurchases by investment funds, but believed that current disclosure requirements are sufficient. This commenter felt that requiring more granular financial disclosure or publicly disclosing the contractual arrangements with respect to these activities would not provide further clarity to investors regarding securities lending, repurchases and reverse repurchases. Another commenter noted that this is especially the case for mutual funds, since they do not generally use repurchase and reverse repurchase strategies and securities lending is not a significant investment strategy.	
6. Are there any other measurements regarding securities lending, repurchases or reverse repurchases that would provide useful	A few commenters told us that, given the revenue generated from securities lending, repurchases and reverse repurchases is immaterial to an investment fund and its investment strategies, and would not influence an investor's investment decision to buy or hold securities of a fund, no measurements of securities lending other than those currently required would provide useful information to investors. Certain commenters submitted that qualitative	After reviewing the comments received, we are not introducing any additional quantitative disclosure requirements at this time other than the requirements in subsections 3.8(4) and (5) of NI 81-106. The CSA are introducing certain qualitative disclosure requirements, which are discussed in the comments and responses to question 7 below. The CSA continue to believe that clear and detailed

information to investors in addition to, or in lieu of, the items described in question 5?	disclosure, such as disclosure regarding the risks and returns of securities lending in the fund's prospectus or annual information form, including the relevant protections and remedies available to the investment fund under the lending agreement, may enhance investor understanding of securities lending activities and their associated risks. One such commenter noted that this was consistent with what the European Securities and Markets Authority (ESMA) is proposing.	disclosure regarding an investment fund's securities lending, repurchase and reverse repurchase activities is important for investors. Accordingly, we will continue to monitor domestic and international developments regarding the regulation of these activities and may introduce new requirements in the future.
	One commenter submitted that the focus of disclosure should be on potential conflicts of interest, which are adequately addressed under existing disclosure requirements.	The CSA agree that disclosure of potential conflicts of interest is crucial. The new disclosure requirements regarding the identity of an investment fund's securities lending agents in the fund's prospectus and annual information form (AIF), as well as the amount of the securities lending revenue received by the lending agent in the fund's financial statements, are intended to provide information about the potential conflicts of interest that may arise in the context of an investment fund's securities lending activities. See Item 10.9.1 of Form 81-101F2, Item 19.11 of Form 41-101F2 and subsections 3.8(4) and (5) of NI 81-106.
	Another commenter felt that disclosure regarding the quality and amount of collateral held against a securities lending transaction would be helpful for investors. Otherwise, it may appear that an investment fund's lending balances represent exposure to the counterparties even though the exposure is over-collateralized. This commenter suggested requiring disclosure of corresponding levels of collateral held against securities loaned or of the net exposure or risk-	The CSA note that subsection 3.8(2) of NI 81-106 already requires disclosure in an investment fund's financial statements about the type and amount of collateral received by the investment fund under its securities lending transactions that are outstanding as at the date of the financial statements. At this time, the CSA do not think that the benefits of requiring additional disclosure regarding collateral would outweigh the costs of providing such disclosure.

	adjusted exposure. One commenter told us that it would support additional disclosure requirements to ensure that investors are properly informed of the non-redeemable investment fund's intention to engage in securities lending, repurchases and reverse repurchases and the associated risks. According to this commenter, the ability to engage in securities lending, repurchases and reverse repurchases should be determined in light of a non-redeemable investment fund's investment objectives and strategies and properly disclosed in the prospectus. Similarly, one commenter noted that, if additional disclosure regarding securities lending, repurchases and reverse repurchases is required, alternate measures in lieu of those proposed by the CSA should be required. However, this commenter could not identify any circumstances where the costs of such disclosure would outweigh the benefits.	 The CSA agree that an investment fund's ability to engage in securities lending, repurchases and reverse repurchases should be determined by the fund's investment objectives and investment strategies, and must be properly disclosed in the investment fund's prospectus in accordance with the applicable Form requirements. See responses above.
7. The CSA are considering adding the agent in respect of securities lending, repurchases and, if applicable, reverse repurchases to the list of service providers required to be	A few commenters were of the view that it is important for investors to know the identity of the major service providers an investment fund uses, the amounts such service providers are paid and whether they are affiliates of the investment fund. However, these commenters did not believe this requirement should apply to repurchases or reverse repurchases, as such activities are generally managed by the investment fund's portfolio manager under the fund's investment management agreement. One commenter noted that, if securities lending	The CSA are introducing requirements for investment funds to disclose the identity of the investment fund's securities lending agent in the investment fund prospectus and AIF. See new Items 19.11 of Form 41-101F2 and 10.9.1 of Form 81-101F2. While the revenue received from securities lending

disclosed in an investment fund's prospectus or AIF, as applicable. Another outcome of disclosing the agent would be that the agent's relationship to the manager would also be disclosed in the prospectus or AIF, so that investors can assess whether amounts are being paid to entities affiliated with the manager in connection with the investment fund's securities lending, repurchase or reverse repurchase activities. **Is this disclosure useful? Should any additional details regarding**	activities conducted by an investment fund's securities lending agent are material in relation to the other activities of the investment fund, information about that agent should be disclosed on a basis consistent with the disclosure regarding the transfer agent of the fund. On the other hand, one commenter was of the view that new disclosure would not be useful given the immaterial nature of the revenue generated by securities lending and the commensurate level of potential risk exposure. However, this commenter suggested that disclosing the credit rating of the securities lending agent may provide additional insight to investors. A few commenters noted that NI 81-102 prescribes that an investment fund's securities lending agent must be the fund's custodian, and this information is currently disclosed in continuous disclosure documents. According to one of these commenters, any related party disclosure that is relevant is already available in an investment fund's financial statement disclosure. One commenter expressed that disclosure of any conflict of interest with an affiliated or non-arm's-	may be immaterial to an investment fund, there may be conflicts of interest arising from an affiliate of the manager acting as the securities lending agent of the investment fund and receiving part of the securities lending revenue. Accordingly, the CSA are of the view that the identity of the securities lending agent is relevant for securityholders of an investment fund and should be disclosed. As subsection 2.15(3) of NI 81-102 requires the securities lending agent of an investment fund to be either the custodian or sub-custodian of the investment fund, concerns regarding the creditworthiness of the securities lending agent are mitigated by the capitalization and other requirements applicable to custodians and sub-custodians under Part 6 of NI 81-102. Therefore, the CSA have not introduced a requirement to disclose the credit rating of an investment fund's securities lending agent. While NI 81-102 does require that the securities lending agent of an investment fund be the custodian or sub-custodian of the investment fund, a securityholder may not know which of the investment fund's custodian or sub-custodians is acting as securities lending agent. Therefore, the CSA are of the view that mandating disclosure of the securities lending agent is an important facet of increasing the transparency of any potential conflicts of interests that exist in respect of an investor's investment in an investment fund. The CSA think that the new disclosure required by Items 19.11 of Form 41-101F2 and 10.9.1 of Form 81-

the agent be provided in an investment fund's prospectus or AIF?	length lending agent must be clear and also address how the conflict is being appropriately managed so as to not disadvantage the investment fund.	101F2 will clearly indicate whether the securities lending agent is related to the manager of the investment fund. In the future, the CSA may consider the usefulness of additional disclosure regarding how any potential conflict of interest between the lending agent and the investment fund is being addressed.
8. We understand that investment funds may seek different indemnities from their lending agent, which provide varying degrees of protection from losses that could arise from securities lending. Would disclosure of the indemnities obtained by an investment fund from its lending agent in the AIF or prospectus of the investment fund be useful for investors in assessing the risks from securities lending?	Some commenters were of the view that disclosure of indemnification arrangements in favour of investment funds is valuable for investors in assessing the risks of the securities lending activities. One such commenter noted that extensive securities lending makes simple investment products into complex products due to the complex lending operations, highly diverse conditions under which the lending takes place and the significant liquidity and counterparty risks associated with the lending. Therefore, it was submitted that disclosure of indemnities would be a necessary first step. This commenter also suggested that the CSA consider whether a certain amount of indemnification should be required. One commenter noted that the final form of indemnity provided in favour of an investment fund varies from arrangement to arrangement and may have numerous carve-outs or conditions. We were told that disclosure of indemnities would be cumbersome and complex and would not enable meaningful comparisons to be made by an investor.	The CSA agree that disclosure of indemnities received by an investment fund from its lending agent is important and useful for investors, and are introducing a requirement to provide such disclosure. See new Items 19.11 of Form 41-101F2 and 10.9.1 of Form 81-101F2. The CSA are not requiring minimum indemnities at this time, given that NI 81-102 currently requires that the market value of the collateral delivered to an investment fund in connection with a securities lending transaction be at least 102% of the market value of the loaned securities (i.e., the investment fund's securities lending exposure must be overcollateralized). While the particular indemnity provided in favour of one investment fund may differ from an indemnity granted to another fund, the CSA do not consider this different from any other arrangement between an investment fund and its service providers, which arrangement may vary from fund to fund. Similar to the required disclosure of the essential terms of contractual

		arrangements between investment funds and certain service providers, the requirement in Items 19.11(3) of Form 41-101F2 and 10.9.1(3) of Form 81-101F2 is to provide a brief description**.**
	A few commenters submitted that, as a result of the requirement in NI 81-102, that an investment fund adjust daily the amount of collateral it holds to ensure that the market value is at least 102% of the value of the loaned securities, borrower indemnification provisions would not materially affect the risks associated with the securities lending.	Although the securities lending exposure of an investment fund under NI 81-102 must be overcollateralized, the CSA think that disclosure regarding the indemnities provided to an investment fund by the securities lending agent may still be relevant. In particular, disclosure of indemnification arrangements may highlight the potential risks or conflicts of interests where the agent is not arm's-length to the manager; for example, the manager in such circumstances may have an interest in the securities lending agent either not providing an indemnity, or providing a very narrow one.
	Other commenters were of the view that, if in particular circumstances indemnification is deemed to be material, then additional information may be provided in response to existing form requirements such as the risk disclosure required by Item 12 of Form 41-101F2 or Item 12(2) of Form 81-101F2.	The CSA agree that risk factor disclosure is important, and all material risks should be disclosed by an investment fund in its prospectus or AIF, as applicable. The CSA also think, however, that specific disclosure regarding any indemnity provided to the investment fund by the securities lending agent should be provided.
	One commenter added that it would be disproportionate to require disclosure in respect of one particular indemnity arrangement when an investment fund has many others.	While disclosure of other indemnities provided to an investment fund may also be beneficial, this phase of the Modernization Project has focused on securities lending, repurchases and reverse repurchases by investment funds and, therefore, we have considered in particular the relevance of the indemnities provided by securities lending agents. In the future, the CSA may

		consider whether disclosure of other indemnities provided to investment funds would be useful as well.
9. Generally, investment funds do not file the agreements that they enter into with their lending agent on SEDAR. Currently, these agreements are not listed in the AIF under Item 16 of Form 81-101F2 or the prospectus under Item 31 of Form 41-101F2. Should these agreements be required to be included as material contracts and filed on SEDAR?	Some commenters submitted that securities lending does not generate material revenue or is generally not fundamental to the investment objectives of a fund, and therefore, agreements entered into between investment funds and their lending agent are not material contracts and should not be required to be filed on SEDAR. On the other hand, one commenter was of the view that securities lending agreements should be required to be disclosed and filed on SEDAR. This commenter noted that it already considers them to be material under the facts-based test for determining materiality of an agreement. Other commenters were of the view that the current requirements relating to the filing and disclosure of material contracts is an adequate test for capturing contracts that are not otherwise specified in Form 81-101F2. According to these commenters, it is appropriate for the investment fund manager to determine whether or not a securities lending agreement constitutes a material contract of the investment fund and, accordingly, whether it should be listed in a fund's prospectus or annual information form. A few commenters cautioned that the contents of a securities lending agreement are already mandated by NI 81-102 and the non-mandated terms, such as negotiated revenue sharing arrangements, are generally	After reviewing the comments received, the CSA are not introducing any requirements with respect to the filing of securities lending agreements. However, we note that, while there is no particular requirement that an investment fund file its securities lending agreement on SEDAR, an investment fund may still be required to file its securities lending agreements if they are material to the investment fund. Therefore, managers should be aware of the applicable rules regarding the filing of material contracts by investment funds, and make a determination regarding whether the securities lending agreement between an investment fund and its securities lending agents should be publicly disclosed on SEDAR.

	confidential and of a competitive and proprietary nature.	
Other general comments	Commenters generally agreed that information regarding the returns, costs and risks of an investment fund's securities lending, repurchase and reverse repurchase activities may be important and relevant to the investment fund's securityholders. However, commenters disagreed on whether additional disclosure regarding such activities, beyond what is currently required, is necessary or beneficial to investors, or whether the benefits of such additional disclosure would outweigh the potential disadvantages and costs.	As detailed above, the Securities Lending Disclosure Requirements introduced by the CSA at this time include a limited number of disclosure items that we consider to be particularly important and relevant to investors. We will continue to monitor international developments and consider whether additional requirements are necessary.
	Some commenters expressed concern that the Securities Lending Disclosure Proposals would obscure important and relevant facts regarding an investment fund with over-disclosure of less relevant information. These commenters felt that the Securities Lending Disclosure Proposals place undue emphasis on securities lending, repurchases and reverse repurchases by investment funds, given that these activities could affect only a small portion of a fund's assets and overall investment activities, and may mislead investors into thinking that such activities play a more important role in the management of the fund than they actually do.	The CSA believe that the Securities Lending Disclosure Requirements strike the appropriate balance between the need for meaningful disclosure regarding the costs, benefits and risks of an investment fund's securities lending and the desire to avoid over-disclosure of less relevant facts. We think these requirements will ensure that the most material facts, such as the revenue sharing arrangement between the investment fund and its securities lending agent and the identity of the securities lending agent, will be disclosed.
	Certain other commenters were of the view that the CSA should have sought information from managers as to the nature and extent of securities lending, repurchases and reverse repurchases by investment funds, and the materiality of such activities, before	See responses above. While the CSA are aware that some managers do not consider the revenue generated by securities lending, repurchases and reverse repurchases to be material to their investment funds, we are of the view that certain disclosure regarding

	proposing additional disclosure requirements. While one commenter felt that conflicts of interest may arise in the context of a fund's securities lending activities, especially where a fund manager is administering the securities lending, this commenter felt that stakeholders should be consulted before new requirements come into force.	these activities is important for investors. The Securities Lending Disclosure Requirements were formulated based on the extensive feedback received from stakeholders in response to the detailed questions asked in Annex C of the Request for Comments.
	One commenter emphasized that retail investors are not in the best position to scrutinize how the securities lending program of a fund is structured and accounted for. According to this commenter, the investment fund governance rules should be reformed so as to require investment funds to have an independent board of directors, rather than the current independent review committee model, as the board would be in a position to put the portfolio managers to task and ask the hard questions.	The CSA believe it is important that investors have access to certain disclosure about the securities lending activities engaged in by the funds in which they invest. A review of the independent review committee model under NI 81-107 is not within the scope of the Modernization Project.
	Commenters also addressed the revenue-sharing arrangements between an investment fund and its securities lending agent. A few commenters noted that securities lending agents provide many services to investment funds, such as research, analytics and trading tools, which, given the over-the-counter nature of the securities lending market, can have an appreciable effect on lending revenues. These commenters also submitted that many lending agents currently provide a lot of transparency to managers regarding the costs, risks and benefits of securities lending and repurchase activities as well as	The CSA do not currently have issues with the types of services provided by securities lending agents to investment funds, or the practice of sharing the securities lending revenue between the investment fund and its securities lending agent. The purpose of the Securities Lending Disclosure Requirements is to provide greater transparency through disclosure of the costs and returns related to the securities lending arrangements entered into by investment funds as well as any potential conflicts of interest between investment funds and their securities lending agents.

	reporting beyond what is required by the regulations. As the costs of these services are generally borne by the securities lending agent, the revenue-sharing arrangements compensate agents for these costs while aligning their incentives with those of the fund in ensuring that lending activity is profitable. One commenter was of the view that a vast majority of Canadians who own investment funds are unaware that the securities held by their funds are being loaned out, let alone what the amount of revenue is going to the fund versus the lending agent or portfolio manager. This commenter felt that the current system, where the fund managers take a portion of lending fees while the securityholders are responsible for the losses, risks and rewards, is not a fair system and does not mitigate potential systemic risks. This commenter saw the present practice as a breach of the fund manager's fiduciary duties to the fund and should not be permitted to continue on this principled basis.	 No change at this time. The CSA believe that securities lending by investment funds should be permitted subject to the requirements in NI 81-102. We are also introducing the Securities Lending Disclosure Requirements.

Part IV - Other comments		
Issue	**Comments**	**Responses**
Annual redemptions of securities based on NAV	On the question of whether the CSA should reconsider its present view that investment funds that permit redemptions of their securities only once a year based on NAV be considered non-redeemable investment funds, one commenter thought that the CSA should revisit this view. This commenter suggested that new	After considering the comments received, the CSA have decided not to revisit our current view. The CSA recognize that many non-redeemable investment funds have been structured based on the long standing interpretation that securities that may be redeemed no more frequently than once a year are not redeemable

	non-redeemable investment funds not be permitted to offer any redemptions at NAV. However, the majority of commenters were of the view that the current distinction between “mutual fund” and “non-redeemable investment fund” be maintained, such that an investment fund that offers redemptions no more than once a year continue to be considered a non-redeemable investment fund. Several commenters were of the view that changing this interpretation would create unnecessary confusion for investors and advisors, who assume that all mutual funds have daily liquidity at NAV. In particular, some commenters thought the definition of “mutual fund” does not capture investment funds with an annual redemption feature, since annual redemptions may not constitute redemptions “on demand”.	“on demand”. Accordingly, the Amendments contemplate that a non-redeemable investment fund may offer an annual redemption of its securities with reference to the NAV of those securities. The CSA note that an annual redemption feature is commonplace among non-redeemable investment funds which publicly offer securities in Canada and we recognize that any benefit to changing our interpretation at this time would be outweighed by the confusion to the marketplace.
	Several commenters urged us to provide greater certainty by articulating the distinction between “mutual fund” and “non-redeemable investment fund” in NI 81-102.	No change. The definitions of “mutual fund” or “non-redeemable investment fund” are contained in the respective *Securities Act* of each CSA jurisdiction, and not in NI 81-102.
	One commenter noted that the occasional redemption right offered by non-redeemable investment funds is not a fundamental component of such products, and the panoply of regulation aimed at protecting the redemption rights of mutual funds in NI 81-102 would not be properly applied to non-redeemable investment funds. Another commenter noted that having different regulatory frameworks would be consistent with the	See responses above. The Amendments impose slightly different requirements on non-redeemable investment funds as compared to mutual funds. The CSA consider the different treatment of mutual funds and non-redeemable investment funds in NI 81-102 to appropriately capture their key distinctive features. In particular, the CSA have not at this time imposed many of the investment restrictions applicable to mutual funds on non-redeemable investment funds. As discussed in this Annex B, the CSA are continuing to

	regulation of non-redeemable investment funds and mutual funds in other jurisdictions. Several commenters reiterated that non-redeemable investment funds are formed and distributed in fundamentally different ways than conventional mutual funds. These commenters emphasized the importance of continuing to provide non-redeemable investment funds with the flexibility to use diverse investment strategies, which is justified by less frequent redemptions. One commenter expressed that regulating non-redeemable investment funds like mutual funds would essentially eliminate investor choice and cause investors to seek such products in jurisdictions outside Canada.	consider whether further investment restrictions should apply to non-redeemable investment funds to be published in conjunction with the Alternative Funds Proposals. The CSA will continue to consider, among other things, whether and the extent to which the frequency of redemption offered by an investment fund supports different investment restrictions. The CSA are of the view that, while non-redeemable investment funds will be subject to core operational requirements and certain investment restrictions that are equally applicable to all publicly offered investment funds, non-redeemable investment funds should continue to have sufficient flexibility to use a range of investment strategies.
	Several commenters were also concerned that reclassifying non-redeemable investment funds with an annual redemption feature as mutual funds would cause non-redeemable investment funds to remove their annual redemption feature. One commenter noted that an annual redemption feature has been a common feature throughout the history of non-redeemable investments funds, and, at least 90% of non-redeemable investment funds currently listed on the TSX have this feature.	As the CSA are not changing our view with respect to treating investment funds that offer an annual redemption feature as non-redeemable investment funds, non-redeemable investment funds may continue to provide annual redemptions of their securities without being considered mutual funds.
	Some commenters submitted that annual redemptions at NAV serve the following important purposes for non-redeemable investment funds and should be preserved: they permit investors to redeem at NAV where the fund's securities are trading at a lower price; they permit investors to liquidate a large holding if the	The CSA were not proposing to eliminate the annual redemption feature for non-redeemable investment funds. The purpose of our question was to examine whether the frequency of redemption alone supports the distinction between a "mutual fund" and a "non-redeemable investment fund" and their different

	fund's securities are thinly traded (which also permits a large redemption to be effected without a significant effect on the market price); and, they support the trading price of the fund's securities to ensure that the securities trade closer to NAV. We were also told that some non-redeemable investment funds provide an annual redemption right because it ensures the fund maintains its status as a "mutual fund trust" for purposes of the *Income Tax Act*. One commenter noted that the removal of any redemption feature at NAV would particularly impact unlisted non-redeemable investment funds where annual redemptions at NAV provide the only liquidity option for investors. Some commenters pointed out that the securities of non-redeemable investment funds in the United States, which do not have annual redemption features, trade at much lower prices relative to their NAV than the securities of Canadian non-redeemable investment funds. We were told that a significant negative impact on the trading price of non-redeemable investment fund securities would harm investors, since their primary means of gaining liquidity is through trading on an exchange.	regulatory frameworks. As noted above, after reviewing the comments received, we have not changed our view on this question. See responses above. The question of whether an investment fund whose securities entitle the holder to request that the fund redeem those securities at least once a year is a non-redeemable investment fund is a matter of legal interpretation and, in our view, is not impacted by the practical consideration of whether annual redemption features cause an investment fund's securities to trade at a price closer to their NAV relative to the securities of investment funds that do not have any redemption feature.
Transitioning and grandfathering of existing funds	With respect to the Investment Restriction Proposals, many commenters preferred grandfathering existing funds rather than a transition period.	After reviewing the comments received, the CSA have decided to grandfather certain non-redeemable investment funds in respect of the non-guaranteed mortgage restriction. See new subsection 20.4(2) of NI 81-102.

		Certain of the other Amendments will have transition periods ranging between six and 18 months. See "Transition Periods and Grandfathering" in the Notice. At the time that any additional proposed investment restrictions for non-redeemable investment funds are published for comment, the CSA will consider whether grandfathering in respect of those provisions would be appropriate.
	One commenter noted that the Proposed Amendments represent material changes, which could never have been anticipated, and many commenters expressed concern that making currently existing non-redeemable investment funds comply with the Proposed Amendments is inconsistent with the investment decision made by investors, their legitimate expectations and the commercial decision made by the manager in launching the fund. These commenters emphasized that managers have created and marketed their non-redeemable investment funds, and investors have purchased these funds, on the basis of their current structure, and this commercial bargain between the funds and their investors should be honoured. In particular, certain commenters were of the view that the bargain made by investors when investing in a non-redeemable investment fund was based on the current non-redeemable investment fund regime and upon fundamental terms set out in the non-redeemable investment fund's prospectus, which include the investment strategies and restrictions of the fund. These commenters questioned how requiring non-redeemable investment funds that are using an investment strategy	Unlike the Proposed Amendments, which proposed to impose restrictions on the use of leverage, short selling and derivatives by non-redeemable investment funds, the CSA expect the Amendments to have a very limited impact on the investment strategies of non-redeemable investment funds. Accordingly, the CSA do not believe any of the Amendments, other than the non-guaranteed mortgage restriction, materially affect the commercial bargain between non-redeemable investment funds and their investors. As stated above, grandfathering is being provided in respect of the non-guaranteed mortgage restriction. The CSA are of the view that many of the Amendments provide basic investor protections that the majority of non-redeemable investment funds already adopt.

	disclosed in their prospectus to retroactively comply with new regulations is in the best interest of investors or consistent with the investor protection objectives of securities law. As a result, these commenters considered it unfair for the rules to be changed such that an existing non-redeemable investment fund's investment strategy could no longer be implemented and submitted that, at a minimum, these funds be grandfathered with respect to the Investment Restriction Proposals.	
	One commenter added that requiring fundamental changes to a non-redeemable investment fund's investment strategies could compromise the ability of the non-redeemable investment fund to report historical performance.	See responses above.
	Some commenters expressed concern that the Proposed Amendments would have an extremely negative impact on the industry and the integrity of the prospectus, and that, even with transitioning, the Proposed Amendments are effectively retroactive rules. One such commenter referred to a standard tax policy principle stating that retroactive change that is not in the taxpayer's favour should be avoided or, at worst, only be used in exceptional circumstances. While this commenter believed tax and securities rules are different, it was submitted that the same principle of avoiding retroactivity should apply in the case of the Proposed Amendments.	In the CSA's view, the Amendments are not retroactive, as they do not apply to activities that occurred prior to the Amendments coming into force. The Amendments only apply to activities by non-redeemable investment funds which occur after the coming into force of the Amendments.
	Several commenters submitted that a transition period is not appropriate because the costs and disruption	See responses above. The CSA expect that generally, the Amendments will not require significant changes to

	associated with transitioning an entire fund family to comply with the Proposed Amendments would be significant for non-redeemable investment fund managers and investors. In particular, it was submitted that the costs and logistics of amending the constating documents of the fund, obtaining required securityholder approvals, and the associated notice and continuous disclosure requirements would be untenable. These commenters also felt that it would not be fair for securityholders or fund managers to bear the costs associated with implementing these changes, particularly since the non-redeemable investment funds were originally launched, marketed and managed in compliance with the existing regulatory regime.	a non-redeemable investment fund's investment strategies or constating documents and, as a result, will not impose significant costs on non-redeemable investment funds. To the extent that non-redeemable investment funds must make changes to certain aspects of their operations (e.g., their securities lending agreements or sales communications), transition periods have been provided.
	A few commenters told us that, absent grandfathering, the only alternative to changing the constating documents of a non-redeemable investment fund would be for the fund to wind up, fit into the alternative funds framework or convert to a non-investment fund issuer.	See responses above. The CSA do not think the Amendments will require non-redeemable investment funds to change their constating documents or wind up.
	One commenter conveyed that a grandfathering provision is warranted, but discretion should remain for managers to transition their non-redeemable investment funds into the new framework if they choose to accept the new restrictions. On the other hand, another commenter was of the view that existing funds should be grandfathered on an "all or none" basis, meaning that they should not be permitted to choose to comply with some of the Proposed Amendments and not others.	See responses above.
	Some commenters felt that the lack of clear permanent	See responses above.

	grandfathering, which would require non-redeemable investment funds to change their investment strategies, restrictions and operations, is not appropriate and will lead to confusion and market inefficiency. One such commenter was of the view that such a state of affairs would be directly contrary to fair and efficient capital markets and would harm confidence in the Canadian marketplace. A few commenters were also of the view that, in the interests of market efficiency and transparency, the CSA's intention with respect to grandfathering should be communicated to the market as soon as practically possible. According to these commenters, grandfathered funds should be permitted to continue to conduct their business, operations and affairs in all respects in compliance with their constating or governing documents and on the basis previously approved by the CSA. A few commenters felt that, even if grandfathering of existing non-redeemable investment funds were not granted, the transition period proposed in the Request for Comments is not sufficient, given the changes that will need to be made in order to comply, including amendments to relevant constating documents and material agreements, as well as obtaining securityholder approval and investment reallocation as well as other technical and procedural changes. One such commenter was of the view that the requirement to transition should not begin until a revised alternative funds regime is in place.	 As described above, other than with respect to the non-guaranteed mortgage restriction, the CSA do not think grandfathering is required with respect to any of the Amendments. The CSA will consider grandfathering with respect to any additional investment restrictions proposed in the future. As described above, given that the Amendments largely focus on introducing fundamental protections for securityholders of non-redeemable investment funds, the CSA are of the view that they should not require non-redeemable investment funds to make significant amendments to their investment portfolio or to their constating documents, which would require securityholder approval. Where, in the CSA's view, non-redeemable investment funds may require a transition period to comply with a particular provision, appropriate transition periods have been provided.

	A few commenters told us that a lack of grandfathering, which would cause currently existing non-redeemable investment funds to change their investment parameters, would negatively impact the future performance of these funds and may force some of them to liquidate assets, which would give rise to other complications and issues that may be more detrimental to securityholders than the perceived benefits that the Proposed Amendments are intended to provide. One such commenter thought that entire marketplaces surrounding the non-redeemable investment fund industry would be affected, potentially driving portfolio security values down and impacting non-redeemable investment fund investors. One commenter felt that forcing existing non-redeemable investment funds to sell their investments in a responsible manner that ensures the preservation of NAV would be a time-consuming process. Accordingly, this commenter requested that existing investments that do not comply with sections 2.2, 2.3 and 2.5 of NI 81-102 be allowed to mature or, where the investment does not have a maturity date, be allowed to be held for up to five years, ensuring that existing investors are not penalized as a result of the proposed amendments. Some commenters submitted that investors who wish to move to non-redeemable investment funds governed by NI 81-102, as amended by the Proposed Amendments, and any alternative funds regime, may sell or redeem their grandfathered funds and purchase those new funds.	See responses above. The CSA are providing 18-month transition periods for the Amendments relating to sections 2.2, 2.3 and 2.5 of NI 81-102 (other than with respect to paragraph 2.3(2)(b), where certain existing funds are being grandfathered). We are of the view that this transition period provides adequate time for a non-redeemable investment fund to dispose of investments which contravene these provisions. We disagree that sections 2.2, 2.3 and 2.5, as amended by the Amendments, would require a five year transition period. When the CSA consider the Alternative Funds Proposals further, we will also consider and publish for comment any transitioning provisions for non-redeemable investment funds subject to NI 81-102 that wish to be subject to the alternative funds framework in NI 81-104.

	Some commenters also expressed a particular view with respect to grandfathering investment funds affected by the non-guaranteed mortgage restriction, and suggested that grandfathering the affected non-redeemable investment funds would be the preferable approach and in the best interest of existing securityholders. One commenter noted that a transition period of 24 months for the non-guaranteed mortgage restriction would not be sufficient. According to this commenter, mortgage loans are contracts between a lender and a borrower and most loan terms would not include a right of demand for repayment and may have terms exceeding 24 months, and even up to 10 years. Therefore, transitioning out of non-guaranteed mortgages would force a fund to divest otherwise performing mortgages.	As noted above, the CSA are grandfathering certain existing non-redeemable investment funds from the non-guaranteed mortgage restriction. However, the CSA continue to have concerns regarding whether an issuer that invests all or substantially all of its assets in non-guaranteed mortgages is an investment fund. Therefore, if an issuer relies on new subsection 20.4(2) of NI 81-102 to invest in non-guaranteed mortgages and seeks to raise additional capital in the public markets, staff from the applicable CSA jurisdictions will closely review the issuer's prospectus with a view to determining whether the issuer is an investment fund, or whether it is a non-investment fund issuer that should comply instead with the securities regulatory regime applicable to such issuers.
	Some commenters noted that if the non-guaranteed mortgage restriction is adopted without grandfathering, mortgage investment entities that are currently structured as non-redeemable investment funds would have to conform their investment objectives to the non-guaranteed mortgage restriction or, in the alternative, they would be forced to wind up or convert to non-investment fund issuers. One commenter noted that causing MIEs to convert to non-investment fund issuers would require them to change their continuous disclosure mid-stream, which this commenter felt was inappropriate.	See response above.

Cost benefit analysis	Many commenters submitted that the direct and indirect costs of the Proposed Amendments materially outweigh the benefits for investors and issuers, and that the Proposed Amendments would impose a significant financial hardship on managers. Costs that were identified by commenters include: • increased costs to investors as a result of the proposed restriction on organizational costs being borne by a non-redeemable investment fund, as management fees may simply be increased to recoup the organizational costs; • significant costs to managers of non-redeemable investment funds as a result of the organizational cost proposals. We were told that these costs would create a barrier for managers to offer non-redeemable investment funds to the public, which would reduce competition and result in more limited investor choice with respect to unique investment products; • a loss of value of investments in non-redeemable investment funds; and • the cost of securityholder meetings to implement changes as a result of the Proposed Amendments.	The CSA note that many of the costs of the Proposed Amendments identified by commenters relate to the Investment Restriction Proposals and Organizational Cost Proposals. As the CSA are only implementing a limited number of the Investment Restriction Proposals, and are not moving forward with the Organizational Cost Proposals at this time, we are of the view that the costs submitted by commenters to be burdensome to non-redeemable investment funds and their managers are not applicable to the Amendments. Accordingly, we believe that the potential benefits of the Amendments outweigh their costs, as they impose core operational requirements on non-redeemable investment funds, which promote the CSA's goal of investor protection. We think the Amendments also provide for market efficiency, as they clearly indicate to managers of investment funds the types of activities and restrictions that the CSA consider inappropriate.
	A few commenters agreed that the imposition of core operational requirements would provide benefits because they promote the CSA's goal of investor protection. However, these commenters submitted that	See responses above.

	it is not clear what benefits the Investment Restriction Proposals provide, as it is not clear what harm the CSA are trying to rectify in imposing investment restrictions. Another commenter added that the CSA have consistently taken the view that the costs of regulation should not outweigh the expected benefits. A few commenters noted that no quantitative analysis of the costs or benefits of the Proposed Amendments was provided in the Request for Comments, and instead, the burden of providing a cost-benefit analysis has been shifted to the public. One commenter was of the view that the Proposed Amendments may lead investors to suspect problems with non-redeemable investment funds where none currently exist, which would be directly contrary to the CSA's mandate of supporting efficiency and building confidence in Canadian capital markets. This commenter also told us that further changes to our capital markets without a clear and present need will be confusing and will reduce, rather than add to, confidence in our capital markets.	 The CSA agree that the costs of regulation should not outweigh the expected benefits and, as discussed above, we are of the view that the benefits of the Amendments outweigh their costs. See response above. The CSA consider that many of the benefits of the Amendments represent core operational requirements for non-redeemable investment funds and fundamental protections for securityholders. The CSA disagree that introducing the Amendments will lead to investors suspecting problems with non-redeemable investment funds. On the contrary, we think that investors may feel greater confidence investing in non-redeemable investment funds on the basis that these funds are subject to similar core protections and operational requirements as those applicable to mutual funds. Moreover, managers of non-redeemable investment funds will have greater clarity and certainty on the types of activities that are permissible, prior to structuring their non-redeemable investment fund offerings and filing a prospectus, which we believe will increase market efficiency.

Part V – List of commenters

Commenters

- AGF Investments Inc.
- Alternative Investment Management Association (AIMA)
- Arrow Capital Management Inc.
- Artemis Investment Management Limited
- Aston Hill Capital Markets Inc.
- Blackheath Fund Management Inc.
- BlackRock Asset Management Canada Limited
- Blake, Cassels & Graydon LLP
- Borden Ladner Gervais LLP
- Brompton Funds Limited
- Canadian Advocacy Council for Canadian CFA Institute Societies, The
- Canadian Foundation for Advancement of Investor Rights (FAIR)
- Canadian Securities Institute, The (CSI)
- Canadian Securities Lending Association (CASLA)
- Canoe Financial LP
- CI Investments Inc.
- Cymbria Corp.
- Faircourt Asset Management Inc.
- Fasken Martineau DuMoulin LLP
- Fidelity Investments Canada ULC
- First Asset Investment Management Inc.
- Front Street Capital
- GD-1 Management Inc. and Global Digit II Management Inc.
- Harvest Portfolios Group Inc.
- IFSE Institute, The
- Investment Funds Institute of Canada, The (IFIC)
- Investment Industry Association of Canada, The (IIAC)
- Man Investments Canada Corp.
- Mark Brown

- McCarthy Tétrault LLP
- McMillan LLP
- Middlefield Group
- Morgan Meighen & Associates Limited
- Osler, Hoskin & Harcourt LLP
- Periscope Capital Inc.
- Private Mortgage Lenders Forum
- Propel Capital Corporation
- Quadravest Capital Management Inc.
- RBC Capital Markets
- RBC Global Asset Management Inc.
- ROI Capital
- Stikeman Elliott LLP
- Stikeman Elliott LLP (on behalf of 42 organizations)
- Stikeman Elliott LLP (on behalf of BMO Capital Markets, CIBC, National Bank Financial, RBC Capital Markets, Scotiabank and TD Securities)
- Strathbridge Asset Management Inc.
- TMX Group Limited
- Trez Capital Fund Management Limited Partnership
- W.A. Robinson Asset Management Ltd.
- Wildeboer Dellelce LLP