Mutual Funds

Notice
National Instrument 81-102
Companion Policy 81-102CP

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**NOTICE OF RULE AND POLICY UNDER
THE SECURITIES ACT
NATIONAL INSTRUMENT 81-102
AND COMPANION POLICY 81-102CP
MUTUAL FUNDS
AND NOTICE OF REVOCATION OF
CANADIAN SECURITIES ADMINISTRATORS NOTICE
AND RESCISSION OF
NATIONAL POLICY STATEMENT NO. 34
AND
NATIONAL POLICY STATEMENT NO. 39**

Notice of Rule and Policy

The Commission has, under section 143 of the *Securities Act* (the "Act"), made National Instrument 81-102 Mutual Funds (the "National Instrument") as a Rule under the Act, and has adopted Companion Policy 81-102CP Mutual Funds (the "Companion Policy") as a Policy under the Act.

The National Instrument and Companion Policy are both initiatives of the Canadian Securities Administrators (the "CSA"). The National Instrument has been, or is expected to be, adopted as a rule in each of British Columbia, Alberta, Manitoba, Ontario and Nova Scotia, a Commission regulation in Saskatchewan, and a policy in all other jurisdictions represented by the CSA. The Companion Policy has been, or is expected to be, implemented as a policy in all of the jurisdictions represented by the CSA.

The National Instrument and the material required by the Act to be delivered to the Minister of Finance were delivered on November 12, 1999. If the Minister does not approve the National Instrument, reject the National Instrument or return it to the Commission for further consideration by January 11, 2000, or if the Minister approves the National Instrument, the National Instrument will come into force, pursuant to section 20.1 of the National Instrument, on February 1, 2000. The Companion Policy will come into force on the date that the National Instrument comes into force.

The CSA published drafts of the National Instrument (the "1999 Draft Instrument") and Companion Policy (the "1999 Draft Policy") in March 1999.[1] The instruments had been previously published for comment in June 1997.[2]

During the comment period on the 1999 Draft Instrument and the 1999 Draft Policy, which ended on May 18, 1999, the CSA received a number of submissions. The comments provided in these submissions have been considered by the CSA and the final versions of the National Instrument and Companion Policy being published with this Notice reflect the decisions of the CSA in this regard.

Appendix A of this Notice lists the commenters on the 1999 Draft Instrument and the 1999 Draft Policy and Appendix B provides a summary of the comments received and the response of the CSA.

[1] In Ontario, at (1999) 22 OSCB (Supp).

[2] In Ontario, at (1997), 20 OSCB (Supp2).

Revocation of National Policy Statements and CSA Notice

Effective the date that the National Instrument comes into force, National Policy Statement No. 34, entitled "Unincorporated Issuers: Requirements to Maintain a Register of Security Holders", and National Policy Statement No. 39, entitled "Mutual Funds", will be rescinded and the CSA Notice entitled *"Mutual Funds: Section 16 Sales Communications"* (CSA #93/5) will be revoked. These policy statements and the CSA notice are replaced or superseded by the matters contained in the National Instrument and Companion Policy.

Background

This Notice summarizes in a general manner the changes made in the National Instrument and Companion Policy from the 1999 Draft Instrument and 1999 Draft Policy. As described above, Appendix B to this Notice outlines the comments received in respect of the 1999 materials, together with CSA responses.

The CSA received a number of comments, in connection with the drafts of the National Instrument and Companion Policy published both in 1997 and March 1999 on the need for change in the following seven areas:

- Use of swap instruments by mutual funds;
- Securities lending by mutual funds and the use of repurchase agreements by mutual funds;
- Standardized regime for the structure of so-called “funds of funds”;
- Timing of transfers among financial institutions and among mutual funds;
- Principal trading in securities between mutual funds and entities related to the manager of the mutual fund;
- Acquisition of securities by mutual funds from underwriters related to the mutual fund manager; and
- Inter-fund trading of securities.

The CSA have decided to permit mutual funds to directly use swaps and the National Instrument contains the rules in this regard.

The CSA have considered the comments on the other areas listed above and have decided not to make changes to the National Instrument in those areas at the present time. The CSA propose that these issues be addressed as part of a parallel process that will enable sufficient public comment and industry consultation regarding any revised rules. The CSA propose to publish proposed rules as amending instruments to the National Instrument to deal with these issues. The CSA consider that their anticipated process of dealing with these significant comments will permit appropriate regulatory and public consideration of the issues, as well as permit the timely replacement of National Policy Statement No. 39 ("NP39"), through the finalization of the National Instrument in advance

of finalizing the appropriate regulatory response to these significant comments.

Substance and Purpose of National Instrument and Companion Policy

The National Instrument is designed to replace NP 39 and will regulate all publicly offered investment funds that fall within the definition of "mutual fund" contained in Canadian securities legislation. Accordingly, all publicly offered investment funds that give investors the right to redeem securities on demand at a price based on the net asset value of those securities will be required to comply with the National Instrument. Specialized mutual funds such as labour sponsored investment funds, mortgage funds and commodity pools will generally be required to comply with the National Instrument and also applicable securities regulation that is in addition to, or in partial substitution for, the provisions of the National Instrument.

The purpose of the Companion Policy is to state the views of the CSA on various matters relating to the National Instrument.

Summary of Changes to National Instrument from 1999 Draft Instrument

This section describes changes made in the National Instrument from the 1999 Draft Instrument except that changes of a minor nature, or those made only for purposes of clarification or drafting reasons, are generally not discussed. For a detailed summary of the contents of the 1999 Draft Instrument, reference should be made to the Notice published with that instrument. As the changes to the National Instrument from the 1999 Draft Instrument are not material, the National Instrument is not subject to a further comment period.

The majority of changes were made in response to comments received; others were made as the result of further consideration of the applicable rules by the CSA.

Section 1.1

The definitions of *"approved credit rating"* and *"approved credit rating organization"* have been amended to recognize Duff & Phelps Credit Rating Co. as an approved credit rating organization and to include, as approved credit ratings, that organization's ratings for commercial paper/short term debt and long term debt. The ratings included are those considered by the CSA to be equivalent to the rating levels of other organizations already contained in the definition of *"approved credit rating"*.

The definition of *"fundamental investment objectives"* has been amended to remove from the definition the inclusion of the phrase "whether the mutual fund is managed to constitute foreign property under the ITA". The CSA state, in section 2.5 of the Companion Policy, their view that whether a mutual fund's securities are foreign or non-foreign property under the Income Tax Act (Canada) ("ITA") is linked to the fundamental investment objectives of the mutual fund as a matter of interpretation. For this reason, this reference has been removed from the definition in the National Instrument.

A definition of *"index mutual fund"* has been added to refer to a mutual fund whose fundamental investment objectives require it to hold securities, or invest, in a manner that replicates a specified widely quoted market index. The definition is used in subsection 15.3(3) to exempt young index mutual funds from a prohibition concerning the content of its sales communications applicable generally to young mutual funds. See the discussion on that subsection in this Notice for further information.

The definition of *"investor fees"* has been amended to clarify that the definition only pertains to fees, charges and expenses payable to the mutual fund organization in which an investor invests. The change was made to clarify that the definition does not include sales commissions paid to participating dealers. The definition also clarifies that it does not include fees, charges and expenses paid to a member of the organization of the mutual fund acting solely as a participating dealer.

Section 2.1

Subsection 2.1(1) has been amended to clarify that the prohibition contained in that section is triggered by the entering into of a specified derivatives transaction or the purchase of index participation units, in addition to the purchase of a security of an issuer. Subsection (3) has been amended to clarify that it is operative only in respect of long positions of the mutual fund in specified derivatives.

Section 2.5

Subsection 2.5(1)(b) has been amended by an inclusion of a reference to incentive fees to clarify that there may be no duplication of incentive fees in arrangements in which a mutual fund invests in the securities of another mutual fund. The change was made to remove ambiguity over whether incentive fees were included in the prohibition against duplication of management fees.

Section 2.6

Section 2.6 has been amended in two ways.

First, subparagraph (a)(i) has been amended to permit a mutual fund to borrow cash or provide a security interest in order to permit it to settle portfolio transactions, so long as after the borrowing, the outstanding amount of all borrowing by the mutual fund does not exceed five percent of its net assets. The CSA have made this change to recognize a procedure that has developed in the industry and that is considered necessary to permit timely and smooth settlement of portfolio transactions.

Second, the language of section 2.6 has been changed to apply generally to "security interests" granted by a mutual fund, rather than encumbrances or specific types of security interests. The CSA believe that the principles contained in the section should apply to all security interests, regardless of the type of security interest that is used in a given context. The CSA have added a provision to permit only those security interests in a specified derivative transaction that are made in accordance with industry practice for the relevant type of transaction and relate only to obligations under particular specified derivatives positions. These changes reflect existing practice and the existing views of the CSA on what was implied by NP39.

Section 2.7

Subsection 2.7(4) has been amended to clarify that the specified derivatives counterparty limit rule contained in that subsection applies only in respect of the exposure of a mutual fund to a counterparty, and therefore does not include the exposure of a counterparty to a mutual fund under the specified derivatives positions.

Section 2.11

Section 2.11 has been amended to provide that the exemption from the notice requirement contained in that section is available if each simplified prospectus of the mutual fund has contained the required disclosure since the later of January 1, 1994 and its inception. The provision formerly required that disclosure since the inception of the mutual fund. The CSA recognize that the former approach did not work well for mutual funds that were in existence before the advent of the derivatives regime introduced in NP39 in 1992.

Section 4.4

The liability regime contained in section 4.4 has been amended in two ways.

First, subsections (1) and (2) have been amended to provide that a manager of a mutual fund is responsible only for its own failure, or the failure of any person or company retained by it or by the mutual fund to discharge any of the manager's responsibilities to the mutual fund, to exercise the prescribed standard of care. The version of section 4.4 contained in the 1999 Draft Instrument would have had the manager liable for the failure of any person or company providing services to the mutual fund or to the manager in connection with the mutual fund to satisfy the standard of care. This approach could have made the manager liable for matters outside its own area of responsibility, which the CSA consider inappropriate.

Second, subsection (5) has been amended to provide that a director of a mutual fund is not subject to the liability regime contained in section 4.4. Directors are subject to the liability regime imposed by the relevant corporate legislation.

Section 5.6

Paragraph 5.6(1)(b) has been amended to add references to tax-deferred transactions under the ITA into which mutual funds may enter, in addition to "qualifying exchanges" under section 132.2 of the ITA. The CSA are satisfied that any tax-deferred transaction entered into by two mutual funds under the ITA is acceptable for the purposes of subsection 5.6(1), subject to satisfaction of the other conditions contained in that subsection.

Section 6.1

Section 6.1 has been amended in two ways.

First, subsection 6.1(2) has been amended to provide that a sub-custodian or custodian outside of Canada may be retained if appropriate to facilitate portfolio transactions of the mutual fund outside Canada. The 1999 Draft Instrument would have permitted such a retention only if "required to execute" transactions outside of Canada. The CSA do not wish to impose an overly onerous standard concerning the appointment of non-Canadian custodians or sub-custodians, and have therefore returned to the wording now contained in NP39 in this regard.

Second, subsection (6) has been added to clarify that a manager of a mutual fund shall not act as custodian or sub-custodian of the mutual fund. The CSA have included this provision to reflect existing CSA policy, which is to have the portfolio assets held by an entity other than the manager; without subsection (6), the National Instrument would have operated to permit the manager to act as custodian.

Sections 6.2 and 6.3

Each of these sections contains a requirement permitting certain entities to act as custodian or sub-custodian of a mutual fund if its shareholders' equity, as reported in its most recent audited financial statements, exceeds certain prescribed amounts. These requirements have been amended to remove the provision that this test must be based on financial statements that have been made public. The CSA recognize that some custodians are not required to make their financial statements public; for instance, some custodians are members of a larger corporate group that do not make public segregated financial statements pertaining only to the custodian.

Section 6.4

This section has been amended in two ways.

First, the section has been amended to permit a custodian or sub-custodian agreement to provide for the granting of a security interest by a mutual fund to secure the obligations of the mutual fund to repay borrowings by the fund from a custodian or sub-custodian for the purpose of settling portfolio transactions. This change corresponds to the change to section 2.6 described above.

Second, the section has been amended to permit a custodian or sub-custodian to charge a mutual fund a safekeeping and administrative services fee arising on the transfer of portfolio assets of the mutual fund.

Both these changes are designed to recognize commercial realities and existing practice.

Section 6.5

Section 6.5 has been amended to permit a mutual fund to pay a safekeeping and administrative services fee to a custodian or sub-custodian arising on the transfer of portfolio assets of the mutual fund. This change corresponds to the change described above in relation to section 6.4.

Section 6.6

This section has been amended to remove the provision that prevented a custodian or sub-custodian from being indemnified by a mutual fund unless the mutual fund had reasonable grounds to believe that the action or inaction of the custodian or sub-custodian that led to the claim was in the best interests of the mutual fund. The CSA recognize that custodians and sub-custodians typically act on instructions

from the mutual fund or the manager and do not consider whether given instructions are in the best interests of the mutual fund. Therefore, the National Instrument imposes a requirement that custodians and sub-custodians not be negligent in carrying out their duties, but not a requirement that any indemnification of their actions be contingent on whether or not the mutual fund has reasonable grounds to believe they acted in the best interests of the mutual fund.

Section 6.8

Subsection 6.8(3) has been amended to provide that a mutual fund may deposit with its counterparty portfolio assets over which it has granted a security interest in connection with a particular specified derivatives transaction. This change represents an exemption from the otherwise applicable custodian provisions, and corresponds to the change to section 2.6 that permits the mutual fund to grant such a security interest.

Section 9.2

Paragraph 9.2(a) has been amended to provide that a mutual fund has one business day to decide whether to reject a purchase order, rather than 24 hours. The one business day requirement is more workable in connection with purchase orders received before weekends or holidays.

Section 9.4

Subsection 9.4(4) has been amended to ensure that the provisions applicable to cheques that are not honoured are also applicable in the case of other forms of payment that are not honoured.

In addition, subsection (4) now provides that a redemption required by that subsection shall be processed as if the redemption order was received on the fourth business day, rather than the third business day, after the pricing date of the original sale order. This change was necessary to tie properly to the provision that specifies that such a redemption is required only if payment on the relevant purchase order is not made on or before the third business day after the pricing date.

Sections 11.1 and 11.2

Paragraphs 3(c) of sections 11.1 and 11.2 have been amended. Those paragraphs set out the purposes for which a dealer holding client funds may withdraw those funds from the relevant trust account. The paragraphs have been amended to provide that the funds may be withdrawn to pay, among other things, fees, charges and expenses payable by an investor in connection with purchase, conversion, holding, transfer or redemption of the relevant securities. The paragraphs no longer make reference to using the funds to pay for "investor fees". This change, together with the clarification to the definition of "investor fees" described above, clarifies that funds in a trust account may be withdrawn to pay any fees owing by the investor in connection with a mutual fund investment, including fees owed to a participating dealer.

Section 12.1

Paragraph 12.1(2)(b) has been amended to provide that the compliance report relating to the principal distributor of a mutual fund may be prepared by the auditor of the principal distributor or by the auditor of the mutual fund.

Section 14.1

Section 14.1 has been amended by the addition of paragraph (b), which permits a mutual fund to set as the record date for a dividend or distribution the last day on which the net asset value per security is calculated before the day on which the net asset value per security is calculated for purposes of the dividend or distribution. This change has been made to accommodate existing practice and to clarify an ambiguity in the corresponding provision of NP39.

Section 15.2

Subsection 15.2(2) has been amended to provide that performance data and disclosure specifically required by the National Instrument to be included in a written sales communication must be in at least 10-point type. The 1999 Draft Instrument required all of the text in a written sales communication to be in at least 10-point type. This change relieves mutual fund organizations and distributors from any extra expense associated with purchasing more advertisement space in order to accommodate the proposed requirements of the 1999 Draft Instrument, but ensures that some of the most important information contained in a sales communication is presented in at least 10-point type in order that the information be more clearly presented to investors.

Section 15.3

Section 15.3 has been amended in three ways.

First, subsection (1) has been amended to provide greater flexibility in the preparation of sales communications that involve comparison of the performance of a mutual fund or asset allocation service with a benchmark. Paragraph (d) of the 1999 Draft Instrument provided that such a comparison could be made only if the benchmark existed and was widely available during the period for which the comparison was made. Paragraph (d) has been amended to permit the comparison of the performance of a mutual fund or asset allocation service with a benchmark that did not exist for all or part of the relevant period, so long as a reconstruction or calculation of what the benchmark would have been during that period, calculated on a basis consistent with its current basis of calculation, is widely recognized and available. This change has been made to recognize that in the case of some new benchmarks, such as the S&P/TSE 60 Index, the preparers of the benchmarks have made generally available calculations of what the benchmark would have been prior to its introduction.

Second, subsection (3) is new, and exempts young index mutual funds from the prohibition of not disclosing the performance of a benchmark during the period for which other young mutual funds are not permitted to publish performance data. The CSA are satisfied that the publication of the performance of the index on which the investments of a young index mutual fund are based is appropriate and not subject to abuse, so long as the index satisfies the rules applicable to benchmarks.

Third, subsection (4) has been amended to provide that a sales communication that provides performance ratings or ranking for a mutual fund or asset allocation service shall provide the relevant rating or ranking for each period for which standard performance data is required to be given. This change is designed to prevent sales communications from "cherry picking" rankings for a mutual fund, and is consistent with the approach of the National Instrument relating to the presentation of performance data.

Section 15.4

Section 15.4 has been amended through changes to the mandated warning disclosure contained in that section. The CSA have attempted to make the required disclosure simpler, shorter and more understandable for the average investor.

In connection with these changes, subsection 15.4(11) of the 1999 Draft Instrument has been deleted. That provision would have required a shorter form of warning than was otherwise required in the case of certain types of sales communication. The CSA have deleted this provision on the basis that the new required forms of disclosure are now simpler and shorter than in the 1999 Draft Instrument or in NP39.

Section 15.5

Section 15.5 has been amended in three ways.

First, subsection (1) has been amended to provide that a mutual fund shall not be described as a "no load" fund if investor fees are payable by an investor on a purchase or redemption of the securities of the mutual fund, or if fees, charges or expenses are payable by an investor to a participating dealer named in the sales communication. This approach is consistent with the approach now contained in NP39. The 1999 Draft Instrument would have prevented a mutual fund from being described as a "no load" fund if sales commissions were charged by participating dealers that were independent of the mutual fund organization. The CSA did not intend this result, and have amended the definition of "investor fees" and amended subsection 15.5(1) accordingly.

Second, subsection (2) has been amended to require that a sales communication for a "no load" mutual fund disclose that management fees and operating expenses are paid by the mutual fund. The 1999 Draft Instrument would have required a summary of those fees, and the CSA have decided that that approach is excessive in the circumstances.

Third, subsection (3) has been amended in a manner similar to subsection (2). Subsection (3) requires that a sales communication containing a reference to the existence or absence of fees or charges, other than the disclosure required by section 15.4 or a reference to the term "no load", shall disclose the types of fees and charges that exist. The 1999 Draft Instrument required disclosure of a summary of the fees and charges that exist.

Section 15.6

Section 15.6 has been amended to permit sales communications for young mutual funds to contain performance data for those funds if they are sent to securityholders of a mutual fund or participants in an asset allocation service under common management with the mutual fund or asset allocation service. This subsection already permitted such materials to go to securityholders of the young mutual fund. The change has been made to recognize that mutual fund organizations with multiple funds will prepare one document containing performance information about all the funds to be sent to all securityholders of all the funds.

Section 16.1

Section 16.1 has been amended in three ways.

First, subsections (3) and (4) have been amended to apply to all non-optional fees, charges and expenses paid in connection with the holding of securities of a mutual fund, rather than only to management fees. This change has been made to ensure that all such fees, charges and expenses payable directly by investors are taken into account for purposes of calculating management expense ratio.

Second, subsection (5) has been changed in an analogous way, in order to provide that all mutual fund expenses rebated by a manager or a mutual fund to a securityholder, rather than only management fees, are properly taken into account in the calculation of management expense ratio.

Third, subsections (7) and (8) have been added to clarify the calculation of management expense ratio in cases of financial years that are less than 12 months. Subsection (7) provides that the phrase "financial year" used in subsection (1) includes a period other than 12 months for which an issuer is required by securities legislation to prepare audited financial statements. Subsection (8) provides that the management expense ratio of a mutual fund for a financial year of less than 12 months shall be annualized. This approach is consistent with the approach taken in National Policy Statement No. 36 and carried forward into National Instrument 81-101 Mutual Fund Prospectus Disclosure. Section 16.1 continues to provide that the calculation of management expense ratio must be based on expenses shown for a financial year; mutual funds may not disclose a management expense ratio for less than a financial year, thereby ensuring that its management expense ratio will be based on total expenses derived from audited financial statements.

Section 18.1

Section 18.1 has been amended by the removal of the requirement that a mutual fund maintain records "for at least as long as the mutual fund is in existence". The CSA are satisfied that the length of time that a mutual fund maintains records is an issue properly left to the business judgment of the organization, having regard to limitation periods and statutory and other common law requirements.

Section 18.2

Section 18.2 has been amended to clarify the purposes for which a securityholder list may be obtained, in order to conform more closely with corporate legislation. The provision now provides that a list may be requested for a matter relating to the relationships among the mutual fund, the members of the organization of the mutual fund, and the securityholders, partners, directors and officers of those entities. This parallels the corporate provisions that provide that shareholder lists may

be obtained for a matter relating to the "affairs" of an issuer, which is defined as the relationship among a corporation, its affiliates and shareholders and the officers and directors of such bodies corporate.[3]

Part 20

Part 20 has been amended to include the relevant dates relating to the implementation of the National Instrument and various dates relating to transitional matters.

Section 20.1 provides that the National Instrument comes into force on February 1, 2000.

Section 20.2 permits sales communications printed before December 31, 1999 to be used until August 1, 2000, despite any requirements in the National Instrument.

Subsection 20.5(1) provides that subsection 4.4(1) of the National Instrument does not come into force until August 1, 2000; this gives mutual fund organizations six months to ensure that all relevant agreements conform with the requirements of that subsection. Subsection 20.5(2) provides that subsections 2.4(2), 2.7(4) and 6.4(1) do not come into force until February 1, 2001; this gives mutual fund organizations one year from the date of the coming into force of the rest of the National Instrument to put systems in place to monitor compliance with subsections 2.4(2) and 2.7(4) and to ensure that agreements with custodians and sub-custodians comply with the requirements of subsections 6.4(1) and 6.8(4).

Appendix A

A number of generally recognized exchanges have been added to Appendix A.

Summary of Changes to the Companion Policy from the 1999 Draft

This section describes the changes made in the Companion Policy from the 1999 Draft Policy. For a detailed summary of the 1999 Draft Policy, reference should be made to the Notice published with that policy. Changes of a minor nature, or those made for drafting or clarification reasons or to conform the Companion Policy to the National Instrument are not discussed in this section.

Section 2.5

Section 2.5 has been expanded to discuss the meaning of the definition "fundamental investment objectives" and its relationship to the disclosure of the fundamental investment objectives of a mutual fund in a simplified prospectus under National Instrument 81-101 and Form 81-101F1. Section 2.5 explains that the definition in the National Instrument is designed to refer to the disclosure of fundamental investment objectives made under National Instrument 81-101, and that a change to the mutual fund requiring a change to that disclosure will require securityholder approval under National Instrument 81-102. Section 2.5 also states that views of the Canadian securities regulatory authorities that whether the securities of a mutual fund are foreign property under the ITA is linked to the fundamental investment objectives of the mutual fund, and that a change in the method by which the mutual fund is managed that changes that status would be likely due to a change in the fundamental investment objectives of the mutual fund.

Section 2.9 of the 1999 Draft Policy

This section, which discussed the definition of "investor fees" has been deleted in conjunction with the amendments to that definition in the National Instrument.

Section 2.13 (Section 2.14 of the 1999 Draft Policy)

Paragraph 4 of subsection 2.13(3) has been added to provide a further example of a circumstance that the Canadian securities regulatory authorities would generally not consider to be a "purchase" of a security by a mutual fund. This paragraph refers to the decision of a mutual fund not to tender into an issuer bid, even though its decision is likely to result in an increase in its percentage holdings of a security beyond what the mutual fund would be permitted under the National Instrument to purchase.

Section 3.3

A reference to section 2.1 of the National Instrument has been added to this section to emphasize that investments in "quasi-mutual funds" or index participation units by mutual funds are subject to all of the investment restrictions of the National Instrument, including section 2.1.

Section 4.2

Paragraph 4 of section 4.2 has been added to clarify the operation of the commodity futures legislation of Ontario in connection with a non-resident sub-adviser advising in respect of a mutual fund using futures.

Section 4.4

Section 4.4 has been added to clarify that the definition of "cash cover" includes interest accrued on the securities or other portfolio assets used for cash cover purposes.

Section 7.2 of the 1999 Draft Policy

This section has been deleted in conjunction with the expansion of the discussion of the term "fundamental investment objectives" in section 2.5 of the Companion Policy.

Section 7.2

Section 7.2 has been amended by the deletion of subsection (2), which noted the need for separate approvals for certain transactions in Quebec. The CVMQ is proceeding to take steps to make such approvals unnecessary following the implementation of the National Instrument.

[3] See for example, the definition of "affairs" in section 2(1) of the *Canada Business Corporations Act*.

Section 11.1

Subsection 11.1(6) has been added to discuss the status of non-interest bearing trust accounts maintained under sections 11.1 or 11.2 of the National Instrument.

Section 12.1

Section 12.1 is new and discusses subsection 13.1(4) of the National Instrument. Section 12.1 emphasizes that the Canadian securities regulatory authorities expect mutual funds to calculate their net asset value per security as quickly as commercially practicable and to make the results of that calculation available to the financial press as quickly as is commercially practicable.

Section 14.1

Section 14.1 is new and states the views of the Canadian securities regulatory authorities on matters concerning management expense ratio calculations. The section emphasizes that the rules of calculation of management expense ratio contained in the National Instrument are applicable regardless of the context in which a mutual fund discloses its management expense ratio. The section also discusses issues relating to the determination of "total expenses" used in the calculation of management expense ratio.

Section 15.1

Section 15.1 discusses section 18.1 of the National Instrument, and states that it is up to a mutual fund, having regard to prudent business practice and any applicable statutory limitation periods, to decide how long it wishes to retain securityholder records required by this section.

Section 16.1

Section 16.1 has been amended by the deletion of subsections (2) and (3) of the 1999 Draft Policy. Those subsections dealt with the need for additional applications in Quebec, which will not be necessary following the implementation of the National Instrument in Quebec.

National Instrument and Companion Policy

The texts of the National Instrument and Companion Policy follow.

Regulation to be Amended - Ontario

In Ontario, the Ontario Commission has amended section 240 of Regulation 1015 of the Revised Regulations of Ontario, 1990, in conjunction with the making of the National Instrument as a rule in Ontario, by replacing, whenever appearing, references to the words "policy or practice" with the words "rule, policy or practice".

Text of Revocation of CSA Notice

The text of the revocation of the CSA Notice described in this Notice is as follows:

> "The CSA Notice entitled *"Mutual Funds: Section 16 Sales Communications"* (CSA #93/5) is revoked effective at the time that National Instrument 81-102 Mutual Funds comes into force."

Text of Rescission of National Policy Statement No. 34 and National Policy Statement No. 39

National Policy Statement No. 34 and National Policy Statement No. 39 are to be replaced by the National Instrument and accordingly will be rescinded.

The text of the rescission of National Policy Statement No. 34 is:

> "National Policy Statement No. 34, entitled "Unincorporated Issuers: Requirement to Maintain a Register of Security Holders", is rescinded, effective at the time that National Instrument 81-102 Mutual Funds comes into force."

The text of the rescission of National Policy Statement No. 39 is:

> "National Policy Statement No. 39, entitled "Mutual Funds", is rescinded, effective at the time that National Instrument 81-102 Mutual Funds comes into force."

DATED: November 12, 1999.

APPENDIX A
LIST OF COMMENTERS ON
NATIONAL INSTRUMENT 81-102 AND
COMPANION POLICY 81-102CP

1 AGF Management Ltd.
2. Duff & Phelps Credit Rating Co. (2 submissions)
3. Fasken Campbell Godfrey
4. Fidelity Investments Canada Limited
5. Global Strategems (Michael Barrett, Managing Editor)
6. Investors Group
7. Osler, Hoskin & Harcourt
8. PricewaterhouseCoopers
9. Royal Bank of Canada, Royal Trust and Royal Mutual Funds Inc.
10. TD Asset Management Inc.
11. The Association of Global Custodians
12. The Investment Funds Institute of Canada (IFIC)
13. Trimark Investment Management Inc.

APPENDIX B
SUMMARY OF COMMENTS RECEIVED ON
NATIONAL INSTRUMENT 81-102 AND
COMPANION POLICY 81-102CP AND
RESPONSE OF THE CANADIAN SECURITIES ADMINISTRATORS

1. INTRODUCTION

The CSA published drafts of National Instrument 81-102 (the "National Instrument") and Companion Policy 81-102CP (the "Companion Policy") in March 1999[4]. The instruments published in March 1999 are called the "1999 Draft Instrument" and "1999 Draft Policy" in this Appendix. The instruments had been previously published for comment in June 1997.[5]

During the comment period on the 1999 Draft Instrument and the 1999 Draft Policy, which ended on May 18, 1999, the CSA received 14 submissions from 13 commenters. The commenters can be grouped as follows:

Mutual fund management companies:	7
Stock exchanges and rating agencies:	1
Accounting firms:	1
Law firms:	2
Trade Associations:	2
TOTAL:	**13**

The two trade associations listed each made submissions in respect of the 1999 Draft Instrument and the 1999 Draft Policy on behalf of their respective members.

The comments provided in these submissions have been considered by the CSA and the final versions of the National Instrument and Companion Policy being published with this Notice reflect the decisions of the CSA in this regard. The CSA thank all commenters for providing their comments on the 1999 Draft Instrument and the 1999 Draft Policy.

Copies of the comment letters may be viewed at the office of Micromedia, 20 Victoria Street, Toronto, Ontario (416) 312-5211 or (800) 387-2689; the office of the British Columbia Securities Commission, 200-865 Hornby Street, Vancouver, British Columbia (604) 899-6500; the office of the Alberta Securities Commission, 10025 Jasper Avenue, Edmonton, Alberta (403) 427-5201; and the office of the Commission des valeurs mobilières du Québec, Stock Exchange Tower, 800 Victoria Square, 17th Floor, Montréal, Québec.

Many of the commenters provided detailed comments on specific sections of the 1999 Draft Instrument and the 1999 Draft Policy. Some comments were of a very technical, non-substantive nature. The following is a summary of the substantive comments received, together with the CSA's responses and, where applicable, the changes adopted by the CSA. As the changes to the 1999 Draft Instrument and the 1999 Draft Policy were not material, the National Instrument

[4] In Ontario, at (1999) 22 OSCB (Supp).

[5] In Ontario, at (1997), 20 OSCB (Supp2).

and the Companion Policy are not subject to a further comment period.

2. COMMENTS PREVIOUSLY RAISED ON 1997 DRAFT INSTRUMENT AND COMPANION POLICY

A number of commenters provided comments on issues that had previously been raised in connection with the draft instruments published in June 1997. The following is a list of those issues:

- the use of repurchase agreements;
- reducing the equity requirement for sub-custodians from $100 million to $50 million;
- reducing the time for reversing a failed redemption order from T+10 to T+3;
- using a currency other than the Canadian or U.S. dollar for calculating net asset value;
- including receivables from the acceptance of purchase orders for mutual fund securities in the definition of "cash cover";
- eliminating the requirement for unitholder approval for a change of auditor;
- permitting the use of specified derivatives with underlying interests in commodities other than gold.

The CSA reconsidered the comments received with respect to these issues and concluded that their responses have not changed since March 1999. Accordingly, the comments on these issues are not set out in the tabular summary of comments which follows. Reference should be made to the Summary of Comments on the 1999 Draft Instrument and the 1999 Draft Policy for the CSA response to these issues.

3. SUBSTANTIVE COMMENTS ON SPECIFIC PROVISIONS

Note: In this Table, "NI" means National Instrument 81-102 Mutual Funds and "CP" means Companion Policy 81-102CP Mutual Funds; "March 1999 Draft" means the version of the materials published for comment in March 1999; "NP 39" means National Policy Statement No. 39; and "CSA" means the Canadian Securities Administrators.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
1	Definition of "approved credit rating" and "approved credit rating organization"	_____	Duff & Phelps should be included as an approved credit rating organization since it is one of only four credit rating agencies recognized by the SEC (U.S.) as a "nationally recognized statistical rating organization" for rating all types of securities. The company has a presence in Canada in the form of a joint venture relationship with DBRS Inc. to provide ratings and research specifically designed for investors in high yield U.S. dollar denominated Canadian issues.	Change made.
2	Definition of "cash cover'	_____	Commercial paper of an approved credit rating should be included in the definition, particularly since it is already permitted for money market funds by clause (d)(iii) of the definition of "money market fund".	No change at this time. The use of commercial paper will be considered in connection with the CSA's work to permit mutual funds to engage in securities lending.
3	Definition of "cash equivalent"	_____	The definition should be amended to include instruments with a term of 13 months, or 25 months in the case of government obligations, and the dollar weighted term to maturity "not exceeding 90 days" (see definition of "money market fund") should be restored to 180 days instead of 90 days. Long-term instruments provide potential for yield improvement without significantly altering the risk profile of a money market portfolio.	No change. This is a comment that was raised prior to the reformulation process when there was some controversy concerning what is a money market fund. The definition reflects the CSA's understanding of the industry consensus on this issue.
4	Definition of "cash equivalent"	_____	The definition should be expanded to include commercial paper (with an "approved credit rating"), repurchase agreements and money market funds. Even if repurchase agreements and commercial paper are not included, money market funds should be included even if they invest in commercial paper and repurchase agreements. The reason for this is that the inter-position of a money market fund changes and enhances the stability and liquidity of the investment beyond the characteristics of the fund's own investment holdings.	No change. Repurchase agreements will be addressed as part of a parallel amending process. The use of money market funds will be considered as part of the review of fund on fund investments. The CSA has concerns about the implications of a "top fund" which uses derivatives investing up to 80% or 90% of its assets in a related money market fund. Any changes in these areas will be made as amendments to the NI. No change with respect to commercial paper (see comment re "cash cover" above).
5	Definition of "conventional convertible security"	_____	An essential element of a conventional convertible security is that the rate or formula for conversion or exchange is fixed by the terms of the convertible security. Otherwise, any exchange or trade of a security (including those at market rates) would be caught by the definition. Such an exchange is not a convertible security, conventional or otherwise. Nonetheless, it should also be clear that they do not constitute "specified derivatives".	Change made. The words "according to its terms" have been added to the definition.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
6	Definition of "dealer managed mutual fund" and "dealer manager"	_____	It is not clear whether these definitions recognize funds with third party advisers (i.e. without a "specified dealer" in the chain) as dealer-managed.	No change. The CSA will consider this issue in their review of the restrictions imposed on related party transactions. The current wording carries forward the requirements of NP 39.
7	Definition of "debt-like security"	_____	It is not clear whether equity-linked GICs and/or linked notes fall within the parameters of the definition. Section 2.4 of the CP should be amended to provide more clarification.	No change. The CSA believe that the definition is clear. Whether a particular investment fits within the definition will depend on the facts as applied to the test in the definition.
8	Definition of "fundamental investment objectives"	_____	The definition does not clearly distinguish between investment objectives and investment strategies. The definition should be amended to clearly distinguish between objectives and strategies to ensure that unnecessary unitholder meetings (which are costly, time consuming and almost invariably poorly attended) are not required. As a result, some funds may provide more general disclosure of their investment objectives in order to avoid having to call unnecessary meetings. With respect to whether the fund is managed to constitute non-foreign property under the ITA, will relief be granted to permit changes to currently disclosed fundamental investment objectives?	Changes made. The CP has been amended to refer to the disclosure requirements of NI 81-101 and Form 81-101F1 which recognizes the difference between investment objectives and investment strategies. Examples of fundamental investment objectives are provided in the CP. The reference to management of a mutual fund so as to constitute foreign property has been removed from the definition since it was but one example of a fundamental investment objective. The CP has been amended to state that the CSA are of the view that whether securities of a mutual fund are foreign property under the ITA is linked to the fund's fundamental investment objectives. The NI does not require change in current fundamental investment objectives of a mutual fund. If a fund is currently being managed to be non-foreign property then that is part of the fundamental investment objectives of that fund.
9	Definition of "hedging"	_____	A threshold of "high" degree in relation to the stated variables should be specified.	No change. See subsection 2.7(1) of the CP.
10	Definition of "index participation units"	_____	The definition appears to preclude the use of index participation units which track an index and employ indexation strategies other than replication of the composition of the index.	Change made. Clause (b) added to provide for strategies that replicate performance of an index.
11	Definition of "investor fees"	_____	Does the definition include all fees applied by the fund manufacturer or must this definition contemplate **all** possible fee expenses that could be applied by a broker/dealer and/or a financial planner?	Definition amended for clarity.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
12	Definition of "mutual fund conflict of interest investment restrictions"	_____	Part (b) of the definition could be problematic since it prevents the crossing of securities. For example, it would preclude a fixed income portfolio manager from buying a bond and then, as it nears maturity, cross the securities to a shorter term bond fund, and in turn crossing the security to a money market fund as it approaches maturity. This type of transaction should be permissible if executed at fair market value through an independent broker/dealer.	No change. Inter-fund trading not permitted by the securities legislation of several of the provinces. Issue to be addressed as part of parallel amending process.
13	Definition of "permitted supra-national agency"	_____	The European Investment Bank should be included in the definition.	No change. A "permitted supranational agency" must be prescribed under paragraph (g) of the definition of "foreign property" in subsection 206(1) of the ITA. The European Investment Bank has not been prescribed.
14	Definition of "purchase"	_____	A transaction should be considered to be a "purchase" only where securities are acquired as a result of a positive action by a fund and not as a result of a passive incident. The automatic conversion of securities in connection with an amalgamation, merger or other reorganization ought not be considered a "purchase", regardless of how the fund voted in connection with the transaction. To make the characterization of a subsequent conversion dependent on the fund's vote may encourage elements of gamesmanship with respect to voting (i.e. to attempt to ensure 100% conversion without any compliance violation). The definition should be simplified to remove the relevance of voting and to classify all automatic or forced conversions (even those with an element of selection) as not being "purchases"	Change made to section 2.13 of CP to clarify that a transaction would not be a "purchase" if the mutual fund declined to tender into an issuer bid. The CSA recognize that referring to voting may not be a perfect solution but voting is fundamental to decision-making.
15	Definition of "report to security-holders"	_____	The definition should be expanded to include any reports sent to securityholders generally. Quarterly reports would be included in the current definition of "sales communications" and this serves no valid policy objective. The expanded definition should then be excluded from the definition of "sales communication". Such reports are only sent to existing securityholders, are not "primarily promotional" in nature and are still subject to section 15.8 with respect to the use of performance data.	No change. The CSA believe that such quarterly reports should contain the modified warning language (see section 15.4).

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
16	Definition of "significant change"	_____	The proposed change to measure the subjective event of "significant change" by estimating investor perception (as opposed to the view of an issuer in the former definition of "material change") is an onerous task. Is the "investor" of average financial knowledge? Given the varying degree of investor sophistication, fund companies require more guidance and examples of instances where a change would be considered "significant". Part 7 of the CP only provides two examples of what the CSA considers "significant changes". This is not sufficient.	No change. The definition imposes a "reasonable" person test.
17	Definition of "special warrant"	_____	In today's market, "special warrant" can include instruments such as special shares or special units and therefore the definition should be expanded to recognize this.	No change. The CSA do not believe that it is necessary to change the term since what is important is whether the security fits within the definition.
18	Section 2.1	_____	Why are securities issued by U.S. states and governments of other foreign jurisdictions not excluded from the concentration restriction? It is not clear why such securities would not be given the same treatment if the basis for the exclusion is low risk, low volatility and sufficient liquidity. Despite subsection 3.1(3) of the CP, it is not clear why the CSA is not willing to codify the standard exemptions granted to international bond funds. Applications of this type are commonly made, the bases for the applications are usually very similar, orders are routinely issued and are very similar in most cases. Why should an international equity fund not be given the same flexibility as an international bond fund on a discretionary basis (s.3.1(3) of CP)?	No change; provision consistent with NP39. The CSA would consider an application for discretionary relief by mutual funds wishing to deviate from those restrictions due to specialized investment objectives.
19	S. 2.1(3) and (4)	_____	These provisions do not clearly instruct whether the fund should appraise index participation units for asset concentration or not.	Subsection 2.1(1) of the NI and subsection 3.3(2) of the CP have been amended to clarify that the purchase of index participation units is subject to section 2.1 of the NI.
20	S. 2.2	_____	Why is the issue of control for a mutual fund or a group of mutual funds different than for any other market participant? The control restrictions in Canadian securities legislation already contain adequate restriction on aggregate holdings of securities of an issuer through the take-over bid, early warning and insider reporting requirements. The concentration restrictions in s. 2.1 provide the necessary diversification protections to guard the interests of investors. From a control perspective the issue is not how many shares are owned by a particular fund i.e. it is irrelevant if a control position is allocated among a dozen funds or restricted to a single account.	No change. This rule is not addressed to the secondary market but is rather intended to address the management of a mutual fund. The fundamental feature of a mutual fund is that it should not control another issuer. The rule is not intended to address diversification. Diversification is addressed by section 2.1.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
21	S.2.2(2)	_____	Although section 2.14 of the CP contains examples of acquisitions that would not generally be considered "purchases", the list is not exhaustive. The current wording might (inadvertently) catch a situation in which a fund's holdings increase as a result of a decision not to tender to an offer (and other unforeseen circumstances). The process for reducing holdings once the 10% level is reached should be amended to conform with the requirements of section 2.4 concerning "illiquid assets".	Change made to s. 2.13 of CP. If the mutual fund acquires securities pursuant to an issuer bid to which it declined to tender, that acquisition would not be considered a purchase. No change. The CSA believe that the time provided is adequate and appropriate.
22	S. 2.4(2)	_____	The monitoring of a fund's holdings in illiquid assets is typically done on a monthly basis. Therefore, the subsection should be amended to provide that "a mutual fund shall not have invested, as at the first month-end following a period of 90 days, more than 15 percent of its net assets taken at market value, in illiquid assets".	No change. The CSA believe that the time provided is adequate and appropriate.
23	S. 2.5(2)(b)	_____	The clause should be amended to extend the exemption to funds listed on exchanges in the United States and other countries. Such an amendment would be parallel to the rule for index participation units. There does not appear to be any policy reason to restrict mutual funds from investing in closed-end funds listed on a U.S. exchange.	No change. The rule reflects those "quasi mutual fund" entities currently known to the CSA as being potential investments for mutual funds. A problem with this section only arises if the mutual fund wishes to invest in an entity that has a redemption feature.
24	S. 2.6	_____	Mutual funds should be able to purchase, for non-hedging purposes, listed warrants and debt-like securities on margin. Hedge funds are permitted to regularly engage in such transactions. Perhaps the CSA should encourage funds to submit statements or implement modest disclosure arrangements to assist in monitoring these transactions.	No change. The CSA believe that leveraged investing is not appropriate for mutual funds offered by way of prospectus.
25	S. 2.6(a)	_____	This subsection should be amended to permit a mutual fund to borrow money on a short-term basis to settle investment transactions. The purchase and sale of fund securities are typically settled on a "contractual settlement" basis. As a result, it is market practice for a custodian's client accounts to regularly go into overdraft. These overdrafts usually are for very short periods of time. In other words, the custodian advances funds to the mutual fund in order to prevent trades from failing given the difference in settlement times and dates. This advance would constitute a borrowing by the mutual fund. Therefore, the subsection should be amended to include an additional exception as follows: *The transaction is a temporary measure to facilitate the settlement of investment transactions by the custodian or a sub-custodian of the mutual fund.*	Change made. The 5% restriction on amount of all borrowings is aggregate (i.e. includes both redemptions and settlements).

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
26	S. 2.6(a)(ii)	_____	The commentary to the NI states that amendments to this provision were made "in response to comments that mutual funds should be permitted to encumber portfolio assets to effect derivatives transactions instead of being restricted to posting margin". However, the wording of the clause does not appear to meet this objective. The wording "to post margin" is more restrictive than permitting a mutual fund to encumber portfolio assets "to effect derivatives transactions". Subsection 6.8(3) does not use the term margin. The words "to post margin" should be deleted.	Drafting changes made to reflect original intention. The words "encumbrance", and "post margin" have been deleted. Reference is now made to a "security interest". The security interest must relate only to obligations under specified derivatives positions. Clause 2.6(a)(iv) has been deleted.
27	S. 2.7	_____	The three to five year term limit on swaps may reduce the ability of a fund to effectively eliminate or decrease its market or currency risk. Other conditions relating to swaps, particularly those pertaining to eligible counterparties, should alleviate regulatory concerns about extended term limits. To alleviate a counterparty credit risk that may arise from long-term swaps, a current practice is to include a three year mutual put in the swap terms which would permit the mutual fund to put the swap back to the counterparty in three years. Thus the counterparty risk is only three years although the term of the swap is much longer. The Canadian swap market has become mature, highly liquid and active, enabling swaps to be unwound at any time therefore term limits should not be imposed.	No change. The CSA consider that the five year limit is acceptable since, among other things, derivatives with limits exceeding five years are not very prevalent. The CSA believe that any impact on a fund's ability to act will not be material. Furthermore, the CSA does not believe that all segments of the Canadian swap market are highly liquid (eg. equity and commodity swaps).
28	Section 2.10	_____	Section 4.2 of the CP appears to add additional requirements that would severely limit the number of entities eligible to act as sub-advisers for funds that wish to use derivatives. Provided the requirements of s. 2.10 of the NI are satisfied, there is no reason why a credible, established foreign sub-adviser should be required to acquire the specific Canadian registrations or qualifications set out in s. 4.2 of the CP. Section 4.2 of the CP should be deleted so as not to reverse the long-standing policy of Canadian law which has recognized the ability of non-resident advisers to advise on Canadian mutual funds. Both the NI and the CP over-emphasize the difficulties associated with managing funds that employ derivative instruments. Derivative instruments are now a well established part of portfolio management and do not require the degree of focus and special requirements set out in the NI.	No change. Section 4.2 of the CP does not impose any requirements but merely reminds industry participants of registration requirements that exist under securities or commodity futures legislation. The CSA believe that the provisions governing derivative instruments are necessary and appropriate.
29	S. 2.10(1)	_____	It is not clear why the restrictions in this subsection only apply to advice of a non-resident adviser concerning standardized futures and options.	No change. There are registration requirements with respect to investments in options and futures. See section 4.2 of the CP.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
30	S. 2.11(2)	_____	The exemption does not cover funds in existence before NP 39 was amended to permit derivatives, which have disclosed in their most recent SP that they may use derivatives and have previously given unitholders notice of their intention to use derivatives, but have not actually done so to date. Such funds should not be required to provide notice to unitholders again simply because each of its simplified prospectuses since inception have not contained this disclosure.	Change made. Notice not required if SP has contained disclosure concerning the use of specified derivatives since the later of January 1, 1994 and the inception of the fund.
31	S. 4.1(1)	_____	Determining the start of the 60 day period is linked to the time that the relevant securities are out of distribution. In some cases that may be the date of closing of the transaction, but in other cases it may not be until sometime after that date. For example, in a firm commitment offering that is not fully subscribed on the date of closing the unsold securities are taken into the underwriter's inventory after closing and are marked to market. Section 4.1 should be amended to ensure that the 60 day period starts to run at the date of the closing of the transaction. This would be sufficient to adequately safeguard mutual fund investors against potential harms.	No change. The CSA believe that it is appropriate to tie the restriction to the end of the distribution.
32	S.4.4(3)	_____	If this provision is intended simply to deal with the indemnification of the manager of the mutual fund by the mutual fund and not all service providers to the mutual funds then it should be clearly specified. The liability and indemnification scheme should apply to persons or companies retained to perform duties or activities that the manager would otherwise be obligated to perform but not to those providing services used by the manager in performing its services for the mutual fund. The provision should be amended to clearly exclude the trustee of the mutual fund. Common law sets the standard that should be applicable to trustees and it is not necessary for the NI to address specifically the indemnification of trustees. Clarification should also be given regarding the status of directors of mutual funds which are corporations and members of independent advisory boards of mutual funds which are trusts.	Changes made to subsections 4.4(1) and (2) to clarify that the section relates to persons retained by the manager or the mutual fund to discharge any of the manager's responsibilities to the mutual fund. Section 4.4 deals only with the relationship between the manager and the mutual fund. It does not purport to regulate the relationship between a trustee and the fund. Subsection 4.4(5) has been amended so that it does not apply to a director of a mutual fund. The liability and indemnification of directors is addressed by corporate law.
33	S. 5.1(a)	_____	Further clarification is needed on the scope of the obligations intended, particularly with respect to the kinds of changes that would require securityholder approval. Is an "increase" measured in absolute dollars or in percentage terms? Do the words "could result in increases" impose a test based on possibility, reasonable expectation or what is conceivable in a worst case scenario? Examples and elaborations in the CP would assist in interpreting the provision.	No change. The CSA believe that section 6.3 of the CP provides sufficient clarification.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
34	S. 5.1(f)	_____	The requirement for securityholder approval should be subject to a "significant change" test as in s. 5.1(g). A 60 day notice period would be preferable so that if any securityholder did not support a reorganization, despite there being no significant change to the mutual fund or the securityholder's rights, the securityholder could redeem his or her securities.	No change. The CSA believe that securityholders should be able to vote on arrangements that result in the mutual fund in which they originally invested ceasing to exist and the securityholders becoming securityholders of another mutual fund.
35	s.5.1(g)	_____	Despite the definition of "significant change" in section 1.1, the meaning of the term in the context of a merger of mutual funds is highly subjective, and will be very difficult to interpret and apply.	No change. Subsection 7.3(2) of the CP provides guidance.
36	S. 5.3	_____	There should be no difference in the required treatment of an increase in charges to the mutual fund between that required for those mutual funds which are permitted to be described as "no load" and those which are not. In either case, investors are equally affected by non-arms length charges and should be afforded the same protections.	No change. The CSA believe that this distinction is valid because there would be no charge to the unitholder of a no-load fund who chooses to redeem. Section is a carry-over from NP39.
37	S. 5.5(2) and 5.8(1)	_____	Whether there is a change of manager or a change of control of the manager, the substantive result is the same - namely, another (new) organization now operates the mutual fund or group of funds. Accordingly, it seems logically inconsistent that these two types of transactions should be treated differently. Presumably, for the time being, securityholder approval will <u>not</u> be required in relation to a proposed change of control of a manager?	No change. At this time securityholder approval is not required for a change in control of manager, although as noted in the notice published with the March 1999 draft instruments, the CSA remain concerned about the implications to investors of changes in control of managers.
38	S. 5.6(1)(b)	_____	Certain other transactions which do not fall within the meaning of "qualifying exchange" under section 132.2 of the ITA should be exempted from obtaining pre-approval of securities regulatory authorities. These would include mergers of mutual fund corporations which, in the normal course, may be equally, if not more, straightforward than a "qualified exchange". As drafted, the provision would require pre-approval for such transactions. These types of transactions should not require pre-approval therefore the provision should be deleted.	Change made to contemplate other tax-deferred transactions under ITA.
39	S. 5.6(1)(i)	_____	Requiring that redemptions be permitted up to the close of business on the day before the effective date of a merger or conversion could be problematic since a fund company's systems could be legitimately inoperative on that date. Consequently, redemptions received on that date would not be processed.	No change. The CSA note that most mergers mutual funds carried out to date have permitted redemptions up to the close of business of the day before the effective date of the merger.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
40	S. 5.8	_____	The notice requirement may not work in cases where the fund manager is a public company and the target of a hostile take-over bid. The level of prescribed disclosure may entail preparation of an entirely separate disclosure document geared to securityholders of the funds as opposed to shareholders of the current manager to whom the take-over bid circular is directed. A notice to securityholders of the funds summarizing the key elements of the transaction should be sufficient. The notice requirement should be restricted to changes of control as a result of the agreement of the mutual fund manager or its owner. For indirect changes of control, prior regulatory approval should be required instead (which could require advance notice to unitholders in appropriate cases) with notice to unitholders in the next mailing of continuous disclosure material.	No change. It is correct that a separate disclosure document addressed to securityholders of the fund may have to be prepared. An application for an exemption can be made in cases where such requirements may be problematic.
41	S. 6.1(2)(b)	_____	The words "if appropriate to facilitate" in the 1997 Draft have been replaced by the words "if required to execute". Although in most cases foreign investment requires foreign custody, there are countries in which it would be possible to take physical possession of securities certificates and remove them to Canada. It is unclear whether the current words would compel Canadian funds to transport physical certificates in such circumstances. Such a requirement would be ill-advised given related delays and risks which would render such securities significantly less liquid than if they were held in a depository or by a sub-custodian in the relevant jurisdiction.	Change made. There was no intention to change the standard. The words "required to execute" have been deleted and the words "appropriate to facilitate" have been included. The latter phrase is used in NP39.
42	S. 6.1(3)(c)	_____	Confirm that this requirement is satisfied where the agreement between the custodian and the sub-custodian permits the custodian to enforce its contractual rights against the sub-custodian with respect to the portfolio assets held by the appointed sub-custodian.	No change. The mutual fund must be able to require the custodian or the sub-custodian to enforce rights on behalf of the mutual fund.
43	S. 6.1(4)	_____	Confirm that a provision, either in the constating documents of the mutual fund itself (where there is no separate custodian agreement) or in the custodian agreement between the mutual fund and the custodian, which permits the custodian to appoint in its discretion one or more sub-custodians would be sufficient to meet the requirement of this provision.	No change. Subsections 6.1(4) and (5) set out the rules in this regard.
44	S. 6.2 and 6.3	_____	The requirement that the trust company's audited financial statements have to have been made public should be deleted. There are very few trust companies left in Canada which make their financial statements available to the public, except on a consolidated basis.	Change made. The words "that have been made public" have been deleted from sections 6.2 and 6.3.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
45	S. 6.4(3)	_____	It is industry practice for custodian agreements to provide that no encumbrance on the portfolio assets of the mutual fund will be created except for either a good faith claim for payment of the fees and expenses of the custodian or for a claim for payment of any amounts advanced by the custodian to the mutual fund for the purpose of settling transactions. If custodians are not permitted to have a security interest in respect of such advances, custodians would not make the advance and the reality is that the majority of investment transactions would fail. Therefore, the NI should be amended to permit encumbrances for amounts owing in respect of advances made by the custodian to settle transactions.	Change made. Clause 6.4(3)(a) amended to permit security interest in portfolio assets to secure obligations of a mutual fund to repay amounts advanced by the custodian for the purpose of settling portfolio transactions.
46	S. 6.4(3)(b) and S. 6.5(5)	_____	It is common for custodians to charge an administrative and safekeeping fee which includes a charge for processing the receipt of assets into custody or the delivery of assets out of custody. Although such processing occurs as a result of purchases and sales by the mutual fund, these transaction-based fees compensate the custodian for performing a specific service, not for the transfer of beneficial ownership. Such fees have never been regarded as inconsistent with s. 7.01(8) of NP 39 which expressly permits contractual provisions requiring payment of "the fees and expenses of the Custodian or sub-custodian as the case may be for safekeeping and administrative services".	Change made to s. 6.4(3)(b) and s. 6.5(5).
47	S. 6.5(5)	_____	This provision should be deleted. It introduces a prohibition which could prevent a mutual fund from achieving proper ownership of assets in markets where such transfers are beneficial and are only available if fees are paid. Many markets, particularly foreign or emerging markets, have different and changing practices regarding securities trading and settlement. As long as the fees paid by the fund are reasonable and consistent with industry norms, it is in the best interests of the fund to be permitted to make transfers in the same way as other investors may.	No change. The CSA believe that it is appropriate to continue the prohibition in NP39 against the payment of such fees, although the changes referred to above have been made to this subsection.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
48	S. 6.6(3)	_____	Indemnification should be permitted if the "custodian" rather than the "mutual fund" has reasonable grounds to believe that the action is in the best interests of the fund. Custodians must meet certain prescribed requirements and act in a fiduciary capacity towards a fund therefore they are in the best position to determine what is in the best interests of a fund. Since a custodian must follow its client's instructions and has no discretion to assess the wisdom of those instructions, it would be highly unfair to require custodians to bear losses resulting from the due execution of instructions that the mutual fund later asserts were not in its best interests. Therefore, the word "and" which joins clauses (a) and (b) should be replaced by the word "or". In the alternative, clause (b) should be deleted. Subsection 6.6(4) should also be amended accordingly.	Change made. Clause 6.6(3)(b) deleted. Subsection 6.6(4) not changed.
49	S. 6.6(3)	_____	The use of the words "legal fees, judgments and amounts paid in settlement" arguably requires some form of litigation in order for the indemnity to operate. However, where a custodian has clearly met its standard of care, the custodian should be entitled to be indemnified out of the assets of the mutual fund without having to take any legal action. In addition, this restrictive language may subject the mutual fund itself to additional costs in order to defend a bona fide claim by the custodian, which cannot be the intent of this provision.	No change. The provision does not make the commencement of formal legal proceedings a precondition for indemnification.
50	S. 6.8(1)	_____	The reference to "initial margin" should be changed to "margin" since the concept of initial margin does not appear elsewhere in the section.	Change made.
51	S. 6.8	_____	The exception in s. 6.8(3) needs to be better expressed to reflect three issues: (i) the exception remains limited to transactions involving forward contracts or options that are not clearing corporation options; (ii) the current language, dealing with "depositing...as collateral" does not encompass the full range of ways in which a mutual fund's assets can be "encumbered"; (iii) the placement of 6.8(3) in the custodial section does not clearly reflect the intention to grant an exception - such an intention should be expressed in the same section which contains the prohibition (i.e in Part 2). A new section should be added to Part 2 to permit the encumbrance of portfolio assets by way of granting a security interest in those assets.	Change made. Subsection 6.8(3) has been amended to permit the deposit of assets in connection with the granting of a security interest relevant to specified derivative transactions. This conforms to the changes made to section 2.6 of the NI.
52	S. 6.8(4)	_____	A transitional provision should be included in Part 20 to allow agreements by which portfolio assets are deposited in accordance with section 6.8 to be amended as is the case for custodial agreements under section 6.4.	Change made. Paragraph 20.5(2)4 added.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
53	S. 9.1(3)	_____	The word "transmitted" should be replaced by the word "sent" for consistency with subsections 9.1(1) and (2).	Change made.
54	S. 9.1(4) and (6)	_____	The ability to establish cut-off times should extend to paper orders as well. Fund managers and dealers may need to establish different cut-off times for different orders, depending on the manner in which the order is processed. Cut-off times for electronic orders could be later than those for paper orders since electronic orders can be processed more quickly. While the language of the NI appears sufficiently permissive to allow for this, a section should be added to the CP to clarify this point. These comments also apply to subsection 10.2(4) and (7).	No change. A distinction has been made for electronic orders because such orders go directly to the order receipt office on the same day.
55	S. 9.1(7)	_____	The provision seems to require either (i) that the person responsible for approving new accounts receive a copy of each and every purchase order received by the dealer, despite the fact that the person responsible for reviewing client trades is also receiving this information, or (ii) that the person approving new accounts must also be the person who performs the know your client review of trades. Dealers should be entitled to establish, within the limits of generally applicable supervisory requirements imposed by securities laws, how they will meet these obligations. To the extent that an "in the jurisdiction" requirement is imposed by the laws of a jurisdiction, the obligation to satisfy that requirement exists notwithstanding this provision. Where such a requirement is not imposed, this NI is not the appropriate place to establish such a requirement.	Change made. The words "approving the opening of new client accounts and for" have been deleted.
56	S. 9.1(7)	_____	The provision should make clear that the relevant information can be communicated electronically.	No change. Electronic transmission is not precluded.
57	S. 9.2(a)	_____	The provision should be amended to state that "the rejection of the order is made no later than the close of business on the business day after the date of receipt of the order by the mutual fund". If the 24 hour requirement is retained, it could mean that a mutual fund that received an order on Friday would have to reject the order on a non-business day.	Change made. The reference to "24 hours" has been replaced with "one business day".
58	S. 9.2(b)	_____	The provision should be amended to require that money be refunded within 3 business days (T+3), to be consistent with the rest of the NI and to ensure that the purchaser's cheque has cleared the banking system.	No change. The CSA believe that there should be no delay in refunding cash to an investor when a purchase order is rejected.
59	S. 9.4(1)	_____	This provision enshrines the T+3 standard. The settlement standard for money market funds should be dealt with separately. The industry norm is currently T+1 for such funds.	No change. The provision imposes a minimum standard. A shorter settlement period is permitted.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
60	S. 9.4(3) & 10.4(4)	_____	In cases of both *in specie* purchases and redemptions the requirement to include details in the statement of portfolio transactions should be deleted. To put this requirement into effect by segregating these assets would require systems enhancements.	No change. The reporting requirement for *in specie* redemptions that is currently in section 13.03 of NP 39 is retained.
61	S. 9.4(4)	_____	The provision should be amended to include any situation in which the mutual fund discovers, after T+3, that there are insufficient funds to settle the purchase. There are forms of payment, other than cheques, which may be returned to the mutual fund if insufficient payor's monies are available. The provision should be amended to address all forms of insufficient payment. For example, payment via electronic fund transfer.	Change made. Reference to "method of payment" has been added.
62	S. 9.4(4)(a)	_____	This clause should be amended to clarify that the order to redeem the securities purchased and force settle the purchase order is deemed to be received on the business day following T+3. This follows the same approach as NP 39 but simply reflects the shorter settlement cycle.	Change made.
63	S. 10.1	_____	For registered accounts the registered holder must be the trustee. The trustee typically delegates a number of functions regarding the administration of the registered plan to the fund company or dealer that sponsors the registered plan and so the trade is often approved by the fund company or dealer and then processed. It would be helpful to clarify these requirements with respect to registered accounts in section 10.2 of the CP.	No change. Paragraph 10.1(1)(b)(i) permits a redemption order to be completed "on behalf of" a securityholder. Therefore, parties are not precluded from making arrangements that they consider appropriate.
64	S. 10.2(6)	_____	Since all orders come from registered dealers, the notice proposed should be given to the participating dealer rather than the securityholder.	No change. The CP clarifies that reference to "securityholder" is to the registered securityholder.
65	S. 11.1	_____	The provision requires a dealer to have "a" trust account. It should be amended to clarify that this does not mean that a dealer must only maintain a single trust account (some may wish to maintain trust accounts with different financial institutions to make it easier to transmit client funds).	Change made to clause 11.1(1)(a) to permit more than one trust account.
66	S. 11.1(4)	_____	Permitting dealers to remit interest annually to a contingency fund, as previously suggested, is a viable and positive option which should be considered by the CSA.	No change at this time.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
67	S. 11.3	_____	Some financial institutions will not pay interest on an account if there is not a sufficient balance maintained in the account at all times. In smaller communities, dealers may not be able to access a branch of a competing financial institution. Assuming the financial institution imposes the same requirements on all accounts with a dealer and pays no interest on any of those accounts, this would presumably meet the specific requirements of clause 11.3(1)(b). Clarification of this point was not included in the recent CSA Staff Notice 33-303 and 81-304 and would be helpful.	No change. The provision does not require that interest always be paid. If no interest is charged "on comparable accounts of the financial institution" then the requirement is satisfied. See subsection 11.1(6) of the CP.
68	S. 11.3(1)(c)	S. 11.3(c)	This provision is unnecessary and should be deleted. The mutual funds benefit from all interest earned on the account. Bank charges are a customary and reasonable cost of obtaining bank services. There is no valid policy reason why the funds should enjoy the benefits associated with the account without paying the normal costs associated with a bank account.	No change. The CSA consider charges against a trust account to be a cost of doing business for principal distributors and participating dealers. The money in a trust account is client money and cannot be reduced through bank charges.
69	S. 11.5	_____	There is no apparent policy rationale for requiring the custodian to open its records to the fund's principal distributor for inspection. It seems reasonable that the manager of operations and the auditors should have access to the fund's records and a cogent argument could be made that the trustee should also have access to these records. The designation of "representatives of the mutual fund" as having the authority to request inspection of contracts may be problematic since the term is not defined in either the NI or the CP.	Change made. The reference to principal distributor has been deleted.
70	S. 12.1	_____	The filing requirement for dealers and distributors should be 140 days (as it is for funds).	No change. The provision is consistent with the financial filing requirements for registrants.
71	S. 12.1(2)(b)	_____	The clause should be amended to allow the principal distributor to file a report of its own auditor or that of the funds' auditor. In certain cases, the auditor of the principal distributor is different from the auditor of the mutual funds. The audit of financial statements of a mutual fund includes an examination of the securityholder accounting system procedures and controls and also covers the co-mingling of money. If the clause is not modified, the auditor of the principal distributor would be required to perform the same procedures as the auditor of the mutual fund performs in rendering an opinion on the financial statements of the mutual fund. This will result in a duplication of effort and cost inefficiency.	Change made.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
72	Part 13	_____	The CICA and other professional bodies are in a better position to offer guidance on these issues and therefore the CSA should not impose detailed and specific regulations regarding the valuation of securities. For example, sections 13.4 and 13.5 should be deleted since it is inappropriate and unnecessary to provide specific direction on only limited subsets of investments. The wording contained in s.14.05 of NP 39 is preferable to the approach set out in subsection 13.5(4) and if the provision is retained it should be amended back to the wording used in NP 39. The requirement of s.13.5(4)(b) should only apply in circumstances in which the daily limits have been reached rather than for all standardized futures for which daily limits are applicable. It would be appropriate to also consider the time value of money that may be built into the futures contract i.e. the "fair value" of the futures contract should be established. It is inappropriate for the CSA to attempt to mandate a particular valuation method given the need for judgment in determining fair value in certain circumstances.	No change. The CSA believe that it is necessary and appropriate to address these issues in the NI. Provisions have been carried forward from NP39. Change made. No change. The CSA believe that the time value is accounted for by basing the value of the future on the gain or loss on the future.
73	S. 13.1(4)	_____	Reference is made to publication of net asset value. Net asset value per security is published. The two concepts are different and equally important. The NI should deal carefully and separately with each.	Changes made throughout NI.
74	S. 13.1(4)	_____	The provision should be deleted. If the provision is retained, it should be amended so that it is not mandatory but instead reflects a concept of "commercially reasonable efforts". Also, the word "timely" must be clarified.	No change. See section 12.1 of the CP.
75	S. 13.4	_____	This section does not address adequately the complexities associated with valuing restricted shares. For example, it does not deal with instances where the information required is not available (eg. proportional class information at the time of purchase and valuation). Also, the time remaining until the lifting of a restriction is a factor in valuation and has not been addressed. There is no room for manager discretion which is advisable in certain situations.	No change. The time remaining until lifting of a restriction is addressed in clause (b).
76	S. 13.5, 6	_____	The term "mark-to-market" should be defined.	Change made. The provision has been deleted. The valuation of swaps is now addressed by paragraph 3 of section 13.5.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
77	Part 14	_____	Section 13.3 requires that capital transactions will be reflected in the first valuation date after the date used to establish an issue or redemption price. Accordingly, it appears that the net asset value per security for distribution purposes will not include capital activity for transactions of that date. This is an inconsistency which will impact calculations, including the capital gains refund mechanism, to the disadvantage of securityholders of the fund. The provision should be clarified so that transactions be reflected in the net asset value per security for distribution purposes.	No change. The CSA are of the opinion that there is no conflict between s. 13.3 and s.14.1(a).
78	S. 14.1	_____	Some funds utilize the following model for distributions: *Day X: 1. - calculate NAVPS* *2.- process orders received prior to cut-off time on Day X at Day X NAVPS* *3.- develop unitholder record* *Day X+1: 1.- calculate NAVPS and distribution per unit* *2.- process orders received since Day X cut-off time and before Day X+1 cut-off time at Day X+1 NAVPS* *3.- process distributions (reinvestments and cheques as appropriate) to unitholders shown on unitholder record.* This is an efficient and fair method of dealing with distributions. The section should be amended to make clear that it will continue to be possible to declare a record date on a day immediately prior to the actual distribution.	Change made. The record date can be the date on which the NAVPS is determined for purposes of paying a dividend or distribution or the last day on which NAVPS was calculated before the date of payment.
79	Part 15	_____	This part does not mention image advertisements, nor does the Notice preceding the NI. The CSA should confirm that CSA Notice 7 - National Policy No. 39 - Mutual Funds - Sales Communications, which excludes image advertisements from the definition of “sales communications”, continues to apply.	No change. Subsection 2.15(3) of the CP addresses image advertising.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
80	S. 15.2(2)	_____	The change to requiring 10-point type will make the creation and use of some advertisements and sales communications prohibitively expensive, as all text will need to be enlarged accordingly and the overall space required will need to be increased to accommodate this. The new requirement may also eliminate the use of certain graphical presentations in advertisements, such as mountain charts. The new requirement is anti-competitive since no other participant in the financial services industry is subject to the same standards. Ultimately, there are sufficient safeguards in the requirement that sales communications not be misleading and the current 8-point type requirement. As a minimum, the 10-point type requirement should be restricted to specified text (including headlines, performance data, warning language), with the flexibility to use any other type size for the balance of the text. The point size of type is merely one factor that determines readability and changing the type size is not an effective way of making disclaimers more readable. An alternative would be to establish a minimum point size and leading relationship, to make the type easier to read. Although a disclaimer would be made larger, because designers can increase the size of the other type, the net result may be that the disclaimer is no more prominent, attractive or effective. The requirement may also make it less efficient to provide French materials since such materials are generally more space intensive than in English. Extensive re-design costs will have to be incurred for many standard documents.	Change made. The 10-point type requirement applies to performance data or disclosure specifically required to be included in sales communications by the NI.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
81	S. 15.3(1)(d)	_____	The clause prohibits comparison to a benchmark that has or will become discontinued(eg. TSE 100) if that benchmark only existed for a portion of the period subject to comparison, thus limiting the period that can be compared. The use of reconstructed benchmarks is the norm. For example, the TSE/S&P 60 will be reconstructed back over a number of years. CSA concerns could be addressed by appropriate disclosure concerning the transition from the discontinued benchmark to another benchmark. The clause prohibits the use of peer group indices and other benchmarks produced by an independent organization which may be entirely suitable for comparison but are not permitted simply because they are or were not widely available throughout the entire period of comparison. For some funds (eg. balanced funds) there are no currently available indices against which to benchmark. To date, the practice has been to take two or more appropriate benchmarks and average the performance on the indices in order to develop a benchmark appropriate to the fund. The clause would appear to prohibit this practice for no valid policy reason.	Change made. Clause 15.3(1)(d) has been amended to permit the use of reconstructed benchmarks that are widely recognized and available. Change made. A new subsection 15.3(3) has been added to permit an index mutual fund to provide performance data for its benchmark index provided the benchmark is widely recognized and available. No change. Exemptive relief can be requested in appropriate circumstances.
82	S. 15.3(2)	_____	This subsection needs to be clarified. The apparent intention is that any comparison of performance data about young funds made to existing securityholders includes only a comparison to a fund or asset allocation service under common management and not to a benchmark. The reference to the prohibition under 15.6(a) is unclear, since 15.6(a) describes the situations in which performance data can be used in a sales communication. Also, it is not clear why the performance data about young funds cannot be compared to a recognized benchmark.	Change made. Subsection 15.3(3) has been added to permit a young fund to make comparisons to a widely recognized and available index.
83	S. 15.3(3)(b)	S. 15.3(4)(b)	For the purposes of comparability of rankings, it is more meaningful to have the ranking information for the standard periods of 1,3,5 and 10 years as opposed to the standard performance data for these periods.	Change made. New paragraph (c) added.
84	S. 15.3(5)	S. 15.3(6)	This subsection appears to conflict with subsection 15.13(3) which restricts references in communications to funds that <u>are</u> money market funds instead of to funds that are or were money market funds under the NI or NP 39. Why does subsection 15.13(3) refer to "communications" while subsection 15.3(5) refers to "sales communications"?	Change made. Subsection 15.13(3) has been deleted.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
85	S. 15.3(4)(c)	S. 15.3(5)(c)	Is it correct that if there is a differential between credit ratings that the lower credit rating would have to be used, as is currently the requirement under subclause 16.04(a)(xv) of NP 39?	Yes. No change.
86	S. 15.4	_____	The sample warning language remains too lengthy and inaccessible. Shorter, simpler general warning language should be adopted for section 15.4.	Change made. All of the sample warnings and disclosure have been amended.
87	S. 15.4(7)(b)	_____	Does the CSA intend that the prescribed statement appear adjacent to the performance numbers or on the same page? Subsection 15.4(6) regarding non-money market funds does not prescribe where the required statement is to be positioned. If the intent of this part is to ensure that disclosure statements appear coterminous to the performance numbers, it is plausible that the remaining disclosure statements will not be read. In light of the change to a minimum of 10 point type, it is submitted that the disclosure will be read and should be part of main disclosure.	Yes. No change.
88	S. 15.4(11)	DELETED	The approach in NP 39 and the 1997 Draft is preferable since there should be no need for warning language in such situations. However, the 50% should refer to the size or area of the communication and not to the text (number of words) of the communication.	Change made. This subsection has been deleted since the warnings have been reduced.
89	S. 15.5	_____	To describe a fund as no-load is misleading notwithstanding this provision. All mutual funds pay distribution costs in some way.	No change.
90	S. 15.5(2)	_____	The term “fees and charges paid by the mutual fund” is very broad and would arguably include fees such as management fees, custody fees, trustee fees, brokerage fees etc. which are not required to be disclosed by any other mutual fund in their sales communications. There is no rationale for requiring such disclosure. The disclosure of fees, charges and trailing commissions should not be required unless such fees and charges are payable by the investor. The market is generally aware that “no load” means no fees or charges payable directly by the investor.	Change made. The words “fees and charges” have been replaced with the words “management fees and operating expenses”. The revised warning language in subsections 15.4(3) and (6) which applies to all mutual funds (other than money market funds) refers to trailing commissions, fees and expenses.
91	S. 15.5(2)(b)	_____	This requirement goes far beyond the NP 39 requirements and will, in practice, proscribe all advertising by no-load funds since even a summary description of all fees and charges paid by the mutual fund will be extensive. General warning language (see comment re 15.4(3)) would address any potential for confusion by alerting investors to the possibility of fees and charges, both direct and indirect.	Change made. The requirement to include a summary of fees and charges has been replaced by a requirement to disclose that management fees and operating expenses are paid by the mutual fund.
92	S. 15.5(2)(c)	_____	Despite the statement in footnote 133 that the CSA wish to alleviate confusion between the term “no-load” and the existence of trailers, the proposed regulatory solution may create confusion.	No change.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
93	S. 15.5(3)	_____	The wording should be limited to only fees and charges payable by the investor directly. To do otherwise would be impractical and would result in no fund referring to itself as "no load". This would not be in the best interests of investors.	Change made. The communication does not need to provide a summary but must disclose the types of fees and charges that exist.
94	S. 15.6(a)(i)	_____	Is this clause breached by delivering a combined annual or semi-annual report to securityholders for all funds within a fund family where one or more funds has operated for less than 12 months? If reports to securityholders are excluded from the definition of "sales communication", then providing combined reports to securityholders will not violate this clause.	Change made. New paragraph 15.6(a)(ii)(B) added to permit delivery of sales communication to securityholders/participants of a mutual fund/asset allocation service under common management.
95	S. 15.7	_____	Would an advertisement making reference to investments available through an asset allocation service profiling the performance of mutual funds not under common management be deemed as "comparing performance"? This type of advertisement does not actually instruct readers to compare, but rather observe the performance history of various funds which comprise portfolios offered through the assets allocation service.	No. No change.
96	S. 15.7(b)	_____	The possibility for fund comparisons has been dramatically narrowed by this provision, particularly in respect of funds that are not under common management. Restricting comparisons of funds in different families to those with similar fundamental investment objectives is troubling given the breadth of the definition.	No change. The CSA believe that comparisons should be permitted only where the fundamental investment objectives are similar.
97	S. 15.8(2)(a)	_____	Is it correct to presume that the CSA will not require sales communications to necessarily present data in a 10, 5, 3 and 1 year order?	No change. The order is not prescribed however the data must be consecutive.
98	S. 15.8(2)(b)(i) and (ii)	_____	Please clarify the methodology that should be employed to ensure compliance with these provisions.	No change. The CSA believe that the provisions are clear.
99	S. 15.8(4)	_____	Will this requirement be waived if fund companies use the most current standard performance data in the sales communication? Many fund companies have newspaper performance advertisements, which are based upon the most current data, and are promptly updated.	Change made. The second part of the provision has been deleted.
100	S. 15.9	_____	It is doubtful whether the additional disclosure requirements imposed by this section are practical and may be adhered to in a manner that is meaningful or useful for investors in a sales communication.	No change.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
101	S. 15.9(2)	_____	This provision imposes significant new requirements. Essentially it limits the use of performance data to either stale-dated performance of the two funds that existed before the transaction or to performance data of the continuing fund, but only after that fund has been in existence for one year. It is not clear what investors gain from seeing stale-dated performance of the two funds prior to reorganization and from not seeing any performance data for the continuing fund for one year. The acquiring fund existed before and continues to exist after the transaction. Therefore, why is it prejudicial to a securityholder to be given performance data of the continuing fund anytime after the transaction, provided there is disclosure about the merger in the sales communication. Requiring performance information for the non-continuing fund may be misleading, especially if the non-continuing fund was considerably smaller than the continuing fund. Investors may be encouraged to make "quick calculations" by blending the performance data for both funds which, for many reasons, may be undesirable (as noted by the rejection of this approach by the CSA).	No change. The application of the provision is limited to cases where there was a significant change to the continuing fund as a result of the transaction.
102	S. 15.12	_____	Does this preclude reference to the anticipated availability date of a new fund in a newsletter or a reader newspaper advertisement? It does not appear that s.15.12(e) prohibits fund companies from mentioning an anticipated launch date when read in conjunction with s. 65 of the Securities Act (Ontario). The CSA should clarify this, perhaps with a cross-reference to corresponding sections in the Securities Act (Ontario).	No change. Reference to anticipated availability is not precluded.
103	Part 16	_____	The calculation does not appear to exclude interest charges, taxes and commissions and brokerage fees on the purchase and sale of portfolio assets. It is in effect a total operating expense ratio. This is a significant change and will have the effect of increasing industry MERs. Comparison with a previous year will yield inconsistent results. Certain taxes, which relate solely to the investing activity of a fund, rather than operating expenses, ought not to be included in the MER calculation. Specifically, for corporate funds, the inclusion of corporate income taxes, capital tax, and foreign withholding taxes are a consequence of investing activity and accordingly, are most properly reflected in the performance of the fund. These costs are outside the control of the manager and bear no relation to operating activities. Therefore, these taxes should be excluded from the calculation of MER. The 1997 CICA Research Report stated that GST/PST should be included in "total expenses" but that income and capital tax be excluded. The industry practice has been to exclude GST when reporting MER.	No change. See subsection 14.1(2) of the CP. The MER is designed to be an all inclusive expense ratio regardless of control over these expenses. The aim is to show investors the actual cost of investing.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
104	S. 16.1(1)	_____	Please clarify whether calendar or business days should be employed.	No change. The CSA believe that the provision is clear as drafted.
105	S. 16.1(2)	_____	Please clarify what is meant by "note to disclosure". Does this include only financial statement disclosure, or does it also include prospectuses and other continuous disclosure documents?	No change. See subsection 14.1(1) of the CP.
106	S. 16.1(2)	_____	The calculation is complex for each fund and some fund companies do not presently provide these details. Presently, notation is made in the financial statements that a portion of the fees otherwise payable by the funds has been absorbed by the mutual fund. This appears to be no longer adequate. Please clarify if this is an accurate interpretation of the new requirement.	No change. The provision requires that a mutual fund disclose more than that some fees have been waived or absorbed.
107	S. 18.1	_____	Some limits should be placed on the type of information to be retained, the length of time it must be retained and what information securityholders can access. The requirement should be replaced by a requirement that records be retained for 7 years (in keeping with the Income Tax Act) or some other reasonable time limit. Also, it should be clarified that records and registers may be kept in electronic form rather than in paper form.	Change made. The words "for at least as long as the mutual fund is in existence" have been deleted. See section 15.1 of the CP. The provision does not require that records be kept in paper form.
108	S. 18.2	_____	The second purpose - "a matter relating to the administration of the mutual fund" - is a very broadly stated purpose and there are no guidelines in the CP concerning how it may be limited. Without some guidance in the CP, it may not be possible to adequately control access to securityholder record information that may be sought for an improper purpose. Each mutual fund company has an obligation of confidentiality to holders of its securities which should only be lessened in the clearest of cases (such as to influence the voting of securities).	Change made. Subsection 18.2(1) has been amended to refer to a "matter relating to the relationships of the mutual fund, the members of the organization of the mutual fund, and the securityholders, directors and officers of those entities".
109	S. 19.1(1)	_____	Clause 2.2(2)(b) of NI 13-101 SEDAR permits electronic filing of exemptive relief applications "reasonably required to facilitate a distribution of securities to which a prospectus relates". Notwithstanding that provision, all applications for exemptive relief under NI 81-102 should be filed on SEDAR including applications under proposed National Policy 12-201 MRRS, subject to existing rules and policy considerations pertaining to confidentiality. Orders granted should be published or otherwise made publicly available as other orders or decisions of CSA members.	Applications for relief from the NI will be filed and processed on SEDAR as is currently the practice with NP 39 applications.
110	S. 19.2(1)	_____	The provision should be amended to clarify that the revocation by the CSA of any exemption order or waiver previously given under NP 39 may not be made without the relevant market participant first having the right to be heard.	No change. Any action taken by a regulator or securities regulatory authority would be subject to the general principles of administrative law as well as any specific requirements in securities law.

	March 1999 Draft Reference	*Final Reference*	*Comment*	*CSA Response*
111	Appendix B - Compliance Reports	_____	The audit reports essentially provide that there is compliance in all material respects with the applicable requirements of NI 81-102. However, the compliance reports do not contain an exclusion for non-material deviations. The language of the compliance reports should be amended to state that there is compliance "in all material respects" with the applicable requirements of NI 81-102.	No change. The CSA want to know whether there has been compliance in all respects with the applicable provisions.
112	S. 7.5(2) & (3) CP	S. 7.4(2) & (3) CP	Recently there have been a number of moves of high profile individual portfolio managers to competing mutual fund organizations. Some mutual fund groups have also heavily marketed, both in public advertising and advertising to the broker network, individual "star" portfolio managers who are managing particular funds. Perhaps there should be at least a minimum notice period (eg. to permit investors to switch to another fund outside or within the existing fund group) before there is such a change (other than a termination for cause, which could occur immediately) rather than tying the change to timely disclosure and amending the prospectus. Consideration should be given to requiring a minimum notice period or even a requirement of securityholder or securities regulatory approval. Notwithstanding 7.5(2) of the CP, the name of the individual portfolio manager may not appear in the prospectus therefore an amendment to the SP may not be necessary to disclose the departure of a particular individual.	No change.

NATIONAL INSTRUMENT 81-102
MUTUAL FUNDS

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NATIONAL INSTRUMENT 81-102
MUTUAL FUNDS

PART 1 DEFINITIONS AND APPLICATION

1.1 Definitions - In this Instrument

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

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

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

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

(b) no approved credit rating organization has rated the security or instrument in a rating category that is not an approved credit rating:

Approved Credit Rating Organization	Commercial Paper/ Short Term Debt	Long Term Debt
CBRS Inc.	A-1	A
Dominion Bond Rating Service Limited	R-1-L	A
Duff & Phelps Credit Rating Co.	D-1	A
Fitch IBCA, Inc.	A-1	A
Moody's Investors Service, Inc.	P-1	A2
Standard & Poor's Corporation	A-1	A
Thomson BankWatch, Inc.	TBW-2	A

"approved credit rating organization" means each of CBRS Inc., Dominion Bond Rating Service Limited, Duff & Phelps Credit Rating Co., Fitch IBCA, Inc., Moody's Investors Service, Inc., Standard & Poor's Corporation, and Thomson BankWatch, Inc. and any of their respective successors;

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

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

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

1. Cash.
2. Cash equivalents.
3. Synthetic cash.
4. Receivables of the mutual fund that arise from the disposition of portfolio assets, net of payables that arise from the acquisition of portfolio assets;

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

(a) the government of Canada or the government of a jurisdiction,

(b) the government of the United States of America, the government of one of the states of the United States of America, the government of another sovereign state or a permitted supranational agency, if, in each case, the evidence of indebtedness has an approved credit rating, or

(c) a Canadian financial institution, or a financial institution that is not incorporated or organized under the laws of Canada or of a jurisdiction if, in either case, evidences of indebtedness of that issuer or guarantor that are rated as short term debt by an approved credit rating organization have an approved credit rating;

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

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

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

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

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

"currency cross hedge" means the substitution by a mutual fund of a risk to one currency for a risk to another currency, if neither currency is a currency in which the mutual fund determines its net asset value per security and the aggregate amount of currency risk to which the mutual fund is exposed is not increased by the substitution;

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

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

"dealer manager" means

(a) a specified dealer that acts as a portfolio adviser,

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

(c) a partner, director or officer of a portfolio adviser referred to in paragraph (b);

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

(a) either

(i) the amount of principal, interest or principal and interest to be paid to the holder is linked in whole or in part by a formula to the appreciation or depreciation in the market price, value or level of one or more underlying interests on a predetermined date or dates, or

(ii) the security provides the holder with a right to convert or exchange the

security into or for the underlying interest or to purchase the underlying interest, and

(b) on the date of acquisition by the mutual fund, the percentage of the purchase price attributable to the component of the security that is not linked to an underlying interest is less than 80 percent of the purchase price paid by the mutual fund;

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

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

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

1. Make or take delivery of the underlying interest of the agreement.

2. Settle in cash instead of delivery;

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

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

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

"guaranteed mortgage" means a mortgage fully and unconditionally guaranteed, or insured, by the government of Canada, by the government of a jurisdiction or by an agency of any of those governments;

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

(a) if

(i) the intended effect of the transaction, or the intended cumulative effect of the series of transactions, is to offset or reduce a specific risk associated with all or a portion of an existing investment or position or group of investments or positions,

(ii) the transaction or series of transactions results in a high degree of negative correlation between changes in the value of the investment or position, or group of investments or positions, being hedged and changes in the value of the instrument or instruments with which the investment or position is hedged, and

(iii) there are reasonable grounds to believe that the transaction or series of transactions no more than offset the effect of price changes in the investment or position, or group of investments or positions, being hedged, or

(b) if the transaction, or series of transactions, is a currency cross hedge;

"illiquid asset" means

(a) a portfolio asset that cannot be readily disposed of through market facilities on which public quotations in common use are widely available at an amount that at least approximates the amount at which the portfolio asset is valued in calculating the net asset value per security of the mutual fund, or

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

"index mutual fund" means a mutual fund that has adopted fundamental investment objectives that require it to

(a) hold the securities that are included in a specified widely quoted market index in substantially the same proportion as those securities are reflected in that index, or

(b) invest in a manner that causes the mutual fund to replicate the performance of that index;

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

(a) hold the securities that are included in a specified widely quoted market index in substantially the same proportion as those securities are reflected in that index, or

(b) invest in a manner that causes the issuer to replicate the performance of that index;

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

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

"long position" means a position held by a mutual fund that, for

(a) an option, entitles the mutual fund to elect to purchase, sell, receive or deliver the underlying interest or, instead, pay or receive cash,

(b) a standardized future or forward contract, obliges the mutual fund to accept delivery of the underlying interest or, instead, pay or receive cash,

(c) a call option on futures, entitles the mutual fund to elect to assume a long position in standardized futures,

(d) a put option on futures, entitles the mutual fund to elect to assume a short position in standardized futures, and

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

"management expense ratio" means the ratio, expressed as a percentage, of the expenses of a mutual fund to its average net asset value, calculated in accordance with Part 16;

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

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

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

(a) all of its assets invested in any or all of

(i) cash,

(ii) cash equivalents,

(iii) evidences of indebtedness, other than cash equivalents, that have remaining terms to maturity of 365 days or less, or

(iv) floating rate evidences of indebtedness not referred to in subparagraph (ii) or (iii), if the principal amounts of the obligations will continue to have a market value of approximately par at the time of each change in the rate to be paid to the holders of the evidences of indebtedness,

(b) a portfolio with a dollar-weighted average term to maturity not exceeding 90 days, calculated on the basis that the term of a floating rate obligation is the period remaining to the date of the next rate setting,

(c) not less than 95 percent of its assets invested in cash, cash equivalents or evidences of indebtedness denominated in a currency in which the net asset value per security of the mutual fund is calculated, and

(d) not less than 95 percent of its assets invested in any or all of

(i) cash,

(ii) cash equivalents, or

(iii) evidences of indebtedness of issuers the commercial paper of which has an approved credit rating;

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

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

(a) prohibit a mutual fund from knowingly making or holding an investment in an issuer in which the mutual fund, alone or together with one or more mutual funds under common management, is a substantial securityholder as defined by securities legislation, or

(b) prohibit the portfolio adviser of the mutual fund, the mutual fund or a responsible person, as defined in securities legislation, from selling portfolio assets of the mutual fund to, or

purchasing portfolio assets from, another mutual fund under common management;

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

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

(a) whose principal place of business is outside of Canada,

(b) that advises a portfolio adviser to a mutual fund, and

(c) that is not registered under securities legislation in the jurisdiction in which the portfolio adviser that it advises is located;

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

1. Receive an amount of cash determinable by reference to a specified quantity of the underlying interest of the option.

2. Purchase a specified quantity of the underlying interest of the option.

3. Sell a specified quantity of the underlying interest of the option;

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

"order receipt office" means, for a mutual fund

(a) the principal office of the mutual fund,

(b) the principal office of the principal distributor of the mutual fund, or

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

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

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

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

"permitted gold certificate" means a certificate representing gold if the gold is

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

(b) of a minimum fineness of 995 parts per 1,000,

(c) held in Canada,

(d) in the form of either bars or wafers, and

(e) if not purchased from a bank listed in Schedule I or II of the *Bank Act* (Canada), fully insured against loss and bankruptcy by an insurance company licensed under the laws of Canada or a jurisdiction;

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

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

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

"portfolio asset" means an asset of a mutual fund;

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

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

(a) an exclusive right to distribute the securities of the mutual fund in a particular area, or

(b) a feature that gives or is intended to give the person or company a material competitive

advantage over others in the distribution of the securities of the mutual fund;

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

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

"report to securityholders" means a report that includes annual or semi-annual financial statements and that is delivered to securityholders of a mutual fund;

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

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

(a) is made

(i) to a securityholder of the mutual fund or participant in the asset allocation service, or

(ii) to a person or company that is not a securityholder of the mutual fund or participant in the asset allocation service, to induce the purchase of securities of the mutual fund or the use of the asset allocation service, and

(b) is not contained in any of the following documents of the mutual fund:

1. A preliminary or *pro forma* prospectus.

2. A simplified prospectus or preliminary or *pro forma* simplified prospectus.

3. An annual information form or preliminary or *pro forma* annual information form.

4. Financial statements, including the notes to the financial statements and the auditor's report on the financial statements.

5. A trade confirmation.

6. A statement of account;

"short position" means a position held by a mutual fund that, for

(a) an option, obliges the mutual fund, at the election of another, to purchase, sell, receive or deliver the underlying interest, or, instead, pay or receive cash,

(b) a standardized future or forward contract, obliges the mutual fund, at the election of another, to deliver the underlying interest or, instead, pay or receive cash,

(c) a call option on futures, obliges the mutual fund, at the election of another, to assume a short position in standardized futures, and

(d) a put option on futures, obliges the mutual fund, at the election of another, to assume a long position in standardized futures;

"significant change" means

(a) a change in the business, operations or affairs of a mutual fund that would be considered important

(i) by a reasonable investor in determining whether to purchase securities of the mutual fund, or

(ii) by a reasonable securityholder of the mutual fund in determining whether to continue to hold securities of the mutual fund, or

(b) a decision to implement a change referred to in paragraph (a) made

(i) by senior management of the mutual fund who believe that confirmation of the decision by the board of directors of the mutual fund is probable, or

(ii) by senior management of the manager of the mutual fund who believe that confirmation of the decision by the board of directors of the manager of the mutual fund is probable;

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

"specified asset-backed security" means a security that

(a) is primarily serviced by the cash flows of a discrete pool of receivables or other financial assets, either fixed or revolving, that by their

terms convert into cash within a finite time, and any rights or assets designed to assure the servicing or timely distribution of proceeds to securityholders, and

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

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

(a) acting solely in respect of mutual fund securities, or

(b) acting solely in respect of transactions in which a person or company registered in the category of limited market dealer in a jurisdiction is permitted to engage;

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

(a) a conventional convertible security,

(b) a specified asset-backed security,

(c) an index participation unit,

(d) a government or corporate strip bond,

(e) a capital, equity dividend or income share of a subdivided equity or fixed income security,

(f) a conventional warrant or right, or

(g) a special warrant;

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

1. Make or take delivery of the underlying interest of the agreement.

2. Settle the obligation in cash instead of delivery of the underlying interest;

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

"swap" means an agreement that provides for

(a) an exchange of principal amounts,

(b) the obligation to make, and the right to receive, cash payments based upon the value, level or price, or on relative changes or movements of the value, level or price, of one or more underlying interests, which payments may be netted against each other, or

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

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

(a) a long position in a portfolio of shares and a short position in a standardized future of which the underlying interest consists of a stock index, if

(i) there is a high degree of positive correlation between changes in the value of the portfolio of shares and changes in the value of the stock index, and

(ii) the ratio between the value of the portfolio of shares and the standardized future is such that, for any change in the value of one, a change of similar magnitude occurs in the value of the other, or

(b) a long position in the evidences of indebtedness issued, or fully and unconditionally guaranteed as to principal and interest, by any of the government of Canada or the government of a jurisdiction and a short position in a standardized future of which the underlying interest consists of evidences of indebtedness of the same issuer and same term to maturity, if

(i) there is a high degree of positive correlation between changes in the value of the portfolio of evidences of indebtedness and changes in the value of the standardized future, and

(ii) the ratio between the value of the evidences of indebtedness and the standardized future is such that, for any change in the value of one, a change of similar magnitude occurs in the value of the other;

"timely disclosure requirements" means the requirements in securities legislation for a reporting issuer to file a press release and a report when a material change occurs in the affairs of the reporting issuer;

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

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

(a) an option, the quantity of the underlying interest of the option position multiplied by the market value of one unit of the underlying interest, multiplied, in turn, by the delta of the option,

(b) a standardized future or forward contract, the quantity of the underlying interest of the position multiplied by the current market value of one unit of the underlying interest; or

(c) a swap, the underlying market exposure, as calculated under paragraph (b), for the long position of the mutual fund in the swap.

1.2 Application - This Instrument applies only to

(a) a mutual fund that offers or has offered securities under a prospectus or simplified prospectus for so long as the mutual fund remains a reporting issuer; and

(b) a person or company in respect of activities pertaining to a mutual fund referred to in paragraph (a) or pertaining to the filing of a prospectus to which subsection 3.1(1) applies.

1.3 Interpretation - Each section, part, class or series of a class of securities of a mutual fund that is referable to a separate portfolio of assets is considered to be a separate mutual fund for purposes of this Instrument.

PART 2 INVESTMENTS

2.1 Concentration Restriction

(1) A mutual fund shall not purchase a security of an issuer, enter into a specified derivatives transaction or purchase index participation units if, immediately after the transaction, more than 10 percent of the net assets of the mutual fund, taken at market value at the time of the transaction, would be invested in securities of any issuer.

(2) Subsection (1) does not apply to a purchase of a government security or a security issued by a clearing corporation.

(3) In determining a mutual fund's compliance with the restrictions contained in this section, the mutual fund shall, for each long position in a specified derivative that is held by the mutual fund for purposes other than hedging and for each index participation unit held by the mutual fund, consider that it holds directly the underlying interest of that specified derivative or its proportionate share of the securities held by the issuer of the index participation unit.

(4) Despite subsection (3), the mutual fund shall not include in the determination referred to in subsection (3) a security or instrument that is a component of, but that represents less than 10 percent of

(a) a stock or bond index that is the underlying interest of a specified derivative; or

(b) the securities held by the issuer of an index participation unit.

2.2 Control Restrictions

(1) A mutual fund shall not

(a) purchase a security of an issuer if, immediately after the purchase, the mutual fund would hold securities representing more than 10 percent of

(i) the votes attaching to the outstanding voting securities of that issuer; or

(ii) the outstanding equity securities of that issuer; or

(b) purchase a security for the purpose of exercising control over or management of the issuer of the security.

(2) If a mutual fund acquires a security of an issuer other than as the result of a purchase, and the acquisition results in the mutual fund exceeding the limits described in paragraph (1)(a), the mutual fund shall as quickly as is commercially reasonable, and in any event no later than 90 days after the acquisition, reduce its holdings of those securities so that it does not hold securities exceeding those limits.

(3) In determining its compliance with the restrictions contained in this section, a mutual fund shall

(a) assume the conversion of special warrants held by it; and

(b) consider that it holds directly the underlying securities represented by any American depositary receipts held by it.

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

(a) purchase real property;

(b) purchase a mortgage, other than a guaranteed mortgage;

(c) purchase a guaranteed mortgage if, immediately after the purchase, more than 10 percent of the net assets of the mutual fund, taken at market value at the time of the purchase, would consist of guaranteed mortgages;

(d) purchase a gold certificate, other than a permitted gold certificate;

(e) purchase gold or a permitted gold certificate if, immediately after the purchase, more than 10 percent of the net assets of the mutual fund, taken at market value at the time of the purchase, would consist of gold and permitted gold certificates;

(f) except to the extent permitted by paragraphs (d) and (e), purchase a physical commodity;

(g) purchase, sell or use a specified derivative other than in compliance with sections 2.7 to 2.11;

(h) purchase, sell or use a specified derivative the underlying interest of which is

(i) a physical commodity other than gold, or

(ii) a specified derivative of which the underlying interest is a physical commodity other than gold; or

(i) purchase an interest in a loan syndication or loan participation if the purchase would require the mutual fund to assume any responsibilities in administering the loan in relation to the borrower.

2.4 Restrictions Concerning Illiquid Assets

(1) A mutual fund shall not purchase an illiquid asset if, immediately after the purchase, more than 10 percent of the net assets of the mutual fund, taken at market value at the time of the purchase, would consist of illiquid assets.

(2) A mutual fund shall not have invested, for a period of 90 days or more, more than 15 percent of its net assets, taken at market value, in illiquid assets.

(3) If more than 15 percent of the net assets of a mutual fund, taken at market value, are illiquid assets, the mutual fund shall, as quickly as is commercially reasonable, take all necessary steps to reduce the percentage of its net assets made up of illiquid assets to 15 percent or less.

2.5 Investments in Other Mutual Funds

(1) A mutual fund shall not purchase a security of another mutual fund unless

(a) immediately after the purchase, not more than 10 percent of the net assets of the mutual fund, taken at market value at the time of the purchase, would be invested in securities of other mutual funds,

(b) there is no duplication of management fees, incentive fees and sales charges between the mutual funds and this is described in the simplified prospectus of the mutual fund, and

(c) either

(i) the other mutual fund is qualified for distribution under a simplified prospectus in the jurisdictions in which the securities of the mutual fund are qualified for distribution under a simplified prospectus, or

(ii) the other mutual fund was established with the approval of the government of a foreign jurisdiction, the only means by which the mutual fund may invest in the securities of issuers of that foreign jurisdiction is through a mutual fund so established, and there is disclosure in the simplified prospectus of the mutual fund of the risk factors that may be associated with the investment in that foreign jurisdiction.

(2) Subsection (1) does not apply to the purchase of

(a) an index participation unit that is a security of a mutual fund; or

(b) a mutual fund that is listed and posted for trading on a Canadian stock exchange.

2.6 Investment Practices - A mutual fund shall not

(a) borrow cash or provide a security interest over any of its portfolio assets unless

(i) the transaction is a temporary measure to accommodate requests for the redemption of securities of the mutual fund while the mutual fund effects an orderly liquidation of portfolio assets, or to permit the mutual fund to settle portfolio transactions and, after giving effect to all transactions undertaken under this subparagraph, the outstanding amount of all borrowings of the mutual fund does not exceed five percent of the net assets of the mutual fund taken at market value at the time of the borrowing,

(ii) the security interest is required to enable the mutual fund to effect a specified derivative transaction under this Instrument, is made in accordance with industry practice for that type of transaction and relates only to obligations arising under that particular specified derivatives transaction, or

(iii) the security interest secures a claim for the fees and expenses of the custodian or a sub-custodian of the mutual fund for services rendered in that capacity as permitted by subsection 6.4(3);

(b) purchase securities on margin, unless permitted by section 2.7 or 2.8;

(c) sell securities short, unless permitted by section 2.7 or 2.8;

(d) purchase a security, other than a specified derivative, that by its terms may require the mutual fund to make a contribution in addition to the payment of the purchase price;

(e) engage in the business of underwriting, or marketing to the public, securities of any other issuer;

(f) lend cash or portfolio assets other than cash;

(g) guarantee securities or obligations of a person or company; or

(h) purchase securities other than through market facilities through which these securities are normally bought and sold unless the purchase price approximates the prevailing market price or the parties are at arm's length in connection with the transaction.

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

(1) A mutual fund shall not purchase an option that is not a clearing corporation option or enter into a swap or a forward contract unless

(a) the option, swap or contract has a remaining term to maturity of

(i) three years or less, or

(ii) between three and five years if, at the time of the transaction, the option, swap or contract provides the mutual fund with a right, at its election, to eliminate its exposure under the option, swap or contract no later than three years after the mutual fund has purchased the option or entered into the swap or contract; and

(b) at the time of the transaction, the option, swap or contract, or equivalent debt of the counterparty, or of a person or company that has fully and unconditionally guaranteed the obligations of the counterparty in respect of the option, swap or contract, has an approved credit rating.

(2) If the credit rating of an option that is not a clearing corporation option, the credit rating of a swap or forward contract, or the credit rating of the equivalent debt of the writer or guarantor of the option, swap or contract, falls below the level of approved credit rating while the option, swap or contract is held by a mutual fund, the mutual fund shall take the steps that are reasonably required to close out its position in the option, swap or contract in an orderly and timely fashion.

(3) Despite any other provisions contained in this Part, a mutual fund may enter into a trade to close out all or part of a position in a specified derivative, in which case the cash cover held to cover the underlying market exposure of the part of the position that is closed out may be released.

(4) The mark-to-market value of the exposure of a mutual fund under its specified derivatives positions with any one counterparty other than an acceptable clearing corporation or a clearing corporation that clears and settles transactions made on a futures exchange listed in Appendix A, calculated in accordance with subsection (5), shall not exceed, for a period of 30 days or more, 10 percent of the net assets of the mutual fund.

(5) The mark-to-market value of specified derivatives positions of a mutual fund with any one counterparty shall be, for the purposes of subsection (4),

(a) if the mutual fund has an agreement with the counterparty that provides for netting or the right of set-off, the net mark-to-market value of the specified derivatives positions of the mutual fund; and

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

2.8 Transactions in Specified Derivatives for Purposes Other than Hedging

(1) A mutual fund shall not

(a) purchase a debt-like security that has an options component or an option, unless, immediately after the purchase, not more than 10 percent of the net assets of the mutual fund, taken at market value at the time of the purchase, would consist of those instruments held for purposes other than hedging;

(b) write a call option, or have outstanding a written call option, that is not an option on futures unless, as long as the position remains open, the mutual fund holds

(i) an equivalent quantity of the underlying interest of the option,

(ii) a right or obligation, exercisable at any time that the option is exercisable, to acquire an equivalent quantity of the underlying interest of the option, and cash cover that, together with margin on account for the position, is not less than the amount, if any, by which the strike price of the right or obligation to acquire the underlying interest exceeds the strike price of the option, or

(iii) a combination of the positions referred to in subparagraphs (i) and (ii) that is sufficient, without recourse to other assets of the mutual fund, to enable the mutual fund to satisfy its obligations to deliver the underlying interest of the option;

(c) write a put option, or have outstanding a written put option, that is not an option on futures, unless, as long as the position remains open, the mutual fund holds

(i) a right or obligation, exercisable at any time that the option is exercisable, to sell an equivalent quantity of the underlying interest of the option, and cash cover in an amount that, together with margin on account for the position, is not less than the amount, if any, by which the strike price of the option exceeds the strike price of the right or obligation to sell the underlying interest,

(ii) cash cover that, together with margin on account for the option position, is not less than the strike price of the option, or

(iii) a combination of the positions referred to in subparagraphs (i) and (ii) that is sufficient, without recourse to other assets of the mutual fund, to enable the mutual fund to acquire the underlying interest of the option;

(d) open or maintain a long position in a debt-like security that has a component that is a long position in a forward contract, or in a standardized future or forward contract, unless the mutual fund holds cash cover in an amount that, together with margin on account for the specified derivative and the market value of the specified derivative, is not less than, on a daily mark-to-market basis, the underlying market exposure of the specified derivative;

(e) open or maintain a short position in a standardized future or forward contract, unless the mutual fund holds

(i) an equivalent quantity of the underlying interest of the future or contract,

(ii) a right or obligation to acquire an equivalent quantity of the underlying interest of the future or contract and cash cover that together with margin on account for the position is not less than the amount, if any, by which the strike price of the right or obligation to acquire the underlying interest exceeds the forward price of the contract, or

(iii) a combination of the positions referred to in subparagraphs (i) and (ii) that is sufficient, without recourse to other assets of the mutual fund, to enable the mutual fund to deliver the underlying interest of the future or contract; or

(f) enter into, or maintain, a swap position unless

(i) for periods when the mutual fund would be entitled to receive payments under the swap, the mutual fund holds cash cover in an amount that, together with margin on account for the swap and the market value of the swap, is not less than, on a daily mark-to-market basis, the underlying market exposure of the swap; and

(ii) for periods when the mutual fund would be required to make payments under the swap, the mutual fund holds

(A) an equivalent quantity of the underlying interest of the swap,

(B) a right or obligation to acquire an equivalent quantity of the underlying interest of the swap and cash cover that, together with margin on account for the position, is not less than the aggregate amount of the obligations of the mutual fund under the swap, or

(C) a combination of the positions referred to in clauses (A) and (B) that is sufficient, without recourse to other assets of the mutual fund, to enable the mutual fund to satisfy its obligations under the swap.

(2) A mutual fund shall treat any synthetic cash position on any date as providing the cash cover equal to the notional principal value of a banker's acceptance then being accepted by a bank listed in Schedule I of the *Bank Act* (Canada) that would produce the same annualized return as the synthetic cash position is then producing.

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

2.10 Adviser Requirements

(1) If a portfolio adviser of a mutual fund receives advice from a non-resident sub-adviser concerning the use of options or standardized futures by the mutual fund, the mutual fund shall not invest in or use options or standardized futures unless

(a) the obligations and duties of the non-resident sub-adviser are set out in a written agreement with the portfolio adviser; and

(b) the portfolio adviser contractually agrees with the mutual fund to be responsible for any loss that arises out of the failure of the non-resident sub-adviser

(i) to exercise the powers and discharge the duties of its office honestly, in good faith and in the best interests of the mutual fund, and

(ii) to exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances.

(2) A mutual fund shall not relieve a portfolio adviser of the mutual fund from liability for loss for which the portfolio adviser has assumed responsibility under paragraph (1)(b) that arises out of the failure of the relevant non-resident sub-adviser

(a) to exercise the powers and discharge the duties of its office honestly, in good faith and in the best interests of the mutual fund, or

(b) to exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances.

(3) Despite subsection 4.4(3), a mutual fund may indemnify a portfolio adviser against legal fees, judgments and amounts paid in settlement, actually and reasonably incurred by that person or company in connection with services provided by a non-resident sub-adviser for which the portfolio adviser has assumed responsibility under paragraph (1)(b), only if

(a) those fees, judgments and amounts were not incurred as a result of a breach of the standard of care described in subsection (1) or (2); and

(b) the mutual fund has reasonable grounds to believe that the action or inaction that caused the payment of the fees, judgments and amounts paid in settlement was in the best interests of the mutual fund.

(4) A mutual fund shall not incur the cost of any portion of liability insurance that insures a person or company for a liability except to the extent that the person or company may be indemnified for that liability under this section.

2.11 Commencement of Use of Specified Derivatives by a Mutual Fund

(1) A mutual fund that has not used specified derivatives shall not begin using specified derivatives unless

(a) its simplified prospectus contains the disclosure required for mutual funds using derivatives; and

(b) the mutual fund has provided to its securityholders, not less than 60 days before it begins using specified derivatives, written notice that discloses its intent to begin using specified derivatives and the disclosure required for mutual funds using derivatives.

(2) A mutual fund is not required to provide the notice referred to in paragraph (1)(b) if each simplified prospectus of the mutual fund since the later of January 1, 1994 and its inception contains the disclosure required for mutual funds using specified derivatives.

PART 3 NEW MUTUAL FUNDS

3.1 Initial Investment in a New Mutual Fund

(1) No person or company shall file a simplified prospectus for a newly established mutual fund unless

(a) an investment of at least $150,000 in securities of the mutual fund has been made, and those securities are beneficially owned, before the time of filing by

(i) the manager, a portfolio adviser, a promoter or a sponsor of the mutual fund,

(ii) the partners, directors, officers or securityholders of any of the manager, a portfolio adviser, a promoter or a sponsor of the mutual fund, or

(iii) a combination of the persons or companies referred to subparagraphs (i) and (ii); or

(b) the simplified prospectus of the mutual fund states that the mutual fund will not issue securities other than those referred to in paragraph (a) unless subscriptions aggregating not less than $500,000 have been received by the mutual fund from investors other than the persons and companies referred to in paragraph (a) and accepted by the mutual fund.

(2) A mutual fund shall not redeem a security issued upon an investment in the mutual fund referred to in paragraph (1)(a) until $500,000 has been received from persons or companies other than the persons and companies referred to in paragraph (1)(a).

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

3.3 Prohibition Against Reimbursement of Organization Costs - None of the costs of incorporation, formation or initial organization of a mutual fund, or of the preparation and filing of any of the preliminary simplified prospectus, preliminary annual information form, initial simplified prospectus or annual information form of the mutual fund shall be borne by the mutual fund or its securityholders.

PART 4 CONFLICTS OF INTEREST

4.1 Prohibited Investments

(1) A dealer managed mutual fund shall not knowingly make an investment in a class of securities of an issuer during, or for 60 days after, the period in which the dealer manager of the mutual fund, or an associate or affiliate of the dealer manager of the mutual fund, acts as an underwriter in the distribution of securities of that class of securities, except as a member of the selling group distributing five percent or less of the securities underwritten.

(2) A dealer managed mutual fund shall not knowingly make an investment in a class of securities of an issuer of which a partner, director, officer or employee of the dealer

manager of the mutual fund, or a partner, director, officer or employee of an affiliate or associate of the dealer manager, is a partner, director or officer, unless the partner, director, officer or employee

(a) does not participate in the formulation of investment decisions made on behalf of the dealer managed mutual fund;

(b) does not have access before implementation to information concerning investment decisions made on behalf of the dealer managed mutual fund; and

(c) does not influence, other than through research, statistical and other reports generally available to clients, the investment decisions made on behalf of the dealer managed mutual fund.

(3) Subsections (1) and (2) do not apply to an investment in a class of securities issued or fully and unconditionally guaranteed by the government of Canada or the government of a jurisdiction.

4.2 **Self-Dealing** - A mutual fund shall not purchase a security from, or sell a security to, any of the following persons or companies, if that person or company would be selling to the mutual fund, or purchasing from the mutual fund, as principal:

1. The manager, portfolio adviser or trustee of the mutual fund.

2. A partner, director or officer of the mutual fund or of the manager, portfolio adviser or trustee of the mutual fund.

3. An associate or affiliate of a person or company referred to in paragraph 1 or 2.

4. A person or company, having fewer than 100 securityholders of record, of which a partner, director or officer of the mutual fund or a partner, director or officer of the manager or portfolio adviser of the mutual fund is a partner, director, officer or securityholder.

4.3 **Exception** - Section 4.2 does not apply to a purchase or sale of a security by a mutual fund if the price payable for the security is

(a) not more than the ask price of the security as reported by any available public quotation in common use, in the case of a purchase by the mutual fund; or

(b) not less than the bid price of the security as reported by any available public quotation in common use, in the case of a sale by the mutual fund.

4.4 **Liability and Indemnification**

(1) An agreement or declaration of trust by which a person or company acts as manager of a mutual fund shall provide that the manager is responsible for any loss that arises out of the failure of the manager, or of any person or company retained by the manager or the mutual fund to discharge any of the manager's responsibilities to the mutual fund,

(a) to exercise the powers and discharge the duties of its office honestly, in good faith and in the best interests of the mutual fund, and

(b) to exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances.

(2) A mutual fund shall not relieve the manager of the mutual fund from liability for loss that arises out of the failure of the manager, or of any person retained by the manager or the mutual fund to discharge any of the manager's responsibilities to the mutual fund,

(a) to exercise the powers and discharge the duties of its office honestly, in good faith and in the best interests of the mutual fund, or

(b) to exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances.

(3) A mutual fund may indemnify a person or company providing services to it against legal fees, judgments and amounts paid in settlement, actually and reasonably incurred by that person or company in connection with services provided by that person or company to the mutual fund, if

(a) those fees, judgments and amounts were not incurred as a result of a breach of the standard of care described in subsection (1) or (2); and

(b) the mutual fund has reasonable grounds to believe that the action or inaction that caused the payment of the fees, judgments and amounts paid in settlement was in the best interests of the mutual fund.

(4) A mutual fund shall not incur the cost of any portion of liability insurance that insures a person or company for a liability except to the

extent that the person or company may be indemnified for that liability under this section.

(5) This section does not apply to any losses to a mutual fund or securityholder arising out of an action or inaction by a custodian or sub-custodian of the mutual fund or by a director of the mutual fund.

PART 5 FUNDAMENTAL CHANGES

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

(a) the basis of the calculation of a fee or expense that is charged to the mutual fund is changed in a way that could result in an increase in charges to the mutual fund;

(b) the manager of the mutual fund is changed, unless the new manager is an affiliate of the current manager;

(c) the fundamental investment objectives of the mutual fund are changed;

(d) the auditor of the mutual fund is changed;

(e) the mutual fund decreases the frequency of the calculation of its net asset value per security;

(f) the mutual fund undertakes a reorganization with, or transfers its assets to, another mutual fund, if

(i) the mutual fund ceases to continue after the reorganization or transfer of assets, and

(ii) the transaction results in the securityholders of the mutual fund becoming securityholders in the other mutual fund; or

(g) the mutual fund undertakes a reorganization with, or acquires assets from, another mutual fund, if

(i) the mutual fund continues after the reorganization or acquisition of assets,

(ii) the transaction results in the securityholders of the other mutual fund becoming securityholders in the mutual fund, and

(iii) the transaction would be a significant change to the mutual fund.

5.2 Approval of Securityholders

(1) Unless a greater majority is required by the constating documents of the mutual fund, the laws applicable to the mutual fund or an applicable agreement, the approval of the securityholders of the mutual fund to a matter referred to in section 5.1 shall be given by a resolution passed by at least a majority of the votes cast at a meeting of the securityholders of the mutual fund duly called and held to consider the matter.

(2) Despite subsection (1), the holders of securities of a class or series of a class of securities of a mutual fund shall vote separately as a class or series of a class on a matter referred to in section 5.1 if that class or series of a class is affected by the action referred to in section 5.1 in a manner different from holders of securities of other classes or series of a class.

(3) Despite section 5.1 and subsections (1) and (2), if the constating documents of the mutual fund so provide, the holders of securities of a class or series of a class of securities of a mutual fund shall not be entitled to vote on a matter referred to in section 5.1 if they, as holders of the class or series of a class, are not affected by the action referred to in section 5.1.

5.3 Circumstances in Which Approval of Securityholders Not Required

(1) Despite section 5.1, the approval of securityholders of a mutual fund is not required to be obtained for a change referred to in paragraph 5.1(a)

(a) if

(i) the mutual fund is at arm's length to the person or company charging the fee or expense to the mutual fund referred to in paragraph 5.1(a) that is changed,

(ii) the simplified prospectus of the mutual fund discloses that, although the approval of securityholders will not be obtained before making the changes, securityholders will be sent a written notice at least 60 days before the effective date of the change that is to be made that could result in an increase in charges to the mutual fund, and

(iii) the notice referred to in subparagraph (ii) is actually sent

60 days before the effective date of the change; or

(b) if

(i) the mutual fund is permitted by this Instrument to be described as a "no-load" fund,

(ii) the simplified prospectus of the mutual fund discloses that securityholders will be sent a written notice at least 60 days before the effective date of a change that is to be made that could result in an increase in charges to the mutual fund, and

(iii) the notice referred to in subparagraph (ii) is actually sent 60 days before the effective date of the change.

5.4 Formalities Concerning Meetings of Securityholders

(1) A meeting of securityholders of a mutual fund called to consider any matter referred to in section 5.1 shall be called on written notice sent not less than 21 days before the date of the meeting.

(2) The notice referred to in subsection (1) shall contain or be accompanied by a statement that includes

(a) a description of the change or transaction proposed to be made or entered into and, if the matter is one referred to in paragraph 5.1(a), the effect that the change would have had on the management expense ratio of the mutual fund had the change been in force throughout the mutual fund's last completed financial year;

(b) the date of the proposed implementation of the change or transaction; and

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

5.5 Approval of Securities Regulatory Authority

(1) The approval of the securities regulatory authority is required before

(a) the manager of a mutual fund is changed, unless the new manager is an affiliate of the current manager;

(b) a reorganization or transfer of assets of a mutual fund is implemented, if the transaction will result in the securityholders of the mutual fund becoming securityholders in another mutual fund;

(c) a change of the custodian of a mutual fund is implemented, if there has been or will be, in connection with the proposed change, a change of the type referred to in paragraph (a); or

(d) a mutual fund suspends, other than under section 10.6, the rights of securityholders to request that the mutual fund redeem their securities.

(2) No person or company, or affiliate or associate of that person or company, may act as manager of a mutual fund if that person or company, or an affiliate or associate of that person or company, has acquired control of a manager of the mutual fund unless the approval of the securities regulatory authority has been obtained for the change in control.

5.6 Pre-Approved Reorganizations and Transfers

(1) Despite subsection 5.5(1), the approval of the securities regulatory authority is not required to implement a transaction referred to in paragraph 5.5(1)(b) if

(a) the mutual fund is being reorganized with, or its assets are being transferred to, another mutual fund to which this Instrument applies and that

(i) is managed by the manager, or an affiliate of the manager, of the mutual fund,

(ii) a reasonable person would consider to have substantially similar fundamental investment objectives, valuation procedures and fee structure as the mutual fund,

(iii) is not in default of any requirement of securities legislation, and

(iv) has a current simplified prospectus in the local jurisdiction;

(b) the transaction is a "qualifying exchange" within the meaning of section 132.2 of the ITA or is a tax-deferred transaction under subsection 85(1), 85.1(1), 86(1) or 87(1) of the ITA;

(c) the transaction contemplates the wind-up of the mutual fund as soon as reasonably possible following the transaction;

(d) the portfolio assets of the mutual fund to be acquired by the other mutual fund as part of the transaction

(i) may be acquired by the other mutual fund in compliance with this Instrument, and

(ii) are acceptable to the portfolio adviser of the other mutual fund and consistent with the other mutual fund's fundamental investment objectives;

(e) the transaction is approved

(i) by the securityholders of the mutual fund in accordance with paragraph 5.1(f), and

(ii) if required, by the securityholders of the other mutual fund in accordance with paragraph 5.1(g);

(f) the materials sent to securityholders of the mutual fund in connection with the approval under paragraph 5.1(f) include

(i) a circular that, in addition to other requirements prescribed by law, describes the proposed transaction, the mutual fund into which the mutual fund will be reorganized, the income tax considerations for the mutual funds participating in the transaction and their securityholders, and, if the mutual fund is a corporation and the transaction involves its shareholders becoming securityholders of a mutual fund that is established as a trust, a description of the material differences between being a shareholder of a corporation and being a securityholder of a trust,

(ii) if not previously sent to all securityholders, the current simplified prospectus and the most recent annual and interim financial statements that have been made public for the mutual fund into which the mutual fund will be reorganized, and

(iii) a statement that securityholders may obtain an annual information form for the mutual fund into which the mutual fund will be reorganized by contacting that mutual fund at a specified address or telephone number;

(g) the mutual fund has complied with section 5.10 in connection with the making of the decision to proceed with the transaction by the board of directors of the manager of the mutual fund or of the mutual fund;

(h) the mutual funds participating in the transaction bear none of the costs and expenses associated with the transaction; and

(i) securityholders of the mutual fund continue to have the right to redeem securities of the mutual fund up to the close of business on the business day immediately before the effective date of the transaction.

(2) A mutual fund that has continued after a transaction described in paragraph 5.5(1)(b) shall, if the audit report accompanying its audited financial statements for its first completed financial year after the transaction contains a reservation in respect of the value of the portfolio assets acquired by the mutual fund in the transaction, send a copy of those financial statements to each person or company that was a securityholder of a mutual fund that was terminated as a result of the transaction and that is not a securityholder of the mutual fund.

5.7 Applications

(1) An application for an approval required under section 5.5 shall contain,

(a) if the application is required by paragraph 5.5(1)(a) or subsection 5.5(2),

(i) details of the proposed transaction,

(ii) details of the proposed new manager or the person or company proposing to acquire control of the manager,

(iii) as applicable, the names, residence addresses and birthdates of

(A) all proposed new partners, directors or

officers of the manager,

(B) all partners, directors or officers of the person or company proposing to acquire control of the manager,

(C) any proposed new individual trustee of the mutual fund, and

(D) any new directors or officers of the mutual fund,

(iv) all information necessary to permit the securities regulatory authority to conduct security checks on the individuals referred to in subparagraph (iii),

(v) sufficient information to establish the integrity and experience of the persons or companies referred to in subparagraphs (ii) and (iii), and

(vi) details of how the proposed transaction will affect the management and administration of the mutual fund;

(b) if the application is required by paragraph 5.5(1)(b),

(i) details of the proposed transaction,

(ii) details of the total annual returns of each of the mutual funds for each of the previous five years,

(iii) a description of the differences between the fundamental investment objectives, investment strategies, valuation procedures and fee structure of each of the mutual funds and any other material differences between the mutual funds, and

(iv) a description of those elements of the proposed transaction that make section 5.6 inapplicable;

(c) if the application is required by paragraph 5.5(1)(c), sufficient information to establish that the proposed custodial arrangements will be in compliance with Part 6;

(d) if the application relates to a matter that would constitute a significant change for the mutual fund, a draft of an amendment to the simplified prospectus of the mutual fund reflecting the change; and

(e) if the matter is one that requires the approval of securityholders, confirmation that the approval has been obtained or will be obtained before the change is implemented.

(2) A mutual fund that applies for an approval under paragraph 5.5(1)(d) shall

(a) make that application to the securities regulatory authority or regulator in the jurisdiction in which the head office or registered office of the mutual fund is situate; and

(b) concurrently file a copy of the application so made with the securities regulatory authority or the regulator in the local jurisdiction if the head office or registered office of the mutual fund is not situated in the local jurisdiction.

(3) A mutual fund that has complied with subsection (2) in the local jurisdiction may suspend the right of securityholders to request that the mutual fund redeem their securities if

(a) the securities regulatory authority or regulator in the jurisdiction in which the head office or registered office of the mutual fund is situate has granted approval to the application made under paragraph (2)(a); and

(b) the securities regulatory authority or regulator in the local jurisdiction has not notified the mutual fund, by the close of business on the business day immediately following the day on which the copy of the application referred to in paragraph (2)(b) was received, either that

(i) the securities regulatory authority or regulator has refused to grant approval to the application, or

(ii) this subsection may not be relied upon by the mutual fund in the local jurisdiction.

5.8 Matters Requiring Notice

(1) No person or company that is a manager of a mutual fund may continue to act as manager of the mutual fund following a direct or indirect

change of control of the person or company unless

(a) notice of the change of control was given to all securityholders of the mutual fund at least 60 days before the change; and

(b) the notice referred to in paragraph (a) contains the information that would be required by law to be provided to securityholders if securityholder approval of the change were required to be obtained.

(2) No mutual fund shall terminate unless notice of the termination is given to all securityholders of the mutual fund at least 60 days before termination.

(3) The manager of a mutual fund that has terminated shall give notice of the termination to the securities regulatory authority within 30 days of the termination.

5.9 Relief from Certain Regulatory Requirements

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

(2) The mutual fund conflict of interest investment restrictions and the mutual fund conflict of interest reporting requirements do not apply to a transaction described in section 5.6.

5.10 Significant Changes - Upon the occurrence of a significant change with respect to a mutual fund, the mutual fund shall

(a) comply with the timely disclosure requirements in connection with the significant change as if the significant change were a material change in the affairs of the mutual fund; and

(b) file an amendment to its simplified prospectus that discloses the significant change in accordance with the requirements of securities legislation as if the amendment were required to be filed under securities legislation.

PART 6 CUSTODIANSHIP OF PORTFOLIO ASSETS

6.1 General

(1) Except as provided in sections 6.8 and 6.9, all portfolio assets of a mutual fund shall be held under the custodianship of one custodian that satisfies the requirements of section 6.2.

(2) Except as provided in subsection 6.5(3) and sections 6.8 and 6.9, portfolio assets of a mutual fund shall be held

(a) in Canada by the custodian or a sub-custodian of the mutual fund; or

(b) outside Canada by the custodian or a sub-custodian of the mutual fund, if appropriate to facilitate portfolio transactions of the mutual fund outside Canada.

(3) The custodian or a sub-custodian of a mutual fund may appoint one or more sub-custodians to hold portfolio assets of the mutual fund, if, for each appointment,

(a) written consent to the appointment has been provided by the mutual fund and, if the appointment is by a sub-custodian, the custodian of the mutual fund;

(b) the sub-custodian that is to be appointed is a person or company described in section 6.2 or 6.3, as applicable;

(c) the arrangements under which a sub-custodian is appointed are such that the mutual fund may enforce rights directly, or require the custodian or a sub-custodian to enforce rights on behalf of the mutual fund, to the portfolio assets held by the appointed sub-custodian; and

(d) the appointment is otherwise in compliance with this Instrument.

(4) The written consent referred to in paragraph (3)(a) may be in the form of a general consent, contained in the agreement governing the relationship between the mutual fund and the custodian, or the custodian and the sub-custodian, to the appointment of persons or companies that are part of an international network of sub-custodians within the organization of the appointed custodian or sub-custodian.

(5) A custodian or sub-custodian shall provide to the mutual fund a list of each person or company that is appointed sub-custodian under a general consent referred to in subsection (4).

(6) Despite any other provisions of this Part, the manager of a mutual fund shall not act as custodian or sub-custodian of the mutual fund.

6.2 Entities Qualified to Act as Custodian or Sub-Custodian for Assets Held in Canada - The custodian of a mutual fund, and a sub-custodian of a

mutual fund that is to hold portfolio assets of the mutual fund in Canada, shall be one of the following:

1. A bank listed in Schedule I or II of the *Bank Act* (Canada).

2. A trust company that is incorporated under the laws of Canada or a jurisdiction and licensed or registered under the laws of Canada or a jurisdiction, and that has shareholders' equity, as reported in its most recent audited financial statements, of not less than $10,000,000.

3. A company that is incorporated under the laws of Canada or of a jurisdiction, and that is an affiliate of a bank or trust company referred to in paragraph 1 or 2, if

   (a) the company has shareholders' equity, as reported in its most recent audited financial statements that have been made public, of not less than $10,000,000; or

   (b) the bank or trust company has assumed responsibility for all of the custodial obligations of the company in respect of that mutual fund.

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

1. An entity referred to in section 6.2.

2. An entity that

   (a) is incorporated or organized under the laws of a country, or a political subdivision of a country, other than Canada;

   (b) is regulated as a banking institution or trust company by the government, or an agency of the government, of the country under whose laws it is incorporated or organized or a political subdivision of that country; and

   (c) has shareholders' equity, as reported in its most recent audited financial statements, of not less than the equivalent of $100,000,000.

3. An affiliate of an entity referred to in paragraph 1 or 2 if

   (a) the affiliate has shareholders' equity, as reported in its most recent audited financial statements that have been made public, of not less than the equivalent of $100,000,000; or

   (b) the entity referred to in paragraph 1 or 2 has assumed responsibility for all of the custodial obligations of the subsidiary in respect of that mutual fund.

6.4 Contents of Custodian and Sub-Custodian Agreements

(1) All custodian agreements and sub-custodian agreements of a mutual fund shall provide for matters relating to

   (a) the requirements concerning the location of portfolio assets contained in subsection 6.1(2);

   (b) the appointment of a sub-custodian required by subsection 6.1(3);

   (c) the requirements concerning lists of sub-custodians contained in subsection 6.1(5);

   (d) the method of holding portfolio assets required by section 6.5 and subsection 6.8(4);

   (e) the standard of care and responsibility for loss required by section 6.6; and

   (f) the review and compliance reports required by section 6.7.

(2) A sub-custodian agreement concerning the portfolio assets of a mutual fund shall provide for the safekeeping of portfolio assets on terms consistent with the custodian agreement of the mutual fund.

(3) No custodian agreement or sub-custodian agreement concerning the portfolio assets of a mutual fund shall

   (a) provide for the creation of any security interest on the portfolio assets of the mutual fund except for a good faith claim for payment of the fees and expenses of the custodian or sub-custodian for acting in that capacity or to secure the obligations of the mutual fund to repay borrowings by the mutual fund from a custodian or sub-custodian for the purpose of settling portfolio transactions; or

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

6.5 Holding of Portfolio Assets and Payment of Fees

(1) Except as provided in subsections (2) and (3) and sections 6.8 and 6.9, portfolio assets of a mutual fund not registered in the name of the mutual fund shall be registered in the name of the custodian or a sub-custodian of the mutual fund or any of their respective nominees with an account number or other designation in the records of the custodian sufficient to show that the beneficial ownership of the portfolio assets is vested in the mutual fund.

(2) Portfolio assets of a mutual fund issued in bearer form shall be designated or segregated by the custodian or a sub-custodian of the mutual fund or the applicable nominee so as to show that the beneficial ownership of the property is vested in the mutual fund.

(3) A custodian or sub-custodian of a mutual fund may deposit portfolio assets of the mutual fund with a depository, or a clearing agency, that operates a book-based system.

(4) The custodian or sub-custodian of a mutual fund arranging for the deposit of portfolio assets of the mutual fund with, and their delivery to, a depository, or clearing agency, that operates a book-based system shall ensure that the records of any of the applicable participants in that book-based system or the custodian contain an account number or other designation sufficient to show that the beneficial ownership of the portfolio assets is vested in the mutual fund.

(5) A mutual fund shall not pay a fee to a custodian or sub-custodian for the transfer of beneficial ownership of portfolio assets of the mutual fund other than for safekeeping and administrative services in connection with acting as custodian or sub-custodian.

6.6 Standard of Care

(1) The custodian and each sub-custodian of a mutual fund, in carrying out their duties concerning the safekeeping of, and dealing with, the portfolio assets of the mutual fund, shall exercise

(a) the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances; or

(b) at least the same degree of care as they exercise with respect to their own property of a similar kind, if this is a higher degree of care than the degree of care referred to in paragraph (a).

(2) A mutual fund shall not relieve the custodian or a sub-custodian of the mutual fund from liability to the mutual fund or to a securityholder of the mutual fund for loss that arises out of the failure of the custodian or sub-custodian to exercise the standard of care imposed by subsection (1).

(3) A mutual fund may indemnify a custodian or sub-custodian against legal fees, judgments and amounts paid in settlement, actually and reasonably incurred by that entity in connection with custodial or sub-custodial services provided by that entity to the mutual fund, if those fees, judgments and amounts were not incurred as a result of a breach of the standard of care described in subsection (1).

(4) A mutual fund shall not incur the cost of any portion of liability insurance that insures a custodian or sub-custodian for a liability, except to the extent that the custodian or sub-custodian may be indemnified for that liability under this section.

6.7 Review and Compliance Reports

(1) The custodian of a mutual fund shall, on a periodic basis not less frequently than annually,

(a) review the custodian agreement and all sub-custodian agreements of the mutual fund to determine if those agreements are in compliance with this Part;

(b) make reasonable enquiries as to whether each sub-custodian satisfies the applicable requirements of section 6.2 or 6.3; and

(c) make or cause to be made any changes that may be necessary to ensure that

(i) the custodian and sub-custodian agreements are in compliance with this Part; and

(ii) all sub-custodians of the mutual fund satisfy the applicable requirements of section 6.2 or 6.3.

(2) The custodian of a mutual fund shall, not more than 60 days after the end of each financial year of the mutual fund, advise the mutual fund in writing

(a) of the names and addresses of all sub-custodians of the mutual fund;

(b) whether the custodian and sub-custodian agreements are in compliance with this Part; and

(c) whether, to the best of the knowledge and belief of the custodian, each sub-custodian satisfies the applicable requirements of section 6.2 or 6.3.

(3) A copy of the report referred to in subsection (2) shall be delivered by or on behalf of the mutual fund to the securities regulatory authority within 30 days after the filing of the annual financial statements of the mutual fund.

6.8 Custodial Provisions relating to Derivatives

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

(2) A mutual fund may deposit portfolio assets with a dealer as margin for transactions outside Canada involving clearing corporation options, options on futures or standardized futures if

(a) in the case of standardized futures and options on futures, the dealer is a member of a futures exchange or, in the case of clearing corporation options, is a member of a stock exchange, and, as a result in either case, is subject to a regulatory audit;

(b) the dealer has a net worth, determined from its most recent audited financial statements that have been made public, in excess of the equivalent of $50 million; and

(c) the amount of margin deposited does not, when aggregated with the amount of margin already held by the dealer on behalf of the mutual fund, exceed 10 percent of the net assets of the mutual fund, taken at market value as at the time of deposit.

(3) A mutual fund may deposit with its counterparty portfolio assets over which it has granted a security interest in connection with a particular specified derivatives transaction.

(4) The agreement by which portfolio assets of a mutual fund are deposited in accordance with this section shall require the person or company holding portfolio assets of the mutual fund so deposited to ensure that its records show that mutual fund is the beneficial owner of the portfolio assets.

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

PART 7 INCENTIVE FEES

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

(a) the fee is calculated with reference to a benchmark or index that

(i) reflects the market sectors in which the mutual fund invests according to its fundamental investment objectives,

(ii) is available to persons or companies other than the mutual fund and persons providing services to it, and

(iii) is a total return benchmark or index;

(b) the payment of the fee is based upon a comparison of the cumulative total return of the mutual fund against the cumulative total percentage increase or decrease of the benchmark or index for the period that began immediately after the last period for which the performance fee was paid; and

(c) the method of calculation of the fee and details of the composition of the benchmark or index are described in the simplified prospectus of the mutual fund.

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

PART 8 CONTRACTUAL PLANS

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

(a) the contractual plan was established, and its terms described in a prospectus or simplified prospectus that was filed with the securities regulatory authority, before the date that this Instrument came into force;

(b) there have been no changes made to the contractual plan or the rights of securityholders under the contractual plan since the date that this Instrument came into force; and

(c) the contractual plan has continued to be operated in the same manner after the date that this Instrument came into force as it was on that date.

PART 9 SALE OF SECURITIES OF A MUTUAL FUND

9.1 Transmission and Receipt of Purchase Orders

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

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

(3) Despite subsections (1) and (2), a purchase order for securities of a mutual fund received at a location referred to in those subsections after normal business hours on a business day, or on a day that is not a business day, may be sent, in the manner and to the place required by those subsections, on the next business day.

(4) A participating dealer or principal distributor that sends purchase orders electronically may

(a) specify a time on a business day by which a purchase order must be received in order that it be sent electronically on that business day; and

(b) despite subsections (1) and (2), send electronically on the next business day a purchase order received after the time so specified.

(5) A mutual fund is deemed to have received a purchase order for securities of the mutual fund when the order is received at an order receipt office of the mutual fund.

(6) Despite subsection (5), a mutual fund may provide that a purchase order for securities of the mutual fund received at an order receipt office of the mutual fund after a specified time on a business day, or on a day that is not a business day, will be considered to be received by the mutual fund on the next business day following the day of actual receipt.

(7) A principal distributor or participating dealer shall ensure that a copy of each purchase order received in a jurisdiction is sent, by the time it is sent to the order receipt office of the mutual fund under subsection (2), to a person responsible for the supervision of trades made on behalf of clients for the principal distributor or participating dealer in the jurisdiction.

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

(a) the rejection of the order is made no later than one business day after receipt by the mutual fund of the order;

(b) on rejection of the order, all cash received with the order is refunded immediately; and

(c) the simplified prospectus of the mutual fund states that the right to reject a purchase order for securities of the mutual fund is reserved and reflects the requirements of paragraphs (a) and (b).

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

9.4 Delivery of Funds and Settlement

(1) A principal distributor or participating dealer shall forward any cash received for payment of the issue price of securities of a mutual fund to an order receipt office of the mutual fund so that the cash arrives at the order receipt office as soon as practicable and in any event no later than the third business day after the pricing date.

(2) Payment of the issue price of securities of a mutual fund shall be made to the mutual fund on or before the third business day after the pricing date for the securities by

(a) a payment of cash in a currency in which the net asset value per security of the mutual fund is calculated; or

(b) good delivery of securities if

(i) the mutual fund would at the time of payment be permitted to purchase those securities,

(ii) the securities are acceptable to the portfolio adviser of the mutual fund and consistent with the mutual fund's investment objectives, and

(iii) the value of the securities is at least equal to the issue price of the securities of the mutual fund for which they are payment, valued as if the securities were portfolio assets of the mutual fund.

(3) If payment of the issue price of securities of a mutual fund is made by the good delivery of securities as contemplated by paragraph (2)(b), the statement of portfolio transactions next prepared by the mutual fund shall include a note providing details of the securities so delivered.

(4) If payment of the issue price of the securities of a mutual fund to which a purchase order pertains is not made on or before the third business day after the pricing date or if the mutual fund has been paid the issue price by a cheque or method of payment that is subsequently not honoured,

(a) the mutual fund shall redeem the securities to which the purchase order pertains as if it had received an order for the redemption of the securities immediately before the close of business on the fourth business day after the pricing date or on the day on which the mutual fund first knows that the method of payment will not be honoured; and

(b) the amount of the redemption proceeds derived from the redemption shall be applied to reduce the amount owing to the mutual fund on the purchase of the securities and any banking costs incurred by the mutual fund in connection with the dishonoured cheque.

(5) If the amount of the redemption proceeds referred to in subsection (4) exceeds the aggregate of issue price of the securities and any banking costs incurred by the mutual fund in connection with the dishonoured cheque, the difference shall belong to the mutual fund.

(6) If the amount of the redemption proceeds referred to in subsection (4) is less than the issue price of the securities and any banking costs incurred by the mutual fund in connection with the dishonoured cheque,

(a) if the mutual fund has a principal distributor, the principal distributor shall pay, immediately upon notification by the mutual fund, to the mutual fund the amount of the deficiency; or

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

PART 10 REDEMPTION OF SECURITIES OF A MUTUAL FUND

10.1 Requirements for Redemptions

(1) No mutual fund shall pay redemption proceeds unless

(a) if the security of the mutual fund to be redeemed is represented by a certificate, the mutual fund has received the certificate or appropriate indemnities in connection with a lost certificate; and

(b) either

(i) the mutual fund has received a written redemption order, duly completed and executed by or on behalf of the securityholder, or

(ii) the mutual fund permits the making of redemption orders by telephone or electronic means by, or on behalf of, a securityholder who has made prior arrangements with the mutual fund in that regard and the relevant redemption order is made in compliance with those arrangements.

(2) A mutual fund may establish reasonable requirements applicable to securityholders who wish to have the mutual fund redeem securities, not contrary to this Instrument, as to procedures to be followed and documents to be delivered

(a) by the time of delivery of a redemption order to an order receipt office of the mutual fund; or

(b) by the time of payment of redemption proceeds.

(3) The manager shall provide to securityholders of a mutual fund at least annually a statement outlining the requirements referred to in subsection (1) and established by the mutual fund under subsection (2), and containing

(a) detailed reference to all documentation required for redemption of securities of the mutual fund;

(b) detailed instructions on the manner in which documentation is to be delivered to participating dealers or the mutual fund;

(c) a description of all other procedural or communication requirements; and

(d) an explanation of the consequences of failing to meet timing requirements.

(4) The statement referred to in subsection (3) is not required to be separately provided, in any year, if the requirements are described in the mutual fund's annual financial statements or annual report, or in a simplified prospectus that is sent to all securityholders in that year.

10.2 Transmission and Receipt of Redemption Orders

(1) Each redemption order for securities of a mutual fund received by a participating dealer at a location that is not its principal office shall, on the day the order is received, be sent by same day or next day courier, same day or next day priority post, telephone or electronic means, without charge to the relevant securityholder or to the mutual fund, to the principal office of the participating dealer.

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

(3) Despite subsections (1) and (2), a redemption order for securities of a mutual fund received at a location referred to in those subsections after normal business hours on a business day, or on a day that is not a business day, may be sent, in the manner and to the place required by those subsections, on the next business day.

(4) A participating dealer or principal distributor that sends redemption orders electronically may

(a) specify a time on a business day by which a redemption order must be received in order that it be sent electronically on that business day; and

(b) despite subsections (1) and (2), send electronically on the next business day a redemption order received after the time so specified.

(5) A mutual fund is deemed to have received a redemption order for securities of the mutual fund when the order is received at an order receipt office of the mutual fund or all requirements of the mutual fund established under paragraph 10.1(2)(a) have been satisfied, whichever is later.

(6) If a mutual fund determines that its requirements established under paragraph 10.1(2)(a) have not been satisfied, the mutual fund shall notify the securityholder making the redemption order, by the close of business on the business day after the date of the delivery to the mutual fund of the incomplete redemption order, that its requirements established under paragraph 10.1(2)(a) have not been satisfied and shall specify procedures still to be followed or the documents still to be delivered by that securityholder.

(7) Despite subsection (5), a mutual fund may provide that orders for the redemption of securities that are received at an order receipt office of the mutual fund after a specified time on a business day, or on a day that is not a business day, will be considered to be received by the mutual fund on the next business day following the day of actual receipt.

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

10.4 Payment of Redemption Price

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

(a) within three business days after the date of calculation of the net asset

value per security used in establishing the redemption price; or

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

(i) the satisfaction of the relevant requirement, or

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

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

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

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

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

(4) If payment of the redemption price of securities of a mutual fund is made under paragraph (3)(b), the statement of portfolio transactions next prepared by the mutual fund shall include a note describing the portfolio assets delivered to the securityholder and the value assigned to the portfolio assets.

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

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

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

10.5 Failure to Complete Redemption Order

(1) If a requirement of a mutual fund referred to in subsection 10.1(1) or established under paragraph 10.1(2)(b) has not been satisfied on or before the close of business on the tenth business day after the date of the redemption of the relevant securities, and, in the case of a requirement established under paragraph 10.1(2)(b), the mutual fund does not waive satisfaction of the requirement, the mutual fund shall

(a) issue, to the person or company that immediately before the redemption held the securities that were redeemed, a number of securities equal to the number of securities that were redeemed, as if the mutual fund had received from the person or company on the tenth business day after the redemption, and accepted immediately before the close of business on the tenth business day after the redemption, an order for the purchase of that number of securities; and

(b) apply the amount of the redemption proceeds to the payment of the issue price of the securities.

(2) If the amount of the issue price of the securities referred to in subsection (1) is less than the redemption proceeds, the difference shall belong to the mutual fund.

(3) If the amount of the issue price of the securities referred to in subsection (1) exceeds the redemption proceeds

(a) if the mutual fund has a principal distributor, the principal distributor shall pay immediately to the mutual fund the amount of the deficiency;

(b) if the mutual fund does not have a principal distributor, the participating dealer that delivered the relevant redemption order to the mutual fund shall pay immediately to the mutual fund the amount of the deficiency; or

(c) if the mutual fund has no principal distributor and no dealer delivered the relevant redemption order to the mutual fund, the manager of the mutual fund shall pay immediately to the mutual fund the amount of the deficiency.

10.6 Suspension of Redemptions

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

(2) A mutual fund that has an obligation to pay the redemption price for securities that have been redeemed in accordance with subsection 10.4(1) may postpone payment during a period in which the right of securityholders to request redemption of their securities is suspended, whether that suspension was made under subsection (1) or pursuant to an approval of the securities regulatory authority.

(3) A mutual fund shall not accept a purchase order for securities of the mutual fund during a period in which it is exercising rights under subsection (1) or at a time in which it is relying on an approval of the securities regulatory authorities contemplated by paragraph 5.5(1)(d).

PART 11 COMMINGLING OF CASH

11.1 Principal Distributors

(1) Cash received by a principal distributor of a mutual fund, or by a person or company providing services to the mutual fund or the principal distributor, for investment in, or on the redemption of, securities of the mutual fund, or on the distribution of assets of the mutual fund, until disbursed as permitted by subsection (3),

(a) shall be accounted for separately and be deposited in a trust account or trust accounts established and maintained in accordance with the requirements of section 11.3; and

(b) may be commingled only with cash received by the principal distributor or service provider for the sale or on the redemption of other mutual fund securities.

(2) Except as permitted by subsection (3), the principal distributor or person or company providing services to the mutual fund or principal distributor shall not use any of the cash referred to in subsection (1) to finance its own or any other operations in any way.

(3) The principal distributor or person or company providing services to a mutual fund or principal distributor may withdraw cash from a trust account referred to in paragraph (1)(a) for the purpose of

(a) remitting to the mutual fund the amount or, if subsection (5) applies, the net amount, to be invested in the securities of the mutual fund;

(b) remitting to the relevant persons or companies redemption or distribution proceeds being paid on behalf of the mutual fund; or

(c) paying fees, charges and expenses that are payable by an investor in connection with the purchase, conversion, holding, transfer or redemption of securities of the mutual fund.

(4) All interest earned on cash held in a trust account referred to in paragraph (1)(a) shall be paid to securityholders or to each of the mutual funds to which the trust account pertains, pro rata based on cash flow,

(a) no less frequently than monthly if the amount owing to a mutual fund or to a securityholder is $10 or more; and

(b) no less frequently than once a year.

(5) When making payments to a mutual fund, the principal distributor or service provider may offset the proceeds of redemption of securities of the mutual fund or amounts held for distributions to be paid on behalf of the mutual fund held in the trust account against amounts held in the trust account for investment in the mutual fund.

11.2 Participating Dealers

(1) Cash received by a participating dealer, or by a person or company providing services to a participating dealer, for investment in, or on the redemption of, securities of a mutual fund, or on the distribution of assets of a mutual fund, until disbursed as permitted by subsection (3)

(a) shall be accounted for separately and shall be deposited in a trust account or trust accounts established and maintained in accordance with section 11.3; and

(b) may be commingled only with cash received by the participating dealer or service provider for the sale or on the redemption of other mutual fund securities.

(2) Except as permitted by subsection (3), the participating dealer or person or company providing services to the participating dealer shall not use any of the cash referred to subsection (1) to finance its own or any other operations in any way.

(3) A participating dealer or person or company providing services to the participating dealer may withdraw cash from a trust account referred to in paragraph (1)(a) for the purpose of

(a) remitting to the mutual fund or the principal distributor of the mutual fund the amount or, if subsection (5) applies, the net amount, to be invested in the securities of the mutual fund;

(b) remitting to the relevant persons or companies redemption or distribution proceeds being paid on behalf of the mutual fund; or

(c) paying fees, charges and expenses that are payable by an investor in connection with the purchase, conversion, holding, transfer or redemption of securities of the mutual fund.

(4) All interest earned on cash held in a trust account referred to in paragraph (1)(a) shall be paid to securityholders or to each of the mutual funds to which the trust account pertains, pro rata based on cash flow,

(a) no less frequently than monthly if the amount owing to a mutual fund or to a securityholder is $10 or more; and

(b) no less frequently than once a year.

(5) When making payments to a mutual fund, a participating dealer or service provider may offset the proceeds of redemption of securities of the mutual fund and amounts held for distributions to be paid on behalf of a mutual fund held in the trust account against amounts held in the trust account for investment in the mutual fund.

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

11.3 Trust Accounts - A principal distributor or participating dealer that deposits cash into a trust account in accordance with section 11.1 or 11.2 shall

(a) advise, in writing, the financial institution with which the account is opened at the time of the opening of the account that

(i) the account is established for the purpose of holding client funds in trust,

(ii) the account is to be labelled by the financial institution as a "trust account",

(iii) the account is not to be accessed by any person other than authorized representatives of the principal distributor or participating dealer, and

(iv) the cash in the trust account may not be used to cover shortfalls in any accounts of the principal distributor or participating dealer;

(b) ensure that the trust account bears interest at rates equivalent to comparable accounts of the financial institution; and

(c) ensure that any charges against the trust account are not paid or reimbursed out of the trust account.

11.4 Exemption

(1) Sections 11.1 and 11.2 do not apply to members of The Investment Dealers Association of Canada, The Alberta Stock Exchange, The Montreal Exchange, The Toronto Stock Exchange or the Vancouver Stock Exchange.

(2) A participating dealer that is a member of an SRO referred to in subsection (1) shall permit the mutual fund and the principal distributor, through their respective auditors or other designated representatives, to examine the books and records of the participating dealer to verify the participating dealer's compliance with the requirements of its association or exchange that relate to the commingling of cash.

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

PART 12 COMPLIANCE REPORTS

12.1 Compliance Reports

(1) A mutual fund that does not have a principal distributor shall complete and file, within 140 days after the financial year end of the mutual fund

(a) a report in the form contained in Appendix B-1 describing compliance by the mutual fund during that financial year with the applicable requirements of Parts 9, 10 and 11; and

(b) a report by the auditor of the mutual fund, in the form contained in Appendix B-1, concerning the report referred to in paragraph (a).

(2) The principal distributor of a mutual fund shall complete and file, within 90 days after the financial year end of the principal distributor

(a) a report in the form contained in Appendix B-2 describing compliance by the principal distributor during that financial year with the applicable requirements of Parts 9, 10 and 11; and

(b) a report by the auditor of the principal distributor or by the auditor of the mutual fund, in the form contained in Appendix B-2, concerning the report referred to in paragraph (a).

(3) Each participating dealer that distributes securities of a mutual fund in a financial year of the participating dealer shall complete and file, within 90 days after the end of that financial year

(a) a report in the form contained in Appendix B-3 describing compliance by the participating dealer during that financial year with the applicable requirements of Parts 9, 10 and 11 in connection with its distribution of securities of all mutual funds in that financial year; and

(b) a report by the auditor of the participating dealer, in the form contained in Appendix B-3, concerning the report referred to in paragraph (a).

(4) Subsection (3) does not apply to members of The Investment Dealers Association of Canada, The Alberta Stock Exchange, The Montreal Exchange, The Toronto Stock Exchange or the Vancouver Stock Exchange.

PART 13 CALCULATION OF NET ASSET VALUE PER SECURITY

13.1 Frequency and Currency of Calculation of Net Asset Value per Security

(1) The net asset value per security of a mutual fund shall be calculated

(a) if the mutual fund does not use specified derivatives, at least once in each week; or

(b) if the mutual fund uses specified derivatives, at least once every business day.

(2) Despite subsection (1)(a), a mutual fund that, at the date that this Instrument comes into force, calculates net asset value per security no less frequently than once a month may continue to calculate net asset value per security at least as frequently as it does at that date.

(3) The net asset value per security of a mutual fund shall be calculated in the currency of Canada or in the currency of the United States of America or both.

(4) A mutual fund that arranges for the publication of its net asset value per security in the financial press shall ensure that its current net asset value per security is provided on a timely basis to the financial press.

13.2 Portfolio Transactions - Each transaction of purchase or sale of a portfolio asset effected by a mutual fund shall be reflected in a calculation of net asset value per security of the mutual fund made not later than the first calculation of net asset value per security made after the date on which the transaction becomes binding.

13.3 Capital Transactions - The issue or redemption of a security of a mutual fund shall be reflected in the first calculation of net asset value per security of the mutual fund made after the calculation of net asset value per security used to establish the issue or redemption price.

13.4 Valuation of Restricted Securities - A mutual fund shall value a restricted security at the lesser of

(a) the value based on reported quotations of that restricted security in common use; and

(b) that percentage of the market value of the securities of the class or series of a class of which the restricted security forms part that are not restricted securities, equal to the percentage that the mutual fund's acquisition cost was of the market value of the securities at the time of acquisition, but taking into account, if appropriate, the amount of time

remaining until the restricted securities will cease to be restricted securities.

13.5 Valuation of Specified Derivatives - A mutual fund shall value specified derivatives transactions and positions in accordance with the following principles:

1. A long position in an option or a debt-like security shall be valued at the current market value of the position.

2. For options written by a mutual fund

   (a) the premium received by the mutual fund for those options shall be reflected as a deferred credit that shall be valued at an amount equal to the current market value of the option that would have the effect of closing the position;

   (b) any difference resulting from revaluation shall be treated as an unrealized gain or loss on investment;

   (c) the deferred credit shall be deducted in calculating the net asset value per security of the mutual fund; and

   (d) any securities that are the subject of a written option shall be valued at their current market value.

3. The value of a forward contract or swap shall be the gain or loss on the contract that would be realized if, on the date that valuation is made, the position in the forward contract or swap were to be closed out.

4. The value of a standardized future shall be

   (a) if daily limits imposed by the futures exchange through which the standardized future was issued are not in effect, the gain or loss on the standardized future that would be realized if, on the date that valuation is made, the position in the standardized future were to be closed out; or

   (b) if daily limits imposed by the futures exchange through which the standardized future was issued are in effect, based on the current market value of the underlying interest of the standardized future.

5. Margin paid or deposited on standardized futures or forward contracts

   (a) shall be reflected as an account receivable; and

   (b) if not in the form of cash, shall be noted as held for margin.

PART 14 RECORD DATE

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

(a) the day on which the net asset value per security is determined for the purpose of calculating the amount of the payment of the dividend or distribution;

(b) the last day on which the net asset value per security of the mutual fund was calculated before the day referred to in paragraph (a); or

(c) if the day referred to in paragraph (b) is not a business day, the last day on which the net asset value per security of the mutual fund was calculated before the day referred to in paragraph (b).

PART 15 SALES COMMUNICATIONS AND PROHIBITED REPRESENTATIONS

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

15.2 Sales Communications - General Requirements

(1) Despite any other provision of this Part, no sales communication shall

   (a) be untrue or misleading; or

   (b) include a statement that conflicts with information that is contained in the preliminary simplified prospectus, the preliminary annual information form, the simplified prospectus or annual information form

      (i) of a mutual fund, or

      (ii) in which an asset allocation service is described.

(2) All performance data or disclosure specifically required by this Instrument and contained in a written sales communication shall be at least as large as 10-point type.

15.3 Prohibited Disclosure in Sales Communications

(1) A sales communication shall not compare the performance of a mutual fund or asset allocation service with the performance or change of any benchmark or investment unless

   (a) it includes all facts that, if disclosed, would be likely to alter materially the

conclusions reasonably drawn or implied by the comparison;

(b) it presents data for each subject of the comparison for the same period or periods;

(c) it explains clearly any factors necessary to make the comparison fair and not misleading; and

(d) in the case of a comparison with a benchmark

(i) the benchmark existed and was widely recognized and available during the period for which the comparison is made, or

(ii) the benchmark did not exist for all or part of the period, but a reconstruction or calculation of what the benchmark would have been during that period, calculated on a basis consistent with its current basis of calculation, is widely recognized and available.

(2) A sales communication for a mutual fund or asset allocation service that is prohibited by paragraph 15.6(a) from disclosing performance data shall not provide performance data for any benchmark or investment other than a mutual fund or asset allocation service under common management with the mutual fund or asset allocation service to which the sales communication pertains.

(3) Despite subsection (2), a sales communication for an index mutual fund may provide performance data for the index on which the investments of the mutual fund are based if the index complies with the requirements for benchmarks contained in paragraph (1)(d).

(4) A sales communication shall not refer to a performance rating or ranking of a mutual fund or asset allocation service unless

(a) the rating or ranking is prepared by an organization that is not a member of the organization of the mutual fund;

(b) standard performance data is provided for any mutual fund or asset allocation service for which a performance rating or ranking is given; and

(c) the rating or ranking is provided for each period for which standard performance data is required to be given.

(5) A sales communication shall not refer to a credit rating of securities of a mutual fund unless

(a) the rating is current and was prepared by an approved credit rating organization;

(b) there has been no announcement by the approved credit rating organization of which the mutual fund or its manager is or ought to be aware that the credit rating of the securities may be down-graded; and

(c) no approved credit rating organization is currently rating the securities at a lower level.

(6) A sales communication shall not refer to a mutual fund as, or imply that it is, a money fund, cash fund or money market fund unless, at the time the sales communication is used and for each period for which money market fund standard performance data is provided, the mutual fund is and was a money market fund, either under National Policy Statement No. 39 or under this Instrument.

(7) A sales communication shall not state or imply that a registered retirement savings plan, registered retirement income fund or registered education savings plan in itself, rather than the mutual fund to which the sales communication relates, is an investment.

15.4 Required Disclosure and Warnings in Sales Communications

(1) A written sales communication shall

(a) bear the name of the principal distributor or participating dealer that distributed the sales communication; and

(b) if the sales communication is not an advertisement, contain the date of first publication of the sales communication.

(2) A sales communication that includes a rate of return or a mathematical table illustrating the potential effect of a compound rate of return shall contain a statement in substantially the following words:

"[The rate of return or mathematical table shown] is used only to illustrate the effects of the compound growth rate and is not intended to reflect future values of [the mutual fund or asset allocation service] or returns on investment [in the mutual fund or from the use of the asset allocation service].".

(3) A sales communication, other than a report to securityholders, of a mutual fund that is not a money market fund and that does not contain performance data shall contain a warning in substantially the following words:

> "Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments. Please read the prospectus before investing. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated.".

(4) A sales communication, other than a report to securityholders, of a money market fund that does not contain performance data shall contain a warning in substantially the following words:

> "Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments. Please read the prospectus before investing. Mutual fund securities are not covered by the Canada Deposit Insurance Corporation or by any other government deposit insurer. There can be no assurances that the fund will be able to maintain its net asset value per security at a constant amount or that the full amount of your investment in the fund will be returned to you. Past performance may not be repeated.".

(5) A sales communication for an asset allocation service that does not contain performance data shall contain a warning in substantially the following words:

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

(6) A sales communication, other than a report to securityholders, of a mutual fund that is not a money market fund and that contains performance data shall contain a warning in substantially the following words:

> "Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments. Please read the prospectus before investing. The indicated rate[s] of return is [are] the historical annual compounded total return[s] including changes in [share or unit] value and reinvestment of all [dividends or distributions] and does [do] not take into account sales, redemption, distribution or optional charges or income taxes payable by any securityholder that would have reduced returns. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated.".

(7) A sales communication, other than a report to securityholders, of a money market fund that contains performance data shall contain

(a) a warning in substantially the following words:

> "Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments. Please read the prospectus before investing. The performance data provided assumes reinvestment of distributions only and does not take into account sales, redemption, distribution or optional charges or income taxes payable by any securityholder that would have reduced returns. Mutual fund securities are not covered by the Canada Deposit Insurance Corporation or by any other government deposit insurer. There can be no assurances that the fund will be able to maintain its net asset value per security at a constant amount or that the full amount of your investment in the fund will be returned to you. Past performance may not be repeated."; and

(b) a statement in substantially the following words, immediately following the performance data:

> "This is an annualized historical yield based on the seven day period ended on [date] [annualized in the case of effective yield by compounding the seven day return] and does not represent an actual one year return.".

(8) A sales communication for an asset allocation service that contains performance data shall contain a warning in substantially the following words:

> "Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments and the use of an asset

allocation service. Please read the prospectus of the mutual funds in which investment may be made under the asset allocation service before investing. The indicated rate[s] of return is [are] the historical annual compounded total return[s] assuming the investment strategy recommended by the asset allocation service is used and after deduction of the fees and charges in respect of the service. The return[s] is [are] based on the historical annual compounded total returns of the participating funds including changes in [share] [unit] value and reinvestment of all [dividends or distributions] and does [do] not take into account sales, redemption, distribution or optional charges or income taxes payable by any securityholder in respect of a participating fund that would have reduced returns. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated.".

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

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

(10) A sales communication for a mutual fund or asset allocation service that purports to arrange a guarantee or insurance in order to protect all or some of the principal amount of an investment in the mutual fund or asset allocation service shall

(a) identify the person or company providing the guarantee or insurance;

(b) provide the material terms of the guarantee or insurance, including the maturity date of the guarantee or insurance;

(c) if applicable, state that the guarantee or insurance does not apply to the amount of any redemptions before the maturity date of the guarantee or before the death of the securityholder and that redemptions before that date would be based on the net asset value per security of the mutual fund at the time; and

(d) modify any other disclosure required by this section appropriately.

(11) The warnings referred to in this section shall be communicated in a manner that a reasonable person would consider clear and easily understood at the same time as, and through the medium by which, the related sales communication is communicated.

(12) A mutual fund that files a prospectus rather than a simplified prospectus shall amend the warnings required by this section to refer to a prospectus, as applicable.

15.5 Disclosure Regarding Distribution Fees

(1) No person or company shall describe a mutual fund in a sales communication as a "no-load fund" or use words of like effect if on a purchase or redemption of securities of the mutual fund investor fees are payable by an investor or if any fees, charges or expenses are payable by an investor to a participating dealer of the mutual fund named in the sales communication, other than

(a) fees and charges related to specific optional services;

(b) for a mutual fund that is not a money market fund, redemption fees on the redemption of securities of the mutual fund that are redeemed within 90 days after the purchase of the securities, if the existence of the fees is disclosed in the sales communication, or in the simplified prospectus of the mutual fund; or

(c) costs that are payable only on the set-up or closing of a securityholder's account and that reflect the administrative costs of establishing or closing the account, if the existence of the costs is disclosed in the sales communication, or in the simplified prospectus of the mutual fund.

(2) If a sales communication describes a mutual fund as "no-load" or uses words to like effect, the sales communication shall

(a) indicate the principal distributor or a participating dealer through which an investor may purchase the mutual fund on a no-load basis;

(b) disclose that management fees and operating expenses are paid by the mutual fund; and

(c) disclose the existence of any trailing commissions paid by a member of the organization of the mutual fund.

(3) A sales communication containing a reference to the existence or absence of fees or charges, other than the disclosure required by section 15.4 or a reference to the term "no-load", shall disclose the types of fees and charges that exist.

(4) The rate of sales charges or commissions for the sale of securities of a mutual fund or the use of an asset allocation service shall be expressed in a sales communication as a percentage of the amount paid by the purchaser and as a percentage of the net amount invested if a reference is made to sales charges or commissions.

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

(a) either

(i) the mutual fund has offered securities under a simplified prospectus in a jurisdiction for at least one completed financial year, or the asset allocation service has been operated for at least 12 months and has invested only in participating mutual funds each of which has offered securities under a simplified prospectus in a jurisdiction for at least one completed financial year, or

(ii) if the sales communication pertains to a mutual fund or asset allocation service that does not satisfy the requirements of subparagraph (i), the sales communication is sent only to

(A) securityholders of the mutual fund or participants in the asset allocation service, or

(B) securityholders of a mutual fund or participants in an asset allocation service under common management with the mutual fund or asset allocation service;

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

(c) the performance data reflects or includes references to all elements of return; and

(d) except as permitted by subsection 15.3(3), the sales communication does not contain performance data for a period that is before the time when the mutual fund offered its securities under a simplified prospectus or before the asset allocation service commenced operation.

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

(a) one or more mutual funds or asset allocation services that are under common management or administration with the mutual fund or asset allocation service to which the advertisement pertains;

(b) one or more mutual funds or asset allocation services that have fundamental investment objectives that a reasonable person would consider similar to the mutual fund or asset allocation service to which the advertisement pertains; or

(c) an index.

15.8 Performance Measurement Periods Covered by Performance Data

(1) A sales communication, other than a report to securityholders, that relates to a money market fund may provide standard performance data only if

(a) the standard performance data has been calculated for the most recent seven day period for which it is practicable to calculate, taking into account publication deadlines; and

(b) the seven day period does not start more than 45 days before the date of the appearance, use or publication of the sales communication.

(2) A sales communication, other than a report to securityholders, that relates to an asset allocation service or to a mutual fund other than a money market fund may provide standard performance data only if

(a) the standard performance data has been calculated for the 10, five, three and one year periods and the period since the inception of the mutual fund if the mutual fund has been offering securities by way of simplified prospectus for more than one and less than 10 years, and

(b) the periods referred to in paragraph (a) end on the same calendar month end that is

(i) not more than 45 days before the date of the appearance or use of the advertisement in which it is included, and

(ii) not more than three months before the date of first publication of any other sales communication in which it is included.

(3) A report to securityholders may contain standard performance data only if

(a) the standard performance data has been calculated for the 10, five, three and one year periods and the period since the inception of the mutual fund if the mutual fund has been offering securities by way of simplified prospectus for more than one and less than 10 years; and

(b) the periods referred to in paragraph (a) end on the day as of which the balance sheet of the financial statements contained in the report to securityholders was prepared.

(4) A sales communication shall clearly identify the periods for which performance data is calculated.

15.9 Changes affecting Performance Data

(1) If, during or after a performance measurement period of performance data contained in a sales communication, there have been changes in the business, operations or affairs of the mutual fund or asset allocation service to which the sales communication pertains that could have materially affected the performance of the mutual fund or asset allocation service, the sales communication shall contain

(a) summary disclosure of the changes, and of how those changes could have affected the performance had those changes been in effect throughout the performance measurement period; and

(b) for a money market fund that during the performance measurement period did not pay or accrue the full amount of any fees and charges of the type described under paragraph 15.11(1)1, disclosure of the difference between the full amounts and the amounts actually charged, expressed as an annualized percentage on a basis comparable to current yield.

(2) If a mutual fund has, in the last 10 years, undertaken a reorganization with, or acquired assets from, another mutual fund in a transaction that was a significant change for the mutual fund or would have been a significant change for the mutual fund had this Instrument been in force at the time of the transaction, then, in any sales communication of the mutual fund,

(a) the mutual fund shall provide summary disclosure of the transaction;

(b) the mutual fund may include its performance data covering any part of a period before the transaction only if it also includes the performance data for the other fund for the same periods;

(c) the mutual fund shall not include its performance data for any part of a period after the transaction unless

(i) 12 months have passed since the transaction, or

(ii) the mutual fund includes in the sales communication the performance data for itself and the other mutual fund referred to in paragraph (b); and

(d) the mutual fund shall not include any performance data for any period that is composed of both time before and after the transaction.

15.10 Formula for Calculating Standard Performance Data

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

(2) In this Part

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

current yield = [seven day return x 365/7] x 100;

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

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

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

(a) determining the net change, exclusive of new subscriptions other than from the reinvestment of distributions or proceeds of redemption of securities of the money market fund, in the value of the account,

(b) subtracting all fees and charges of the type referred to in paragraph 15.11(1)3 for the seven day period, and

(c) dividing the result by the value of the account at the beginning of the seven day period;

"standard performance data" means

(a) for a money market fund

(i) the current yield, or

(ii) the current yield and effective yield, if the effective yield is reported in a type size that is at least equal to that of the current yield, and

(b) for any mutual fund other than a money market fund, the total return

calculated in each case in accordance with this section; and

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

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

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

(3) If there are fees and charges of the type described in paragraph 15.11(1)1 relevant to the calculation of redeemable value and initial value of the securities of a mutual fund, the redeemable value and initial value of securities of a mutual fund shall be the net asset value of one unit or share of the mutual fund at the beginning or at the end of the performance measurement period, minus the amount of those fees and charges calculated by applying the assumptions referred to in that paragraph to a hypothetical securityholder account.

(4) If there are no fees and charges of the type described in paragraph 15.11(1)1 relevant to a calculation of total return, the calculation of total return for a mutual fund may assume a hypothetical investment of one security of the mutual fund and be calculated as follows:

(a) "initial value" means the net asset value of one unit or share of a mutual fund at the beginning of the performance measurement period; and

(b) "redeemable value" =

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

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

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

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

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

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

(6) Performance data

(a) for a mutual fund other than a money market fund shall be calculated to the

nearest one-tenth of one percent; and

(b) for a money market fund shall be calculated to the nearest one-hundredth of one percent.

15.11 Assumptions for Calculating Standard Performance Data

(1) The following assumptions shall be made in the calculation of standard performance data of a mutual fund:

1. Recurring fees and charges that are payable by all securityholders

(a) are accrued or paid in proportion to the length of the performance measurement period;

(b) if structured in a manner that would result in the performance information being dependent on the size of an investment, are calculated on the basis of an investment equal to the greater of $10,000 or the minimum amount that may be invested; and

(c) if fully negotiable, are calculated on the basis of the average fees paid by accounts of the size referred to in paragraph (b).

2. There are no fees and charges related to specific optional services.

3. All fees and charges payable by the mutual fund are accrued or paid.

4. Dividends or distributions by the mutual fund are reinvested in the mutual fund at the net asset value per security of the mutual fund on the reinvestment dates during the performance measurement period.

5. There are no non-recurring fees and charges that are payable by some or all securityholders and no recurring fees and charges that are payable by some but not all securityholders.

6. A complete redemption occurs at the end of the performance measurement period so that the ending redeemable value includes elements of return that have been accrued but not yet paid to securityholders.

(2) The following assumptions shall be made in the calculation of standard performance data of an asset allocation service:

1. Fees and charges that are payable by participants in the asset allocation service

(a) are accrued or paid in proportion to the length of the performance measurement period;

(b) if structured in a manner that would result in the performance information being dependent on the size of an investment, are calculated on the basis of an investment equal to the greater of $10,000 or the minimum amount that may be invested; and

(c) if fully negotiable, are calculated on the basis of the average fees paid by accounts of the size referred to in paragraph (b).

2. There are no fees and charges related to specific optional services.

3. The investment strategy recommended by the asset allocation service is utilized for the performance measurement period.

4. Transfer fees are

(a) accrued or paid;

(b) if structured in a manner that would result in the performance information being dependent on the size of an investment, calculated on the basis of an account equal to the greater of $10,000 or the minimum amount that may be invested; and

(c) if the fees and charges are fully negotiable, calculated on the basis of the average fees paid by an account of the size referred to in paragraph (b).

5. A complete redemption occurs at the end of the performance measurement period so that the ending redeemable value includes elements of return that have been accrued but not yet paid to securityholders.

(3) The calculation of standard performance data shall be based on actual historical performance and the fees and charges

payable by the mutual fund and securityholders, or the asset allocation service and participants, in effect during the performance measurement period.

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

(a) whether the security represents a share in a corporation or an interest in a non-corporate entity;

(b) the name of the mutual fund and its manager;

(c) the fundamental investment objectives of the mutual fund;

(d) without giving details, whether the security is or will be a qualified investment for a registered retirement savings plan, registered retirement income fund or registered education savings plan or qualifies or will qualify the holder for special tax treatment; and

(e) any additional information permitted by securities legislation.

15.13 Prohibited Representations

(1) Securities issued by an unincorporated mutual fund shall be described by a term that is not and does not include the word "shares".

(2) No communication by a mutual fund or asset allocation service, its promoter, manager, portfolio adviser, principal distributor, participating dealer or a person providing services to the mutual fund or asset allocation service shall describe a mutual fund as a commodity pool or as a vehicle for investors to participate in the speculative trading of, or leveraged investment in, derivatives, unless the mutual fund is a commodity pool as defined in National Instrument 81-101 Mutual Fund Prospectus Disclosure.

PART 16 CALCULATION OF MANAGEMENT EXPENSE RATIO

16.1 Calculation of Management Expense Ratio

(1) A mutual fund may disclose its management expense ratio only if the management expense ratio is calculated for a financial year of the mutual fund and if it is calculated by

(a) dividing

(i) the total expenses of the mutual fund for the financial year as shown on its income statement,

by

(ii) the average net asset value of the mutual fund for the financial year, obtained by

(A) adding together the net asset values of the mutual fund as at the close of business of the mutual fund on each day during the financial year on which the net asset value of the mutual fund has been calculated, and

(B) dividing the amount obtained under clause (A) by the number of days during the financial year on which the net asset value of the mutual fund has been calculated; and

(b) multiplying the result obtained under paragraph (a) by 100.

(2) If any fees and expenses otherwise payable by a mutual fund in a financial year were waived or otherwise absorbed by a member of the organization of the mutual fund, the mutual fund shall disclose in a note to the disclosure of its management expense ratio, details of

(a) what the management expense ratio would have been without any waivers or absorptions;

(b) the length of time that the waiver or absorption is expected to continue;

(c) whether the waiver or absorption can be terminated at any time by the member of the organization of the mutual fund; and

(d) any other arrangements concerning the waiver or absorption.

(3) All non-optional fees, charges and expenses paid directly by investors of a mutual fund in connection with the holding of securities of the mutual fund during the period to which the disclosed management expense ratio relates shall be included by the mutual fund in its calculation of the management expense ratio with an appropriate explanation in a note to the disclosure.

(4) If the aggregate amount of a non-optional fee, charge and expense payable directly by investors of a mutual fund in connection with the holding of securities of the mutual fund during the period to which the disclosed management expense ratio relates is not ascertainable, the mutual fund shall include

the maximum amount of the non-optional investor fee that could have been paid by those investors in its calculation of the management expense ratio.

(5) Mutual fund expenses rebated by a manager or a mutual fund to a securityholder shall not be deducted from total expenses of the mutual fund in determining the management expense ratio of the mutual fund.

(6) A mutual fund that has separate classes or series of securities shall calculate a management expense ratio for each class or series, in the manner required by this section, modified as appropriate.

(7) In this section, the phrase "financial year" includes, for an issuer, a period other than the 12 months for which the issuer is required by securities legislation to prepare audited financial statements.

(8) The management expense ratio of a mutual fund for a financial year of less than 12 months shall be annualized.

16.2 Fund of Funds Calculation - For the purposes of subparagraph 16.1(1)(a)(i), the total expenses of a mutual fund for a financial year that invests in securities of one or more other mutual funds is equal to the sum of

(a) the total expenses incurred by the mutual fund attributable to its investment in each underlying mutual fund, as calculated by

(i) multiplying the total expenses of each underlying mutual fund for the financial year as shown on the income statement of each underlying mutual fund,

by

(ii) the average proportion of securities of the underlying mutual fund held by the mutual fund during the financial year, calculated by

(A) adding together the proportion of securities of the underlying mutual fund held by the mutual fund on each day in the financial year, and

(B) dividing the amount obtained under clause (A) by the number of days in the financial year; and

(b) the total expenses of the mutual fund for the financial year as shown on its income statement.

PART 17 FINANCIAL STATEMENT REQUIREMENTS

17.1 Information About Specified Derivatives

(1) A mutual fund shall, in the statement of investment portfolio included in the annual and interim financial statements of the mutual fund, or in the notes to that statement, disclose

(a) for long positions in clearing corporation options, the number of options, the underlying interest, the strike price, the expiration month and year, the cost and the market value;

(b) for long positions in options on futures, the number of options on futures, the futures contracts that form the underlying interest, the strike price, the expiration month and year of the option on futures, the delivery month and year of the futures contract that forms the underlying interest of the option on futures, the cost and the market value;

(c) for clearing corporation options written by the mutual fund, the particulars of the deferred credit account, indicating the number of options, the underlying interest, the strike price, the expiration month and year, the premium received and the value as determined under section 13.5;

(d) for options purchased by the mutual fund that are not clearing corporation options, the number of options, the credit rating of the issuer of the options, whether the rating has fallen below the approved credit rating, the underlying interest, the principal amount or quantity of the underlying interest, the strike price, the expiration date, the cost and the market value;

(e) for options written by the mutual fund that are not clearing corporation options, the particulars of the deferred credit account, indicating the number of options, the underlying interest, the principal amount or quantity of the underlying interest, the exercise price, the expiration date, the premium received and the value as determined under section 13.5;

(f) for positions in standardized futures, the number of standardized futures, the underlying interest, the price at which the contract was entered into, the delivery month and year and the value as determined under section 13.5;

(g) for positions in forward contracts, the number of forward contracts, the credit rating of the counterparty, whether the rating has fallen below the approved credit rating level, the underlying interest, the quantity of the underlying interest, the price at which the contract was entered into, the settlement date and the value as determined under section 13.5; and

(h) for debt-like securities, the principal amount of the debt, the interest rate, the payment dates, the underlying interest, the principal amount or quantity of the underlying interest, a description of whether the derivative component is an option or a forward contract with respect to the underlying interest, the strike price in the case of an options component and the set price in the case of a forward component, and the value as determined under section 13.5.

(2) If applicable, the statement of investment portfolio included in the annual and interim financial statements of the mutual fund, or the notes to that statement, shall identify by an asterisk or other notation the underlying interest that is being hedged by each position taken by the mutual fund in a specified derivative.

17.2 Additional Disclosure Requirements

(1) The annual financial statements of a mutual fund shall

(a) set out in appropriate detail the amounts of all fees, charges and expenses, if any, that have been charged to the mutual fund during each financial year reported upon in the financial statements; and

(b) set out the net asset value per security of the mutual fund as at the end of the last completed financial year and as at the end of each of the four preceding completed financial years, or such fewer number of financial years as the mutual fund has been in existence.

(2) The annual and interim financial statements of a mutual fund shall disclose

(a) the management expense ratio of each class or series of a class of securities of the mutual fund for each of the last five completed financial years of the mutual fund or such fewer number of financial years as the mutual fund has been in existence, and shown for periods of less than 12 months on an annualized basis with reference to the period covered and the fact that the management expense ratio shown is annualized; and

(b) a brief description of the method of calculating the management expense ratio.

17.3 Approval of Financial Statements

(1) The board of directors of a mutual fund that is a corporation shall

(a) approve the annual financial statements of the mutual fund that are to be delivered on request to purchasers of its securities; and

(b) authorize two directors of the mutual fund to sign those financial statements to evidence that approval.

(2) The manager or the trustee or trustees of a mutual fund that is a trust, or another person or company authorized to do so by the constating documents of the mutual fund, shall

(a) approve the annual financial statements of the mutual fund that, on and after the date the simplified prospectus of the mutual fund is filed, are to be delivered to purchasers of its securities with the prospectus or the simplified prospectus or are incorporated by reference into the simplified prospectus; and

(b) authorize two appropriate persons to sign those financial statements to evidence that approval.

PART 18 SECURITYHOLDER RECORDS

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

(a) the names and latest known addresses of each securityholder of the mutual fund;

(b) the number and class or series of a class of securities held by each securityholder of the mutual fund; and

(c) the date and details of each issue and redemption of securities, and each distribution, of the mutual fund.

18.2 Availability of Records

(1) A mutual fund that is not a corporation shall make, or cause to be made, the records referred to in section 18.1 available for inspection, free of charge, during normal business hours at its principal or head office by a securityholder or a representative of a securityholder, if the securityholder has agreed in writing that the information contained in the register will not be used by the securityholder for any purpose other than attempting to influence the voting of securityholders of the mutual fund or a matter relating to the relationships among the mutual fund, the members of the organization of the mutual fund, and the securityholders, partners, directors and officers of those entities.

(2) A mutual fund shall, upon written request by a securityholder of the mutual fund, provide, or cause to be provided, to the securityholder a copy of the records referred to in paragraphs 18.1(a) and (b) if the securityholder

(a) has agreed in writing that the information contained in the register will not be used by the securityholder for any purpose other than attempting to influence the voting of securityholders of the mutual fund or a matter relating to the administration of the mutual fund; and

(b) has paid a reasonable fee to the mutual fund that does not exceed the reasonable costs to the mutual fund of providing the copy of the register.

PART 19 EXEMPTIONS AND APPROVALS

19.1 Exemption

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

(2) Despite subsection (1), in Ontario only the regulator may grant such an exemption.

19.2 Exemption or Approval under Prior Policy

(1) A mutual fund that has obtained, from the regulator or securities regulatory authority, an exemption or waiver from, or approval under, a provision of National Policy Statement No. 39 before this Instrument came into force is exempt from any substantially similar provision of this Instrument, if any, on the same conditions, if any, as are contained in the earlier exemption or approval, unless the regulator or securities regulatory authority has revoked that exemption or waiver under authority provided to it in securities legislation.

(2) Despite Part 7, a mutual fund that has obtained, from the regulator or securities regulatory authority, approval under National Policy Statement No. 39 to pay incentive fees may continue to pay incentive fees on the terms of that approval if disclosure of the method of calculation of the fees and details of the composition of the benchmark or index used in calculating the fees are described in the simplified prospectus of the mutual fund.

(3) A mutual fund that intends to rely upon subsection (1) shall, at the time of the first filing of its *pro forma* simplified prospectus after this Instrument comes into force, send to the regulator a letter or memorandum containing

(a) a brief description of the nature of the exemption from, or approval under, National Policy Statement No. 39 previously obtained; and

(b) the provision in the Instrument that is substantially similar to the provision in National Policy Statement No. 39 from or under which the exemption or approval was previously obtained.

PART 20 TRANSITIONAL

20.1 Effective Date - This Instrument comes into force on February 1, 2000.

20.2 Sales Communications - Sales communications, other than advertisements, that were printed before December 31, 1999 may be used until August 1, 2000, despite any requirements in this Instrument.

20.3 Reports to Securityholders - This Instrument does not apply to reports to securityholders printed before this Instrument came into force.

20.4 Mortgage Funds - Paragraphs 2.3(b) and (c) do not apply to a mutual fund that has adopted fundamental investment objectives to permit it to invest in mortgages in accordance with National Policy Statement No. 29 if

(a) a National Instrument replacing National Policy Statement No. 29 has not come into force;

(b) the mutual fund was established, and has a prospectus or simplified prospectus for which a receipt was issued, before the date that this Instrument came into force; and

(c) the mutual fund complies with National Policy Statement No. 29.

20.5 Delayed Coming into Force

(1) Despite section 20.1, subsection 4.4(1) does not come into force until August 1, 2000.

(2) Despite section 20.1, the following provisions of this Instrument do not come into force until February 1, 2001:

1. Subsection 2.4(2).

2. Subsection 2.7(4).

3. Subsection 6.4(1).

4. Subsection 6.8(4).

NATIONAL INSTRUMENT 81-102

APPENDIX A

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

Futures Exchanges

Australia

Sydney Futures Exchange
Australian Financial Futures Market

Austria

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

Belgium

Belfox CV (Belgium Futures and Options Exchange)

Brazil

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

Canada

The Winnipeg Commodity Exchange
The Toronto Futures Exchange
The Montreal Exchange

Denmark

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

Finland

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

France

Marché à terme international de France S.A. (MATIF S.A.)
Marché des option négociables à Paris (MUNCP)

Germany

DTB Deutsche Terminbörse GmbH
EUREX

Hong Kong

Hong Kong Futures Exchange Limited

Ireland

Irish Futures and Options Exchange

Italy

Milan Italiano Futures Exchange

Japan

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

Netherlands

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

New Zealand

New Zealand Futures and Options Exchange

Norway

Oslo Stock Exchange

Philippines

Manila International Futures Exchange

Portugal

Bosa de Derivatives de Porto

Singapore

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

Spain

Meff Renta Fija
Meff Renta Variable

Sweden

OM Stockholm Fondkommission AB

Switzerland

EUREX

United Kingdom

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

United States

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

NATIONAL INSTRUMENT 81-102

APPENDIX B-1

Compliance Report

TO: [The appropriate securities regulatory authorities]

FROM: [Name of mutual fund]

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

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

[NAME of mutual fund]

Signature

Name and office of the person executing this report

Date

NATIONAL INSTRUMENT 81-102

APPENDIX B-1

Audit Report

TO: [The appropriate securities regulatory authorities]

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

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

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

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

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

City
Date

Chartered Accountants

NATIONAL INSTRUMENT 81-102

APPENDIX B-2

Compliance Report

TO: [The appropriate securities regulatory authorities]

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

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

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

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

[NAME of the Distributor]

Signature

Name and office of the person executing this report

Date

NATIONAL INSTRUMENT 81-102

APPENDIX B-2

Audit Report

TO: [The appropriate securities regulatory authorities]

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

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

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

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

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

City
Date Chartered Accountants

NATIONAL INSTRUMENT 81-102

APPENDIX B-3

Compliance Report

TO: [The appropriate securities regulatory authorities]

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

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

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

[NAME of the Distributor]

Signature

Name and office of the person executing this report

Date

NATIONAL INSTRUMENT 81-102

APPENDIX B-3

Audit Report

TO: [The appropriate securities regulatory authorities]

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

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

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

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

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

City
Date

Chartered Accountants

COMPANION POLICY 81-102CP TO NATIONAL INSTRUMENT 81-102 MUTUAL FUNDS

TABLE OF CONTENTS

COMPANION POLICY 81-102CP TO NATIONAL INSTRUMENT 81-102 MUTUAL FUNDS

PART 1 PURPOSE

1.1 **Purpose** - The purpose of this Policy is to state the views of the Canadian securities regulatory authorities on various matters relating to National Instrument 81-102 Mutual Funds (the "Instrument"), including

(a) the interpretation of various terms used in the Instrument;

(b) recommendations concerning the operating procedures that the Canadian securities regulatory authorities suggest that mutual funds, or persons performing services for mutual funds, adopt to ensure compliance with the Instrument;

(c) discussions of circumstances in which the Canadian securities regulatory authorities have granted relief from particular requirements of National Policy Statement No. 39 ("NP39"), the predecessor to the Instrument, and the conditions that those authorities imposed in granting that relief; and

(d) recommendations concerning applications for approvals required under, or relief from, provisions of the Instrument.

PART 2 COMMENTS ON DEFINITIONS CONTAINED IN THE INSTRUMENT

2.1 **"asset allocation service"** - The definition of "asset allocation service" in the Instrument includes only specific administrative services in which an investment in mutual funds subject to the Instrument is an integral part. The Canadian securities regulatory authorities do not view this definition as including general investment services such as discretionary portfolio management that may, but are not required to, invest in mutual funds subject to this Instrument.

2.2 **"cash equivalent"** - The definition of "cash equivalent" in the Instrument includes certain evidences of indebtedness of Canadian financial institutions. This includes banker's acceptances.

2.3 **"clearing corporation"** - The definition of "clearing corporation" in the Instrument includes both incorporated and unincorporated organizations, which may, but need not, be part of an options or futures exchange.

2.4 **"debt-like security"** - Paragraph (b) of the definition of "debt-like security" in the Instrument provides that the value of the component of an instrument that is not linked to the underlying interest of the instrument must account for less than 80 percent of the aggregate value of the instrument in order that the instrument be considered a debt-like security. The Canadian securities regulatory authorities have structured this provision in this manner to emphasize what they consider the most appropriate manner to value these instruments. That is, one should first value the component of the instrument that is not linked to the underlying interest, as this is often much easier to value than the component that is linked to the underlying interest. The Canadian securities regulatory authorities recognize the valuation difficulties that can arise if one attempts to value, by itself, the component of an instrument that is linked to the underlying interest.

2.5 **"fundamental investment objectives"**

(1) The definition of "fundamental investment objectives" is relevant in connection with paragraph 5.1(c) of the Instrument, which requires that the approval of securityholders of a mutual fund be obtained before any change is made to the fundamental investment objectives of the mutual fund. The fundamental investment objectives of a mutual fund are required to be disclosed in a simplified prospectus under Part B of Form 81-101F1 Contents of Simplified Prospectus. The definition of "fundamental investment objectives" contained in the Instrument uses the language contained in the disclosure requirements of Part B of Form 81-101F1, and the definition should be read to include the matters that would have to be disclosed under the Item of Part B of the form concerning "Fundamental Investment Objectives". Accordingly, any change to the mutual fund requiring a change to that disclosure would trigger the requirement for securityholder approval under paragraph 5.1(c) of the Instrument.

(2) Part B of Form 81-101F1 sets out, among other things, the obligation that a mutual fund disclose in a simplified prospectus both its fundamental investment objectives and its investment strategies. The matters required to be disclosed under the Item of Part B of the form relating to "Investment Strategies" are not "fundamental investment objectives" under the Instrument.

(3) Generally speaking, the "fundamental investment objectives" of a mutual fund are those attributes that define its fundamental nature. For example, mutual funds that are guaranteed or insured, or that pursue a highly specific investment approach such as index funds or derivative funds, may be defined by those attributes. Often the manner in which a mutual fund is marketed will provide evidence as to its fundamental nature; a mutual fund

whose advertisements emphasize, for instance, that investments are guaranteed likely will have the existence of a guarantee as a "fundamental investment objective".

(4) The Canadian securities regulatory authorities are of the view that whether the securities of a mutual fund are foreign property under the ITA is linked to the mutual fund's fundamental investment objectives. Therefore, a change in the method by which the mutual fund is managed that results in its securities going from being foreign property to being non-foreign property, or vice versa, would be likely due to a change in the mutual fund's fundamental investment objectives.

(5) One component of the definition of "fundamental investment objectives" is that those objectives distinguish a mutual fund from other mutual funds. This component does not imply that the fundamental investment objectives for each mutual fund must be unique. Two or more mutual funds can have identical fundamental investment objectives.

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

2.7 **"hedging"**

(1) One component of the definition of "hedging" is the requirement that hedging transactions result in a "high degree of negative correlation between changes in the value of the investment or position, or group of investments or positions, being hedged and changes in the value of the instrument or instruments with which the investment or position is hedged". The Canadian securities regulatory authorities are of the view that there need not be complete congruence between the hedging instrument or instruments and the position or positions being hedged if it is reasonable to regard the one as a hedging instrument for the other, taking into account the closeness of the relationship between fluctuations in the price of the two and the availability and pricing of hedging instruments.

(2) The definition of "hedging" includes a reference to the "maintaining" of the position resulting from a hedging transaction or series of hedging transactions. The inclusion of this component in the definition requires a mutual fund to ensure that a transaction continues to offset specific risks of the mutual fund in order that the transaction be considered a "hedging" transaction under the Instrument; if the "hedging" position ceases to provide an offset to an existing risk of a mutual fund, then that position is no longer a hedging position under the Instrument, and can be held by the mutual fund only in compliance with the specified derivatives rules of the Instrument that apply to non-hedging positions. The component of the definition that requires the "maintaining" of a hedge position does not mean that a mutual fund is locked into a specified derivatives position; it simply means that the specified derivatives position must continue to satisfy the definition of "hedging" in order to receive hedging treatment under the Instrument.

(3) Paragraph (b) of the definition of "hedging" has been included to ensure that currency cross hedging continues to be permitted under the Instrument. Currency cross hedging is the substitution of currency risk associated with one currency for currency risk associated with another currency, if neither currency is a currency in which the mutual fund determines its net asset value per security and the aggregate amount of currency risk to which the mutual fund is exposed is not increased by the substitution. Currency cross hedging is to be distinguished from currency hedging, as that term is ordinarily used. Ordinary currency hedging, in the context of mutual funds, would involve replacing the mutual fund's exposure to a "non-net asset value" currency with exposure to a currency in which the mutual fund calculates its net asset value per security. That type of currency hedging is subject to paragraph (a) of the definition of "hedging".

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

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

2.10 **"option"** - The definition of "option" includes warrants, whether or not the warrants are listed on a

stock exchange or quoted on an over-the-counter market.

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

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

2.13 **"purchase"**

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

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

1. The mutual fund effects an ordinary purchase of the security, or, at its option, exercises, converts or exchanges a convertible security held by it.

2. The mutual fund receives the security as consideration for a security tendered by the mutual fund into a take-over bid.

3. The mutual fund receives the security as the result of a merger, amalgamation, plan of arrangement or other reorganization for which the mutual fund voted in favour.

4. The mutual fund receives the security as a result of the automatic exercise of an exchange or conversion right attached to another security held by the mutual fund in accordance with the terms of that other security or the exercise of that exchange or conversion right at the option of the mutual fund.

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

1. The mutual fund receives the security as a result of a compulsory acquisition by an issuer following completion of a successful take-over bid.

2. The mutual fund receives the security as a result of a merger, amalgamation, plan of arrangement or other reorganization that the mutual fund voted against.

3. The mutual fund receives the security as the result of the exercise of an exchange or conversion right attached to a security held by the mutual fund made at the discretion of the issuer of the security held by the mutual fund.

4. The mutual fund declines to tender into an issuer bid, even though its decision is likely to result in an increase in its percentage holdings of a security beyond what the mutual fund would be permitted under the Instrument to purchase.

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

2.15 **"sales communication"**

(1) The term "sales communication" refers to a communication to a securityholder of a mutual fund and to a person or company that is not a securityholder if the purpose of the communication is to induce the purchase of securities of the mutual fund. A sales communication therefore does not include a communication solely between a mutual fund or its promoter, manager, principal distributor or portfolio adviser and a participating dealer, or between the principal distributor or a participating dealer and its registered salespersons, that is indicated to be internal or confidential and that is not designed to be passed on by any principal distributor, participating dealer or registered salesperson to any securityholder of, or potential investor in, the mutual fund. In the view of the Canadian securities regulatory authorities, if a communication of that type were so passed on by the principal distributor, participating dealer or registered salesperson, the communication

would be a sales communication made by the party passing on the communication if the recipient of the communication were a securityholder of the mutual fund or if the intent of the principal distributor, participating dealer or registered salesperson in passing on the communication were to induce the purchase of securities of the mutual fund.

(2) The term "sales communication" is defined in the Instrument such that the communication need not be in writing and includes any oral communication. The Canadian securities regulatory authorities are of the view that the requirements in the Instrument pertaining to sales communications would apply to statements made at an investor conference to securityholders or to others to induce the purchase of securities of the mutual fund.

(3) The Canadian securities regulatory authorities are of the view that image advertisements that are intended to promote a corporate identity or the expertise of a mutual fund manager fall outside the definition of "sales communication". However, an advertisement or other communication that refers to a specific mutual fund or funds or promotes any particular investment portfolio or strategy would be a sales communication and therefore be required to include warnings of the type now described in section 15.4 of the Instrument.

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

2.16 "specified derivative"

(1) The term "specified derivative" is defined to mean an instrument, agreement or security, the market price, value or payment obligations of which are derived from, referenced to or based on an underlying interest. Certain instruments, agreements or securities that would otherwise be specified derivatives within the meaning of the definition are then excluded from the definition for purposes of the Instrument.

(2) Because of the broad ambit of the lead-in language to the definition, it is impossible to list every instrument, agreement or security that might be caught by that lead-in language but that is not considered to be a derivative in any normal commercial sense of that term. The Canadian securities regulatory authorities consider conventional floating rate debt instruments, securities of a mutual fund or commodity pool, non-redeemable securities of an investment fund, American depositary receipts and instalment receipts to be within this category and will not treat those instruments as a specified derivative in administering the Instrument.

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

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

PART 3 INVESTMENTS

3.1 Evidences of Indebtedness of Foreign Governments and Supranational Agencies

(1) Section 2.1 of the Instrument prohibits mutual funds from purchasing a security of an issuer, other than a government security or a security issued by a clearing corporation if, immediately after the purchase, more than 10 percent of the net assets of the mutual fund, taken at market value at the time of the purchase, would be invested in securities of that issuer. The term "government security" is defined in the Instrument as an evidence of indebtedness that is issued, or fully and unconditionally guaranteed as to principal and interest, by any of the government of Canada, the government of a jurisdiction or the government of the United States of America.

(2) Before the Instrument came into force, the Canadian securities regulatory authorities granted relief from the predecessor provision of NP39 to a number of international bond

funds in order to permit those mutual funds to pursue their fundamental investment objectives with greater flexibility.

(3) The Canadian securities regulatory authorities will continue to consider applications for relief from section 2.1 of the Instrument if the mutual fund making the application demonstrates that the relief will better enable the mutual fund to meet its fundamental investment objectives. This relief will ordinarily be restricted to international bond funds.

(4) The relief from paragraph 2.04(1)(a) of NP39, which is replaced by section 2.1 of the Instrument, that has been provided to a mutual fund has generally been limited to the following circumstances:

1. The mutual fund has been permitted to invest up to 20 percent of its net assets, taken at market value at the time of purchase, in evidences of indebtedness of any one issuer if those evidences of indebtedness are issued, or guaranteed fully as to principal and interest, by supranational agencies or governments other than the government of Canada, the government of a jurisdiction or the government of the United States of America and are rated "AA" by Standard & Poor's, or have an equivalent rating by one or more other approved credit rating organizations.

2. The mutual fund has been permitted to invest up to 35 percent of its net assets, taken at market value at the time of purchase, in evidences of indebtedness of any one issuer, if those securities are issued by issuers described in paragraph 1 and are rated "AAA" by Standard & Poor's, or have an equivalent rating by one or more other approved credit rating organizations.

(5) It is noted that the relief described in paragraphs 3.1(4)1 and 2 cannot be combined for one issuer.

(6) Despite subsection (4), the relief from paragraph 2.04(1)(a) of NP39, which is replaced by section 2.1 of the Instrument, provided to a mutual fund whose securities are a registered investment under the ITA or whose securities are not, and are described in the current prospectus or simplified prospectus of the mutual fund as not being foreign property under the ITA has generally been restricted to allowing the mutual fund to invest no more than 20 percent of its net assets, taken at market value at the time of purchase, in securities issued by issuers described in subsection (4) if the securities of those issuers are foreign property under the ITA.

(7) In addition to the limitation described in subsection (6), the relief from paragraph 2.04(1)(a) of NP39, which is replaced by section 2.1 of the Instrument, has generally been provided only if

(a) the securities that may be purchased under the relief referred to in subsections (4) and (6) are traded on a mature and liquid market;

(b) the acquisition of the evidences of indebtedness by the mutual fund is consistent with its fundamental investment objectives;

(c) the prospectus or simplified prospectus of the mutual fund disclosed the additional risks associated with the concentration of the net assets of the mutual fund in securities of fewer issuers, such as the potential additional exposure to the risk of default of the issuer in which the fund has so invested and the risks, including foreign exchange risks, of investing in the country in which that issuer is located; and

(d) the prospectus or simplified prospectus of the mutual fund gave details of the relief provided by the Canadian securities regulatory authorities, including the conditions imposed and the type of securities covered by the exemption.

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

3.3 Investment in Other Mutual Funds

(1) Subsection 2.5(1) of the Instrument contains restrictions on the ability of a mutual fund to invest in the securities of another mutual fund. Subsection 2.5(2) of the Instrument provides that subsection (1) does not apply to the purchase of a mutual fund that is listed and posted for trading on a stock exchange.

(2) Subsection 2.5(2) of the Instrument removes from the fund of funds rules any security of an issuer that may technically be a mutual fund, such as a subdivided offering or an index participation unit, but that is not a conventional mutual fund and for which the fund of funds rules should not be applicable. Since those vehicles are generally listed on a stock exchange, the Canadian securities regulatory authorities have used this distinguishing feature to define the vehicles whose securities may be purchased by a mutual fund without regard to the fund of funds regime. The purchase of those vehicles is, of course, subject to the other investment restrictions of the Instrument, including, without limitation, section 2.1 of the Instrument.

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

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

PART 4 USE OF SPECIFIED DERIVATIVES

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

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

1. A mutual fund may only invest in or use clearing corporation options and over-the-counter options if the portfolio adviser advising with respect to these investments

   (a) is permitted, either by virtue of registration as an adviser under the securities legislation or commodity futures legislation of the jurisdiction in which the portfolio adviser is providing the advice or an exemption from the requirement to be registered, to provide that advice to the mutual fund under the laws of that jurisdiction; and

   (b) has satisfied all applicable option proficiency requirements of that jurisdiction which, ordinarily, will involve completion of the Canadian Options Course.

2. A mutual fund may invest in or use futures and options on futures only if the portfolio adviser advising with respect to these investments or uses is registered as an adviser under the securities or commodity futures legislation of the jurisdiction in which the portfolio adviser is providing the advice, if this registration is required in that jurisdiction, and meets the proficiency requirements for advising with respect to futures and options on futures in the jurisdiction.

3. A portfolio adviser of a mutual fund that receives advice from a non-resident sub-adviser as contemplated by section 2.10 of the Instrument is not relieved from the registration requirements described in paragraphs 1 and 2.

4. In Ontario, a non-resident sub-adviser is required, under the commodity futures legislation of Ontario, to be registered in Ontario if it provides advice to another portfolio adviser of a mutual fund in Ontario concerning the use of standardized futures by the mutual fund. Section 2.10 of the Instrument does not exempt the non-resident sub-adviser from this requirement. A non-resident sub-adviser should apply for an exemption in Ontario if it wishes to carry out the arrangements contemplated by section 2.10 without being registered in Ontario under that legislation.

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

4.4 **Cash Cover** - The definition of "cash cover" in the Instrument prescribes the securities or other portfolio

assets that may be used to satisfy the cash cover requirements relating to specified derivatives positions of mutual funds required by Part 2 of the Instrument. The definition of "cash cover" includes various interest-bearing securities; the definition includes interest accrued on those securities, and so mutual funds are able to include accrued interest for purposes of cash cover calculations.

PART 5 LIABILITY AND INDEMNIFICATION

5.1 Liability and Indemnification

(1) Subsection 4.4(1) of the Instrument contains provisions that require that any agreement or declaration of trust under which a person or company acts as manager of a mutual fund provide that the manager is responsible for any loss that arises out of the failure of it, and of any person or company retained by it or the mutual fund to discharge any of the manager's responsibilities to the mutual fund, to satisfy the standard of care referred to in that section. Subsection 4.4(2) of the Instrument provides that a mutual fund shall not relieve the manager from that liability.

(2) The purpose of these provisions is to ensure that the manager remains responsible to the mutual fund and therefore indirectly to its securityholders for the duty of care that is imposed by the securities legislation of most jurisdictions, and to clarify that the manager is responsible to ensure that service providers perform to the level of that standard of care. The Instrument does not regulate the contractual relationships between the manager and service providers; whether a manager can seek indemnification from a service provider that fails to satisfy that standard of care is a contractual issue between those parties.

(3) Subsection 4.4(5) of the Instrument provides that section 4.4 does not apply to any losses to a mutual fund or securityholder arising out of an action or inaction by a custodian or sub-custodian or by a director of a mutual fund. A separate liability regime is imposed, on custodians or sub-custodians by section 6.6 of the Instrument. Directors are subject to the liability regime imposed by the relevant corporate legislation.

PART 6 SECURITYHOLDER MATTERS

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

6.2 Limited Liability

(1) Mutual funds generally are structured in a manner that ensures that investors are not exposed to the risk of loss of an amount more than their original investment. This is a very important and essential attribute of mutual funds.

(2) Mutual funds that are structured as corporations do not raise pressing liability problems because of the limited liability regime of corporate statutes.

(3) Mutual funds that are structured as limited partnerships may raise some concerns about the loss of limited liability if limited partners participate in the management or control of the partnership. The Canadian securities regulatory authorities encourage managers of mutual funds that are structured as limited partnerships to consider this issue in connection with the holding of meetings of securityholders, even if required under section 5.1 of the Instrument. In addition, all managers of mutual funds that are structured as limited partnerships should consider whether disclosure and discussion of this issue should be included as a risk factor in simplified prospectuses.

6.3 Calculation of Fees - Paragraph 5.1(a) of the Instrument requires securityholder approval before the basis of the calculation of a fee or expense that is charged to a mutual fund is changed in a way that could result in an increase in charges to the mutual fund. The Canadian securities regulatory authorities note that the phrase "basis of the calculation" includes any increase in the rate at which a particular fee is charged to the mutual fund.

PART 7 CHANGES

7.1 Integrity and Competence of Mutual Fund Management Groups

(1) Paragraph 5.5(1)(a) of the Instrument requires that the approval of the securities regulatory authority be obtained before the manager of a mutual fund is changed. Subsection 5.5(2) of the Instrument contemplates similar approval to a change in control of a manager.

(2) In connection with each of these approvals, applicants are required by section 5.7 of the

Instrument to provide information to the securities regulatory authority concerning the integrity and experience of the persons or companies that are proposed to be involved in, or control, the management of the mutual fund after the proposed transaction.

(3) The Canadian securities regulatory authorities would generally consider it helpful in their assessment of the integrity and experience of the proposed new management group that will manage a mutual fund after a change in manager if the application set out, among any other information the applicant wishes to provide

(a) the name, registered address and principal business activity or the name, residential address and occupation or employment of

(i) if the proposed manager is not a public company, each beneficial owner of securities of each shareholder, partner or limited partner of the proposed manager, and

(ii) if the proposed manager is a public company, each beneficial owner of securities of each shareholder of the proposed manager that is the beneficial holder, directly or indirectly, of more than 10 percent of the outstanding securities of the proposed manager; and

(b) information concerning

(i) if the proposed manager is not a public company, each shareholder, partner or limited partner of the proposed manager,

(ii) if the proposed manager is a public company, each shareholder that is the beneficial holder, directly or indirectly, of more than 10 percent of the outstanding securities of the proposed manager,

(iii) each director and officer of the proposed manager, and

(iv) each proposed director, officer or individual trustee of the mutual fund.

(4) The Canadian securities regulatory authorities would generally consider it helpful if the information relating to the persons and companies referred to in paragraph (3)(b) included

(a) for a company

(i) its name, registered address and principal business activity,

(ii) the number of securities or partnership units of the proposed manager beneficially owned, directly or indirectly, and

(iii) particulars of any existing or potential conflicts of interest that may arise as a result of the activities of the company and its relationship with the management group of the mutual fund; and

(b) for an individual

(i) his or her name, birthdate and residential address,

(ii) his or her principal occupation or employment,

(iii) his or her principal occupations or employment during the five years before the date of the application, with a particular emphasis on the individual's experience in the financial services industry,

(iv) the individual's educational background, including information regarding courses successfully taken that relate to the financial services industry,

(v) his or her position and responsibilities with the proposed manager or the controlling shareholders of the proposed manager or the mutual fund,

(vi) whether he or she is, or within five years before the date of the application has been, a director, officer or promoter of any reporting issuer other than the mutual fund, and if so, disclosing the names of the reporting issuers and their business purpose, with a particular emphasis on relationships between the individual and other mutual funds,

(vii) the number of securities or partnership units of the proposed manager beneficially owned, directly or indirectly,

(viii) particulars of any existing or potential conflicts of interest that may arise as a result of the individual's outside business interests and his or her relationship with the management group of the mutual fund, and

(ix) a description of the individual's relationships to the proposed manager and other service providers to the mutual fund.

(5) The Canadian securities regulatory authorities would generally consider it helpful in their assessment of the integrity and experience of the persons or companies that are proposed to manage a mutual fund after a change of control of the manager, if the application set out, among any other information that applicant wishes to provide, a description of

(a) the proposed corporate ownership of the manager of the mutual fund after the proposed transaction, indicating for each proposed direct or indirect shareholder of the manager of the mutual fund the information about that shareholder referred to in subsection (4);

(b) the proposed officers and directors of the manager of the mutual fund, of the mutual fund and of each of the proposed controlling shareholders of the mutual fund, indicating for each individual, the information about that individual referred to in subsection (4);

(c) any anticipated changes to be made to the officers and directors of the manager of the mutual fund, of the mutual fund and of each of the proposed controlling shareholders of the mutual fund that are not set out in paragraph (b); and

(d) the relationship of the members of the proposed controlling shareholders and the other members of the management group to the manager and any other service provider to the mutual fund.

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

7.3 Regulatory Approval for Reorganizations

(1) Paragraph 5.7(1)(b) of the Instrument requires certain details to be provided in respect of an application for regulatory approval required by paragraph 5.5(1)(b) that is not automatically approved under subsection 5.6(1). The Canadian securities regulatory authorities will be reviewing this type of proposed transaction, among other things, to ensure that adequate disclosure of the differences between the funds participating in the proposed transaction is given to securityholders of the mutual fund that will be merged, reorganized or amalgamated with another mutual fund.

(2) If a mutual fund is proposed to be merged, amalgamated or reorganized with a mutual fund that has a net asset value that is smaller than the net asset value of the terminating mutual fund, the Canadian securities regulatory authorities will consider the implications of the proposed transaction on the smaller continuing mutual fund. The Canadian securities regulatory authorities believe that this type of transaction generally would constitute a significant change for the smaller continuing mutual fund, thereby triggering the requirements of paragraph 5.1(g) and section 5.10 of the Instrument.

7.4 Significant Changes

(1) The Canadian securities regulatory authorities will not outline all changes in a mutual fund that could constitute a significant change for the mutual fund within the meaning of the Instrument. However, they wish to state their views of two matters in this Policy.

(2) First, the Canadian securities regulatory authorities note that the change of portfolio adviser of a mutual fund will generally constitute a significant change for the mutual fund.

(3) In addition, the departure of a high-profile individual from the employ of a portfolio adviser of a mutual fund may constitute a significant change for the mutual fund, depending on the circumstances. The definition of significant change is based on a change in the business, operations or affairs of a mutual fund that would be considered important by a reasonable investor or securityholder. Whether such a person would consider the departure of a high-profile individual to be important in this sense would likely depend substantially on how prominently the mutual fund featured that individual in its marketing. The Canadian securities regulatory authorities consider it unlikely that a mutual fund that emphasized the ability of a particular individual to encourage investors to purchase the fund could later take the position that the departure of that individual was immaterial to investors and therefore not a significant change.

PART 8 CUSTODIANSHIP OF PORTFOLIO ASSETS

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

8.2 Book-Based System

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

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

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

PART 9 CONTRACTUAL PLANS

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

PART 10 SALES AND REDEMPTIONS OF SECURITIES

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

(a) investors' cash is received by a mutual fund promptly;

(b) the opportunity for loss of an investors' cash before investment in the mutual fund is minimized; and

(c) the mutual fund or the appropriate investor receives all interest that accrues on cash during the periods between delivery of the cash by an investor until investment in the mutual fund, in the case of the purchase of mutual fund securities, or between payment of the cash by the mutual fund until receipt by the investor, in the case of redemptions.

10.2 Interpretation

(1) The Instrument refers to "securityholders" of a mutual fund in several provisions, most notably in Parts 9 and 10 when referring to purchase and redemption orders received by a mutual fund or a participating dealer or principal distributor from "securityholders".

(2) Mutual funds must keep a record of the holders of their securities. A mutual fund registers a holder of its securities on this record as requested by the person or company placing a purchase order or as subsequently requested by that registered securityholder. The Canadian securities regulatory authorities are of the view that a mutual fund is entitled to rely on its register of holders of securities to determine the names of such holders and in its determination as to whom it is to take instructions from.

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

10.3 Receipt of Orders

(1) A principal distributor or participating dealer of a mutual fund should endeavour, to the extent possible, to receive cash to be invested in the mutual fund at the time the order to which they pertain is placed.

(2) A dealer receiving an order for redemption should, at the time of receipt of the investor's order, obtain from the investor all relevant documentation required by the mutual fund in respect of the redemption including, without limitation, any written request for redemption that may be required by the mutual fund, duly completed and executed, and any certificates representing the mutual fund securities to be redeemed, so that all required documentation is available at the time the redemption order is transmitted to the mutual fund or to its principal distributor for transmittal to the mutual fund.

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

10.5 Coverage of Losses

(1) Subsection 9.4(6) of the Instrument provides that certain participating dealers may be required to compensate a mutual fund for a loss suffered as the result of a failed settlement of a purchase of securities of the mutual fund. Similarly, subsection 10.5(3) of the Instrument provides that certain participating dealers may be required to compensate a mutual fund for a loss suffered as the result of a redemption that could not be completed due to the failure to satisfy the requirements of the mutual fund concerning redemptions.

(2) The Canadian securities regulatory authorities have not carried forward into the Instrument the provisions contained in NP39 relating to a participating dealer's ability to recover from their clients or other participating dealers any amounts that they were required to pay to a mutual fund. If participating dealers wish to provide for such rights they should make the appropriate provisions in the contractual arrangements that they enter into with their clients or other participating dealers.

PART 11 COMMINGLING OF CASH

11.1 Commingling of Cash

(1) Part 11 of the Instrument requires principal distributors and participating dealers to account separately for cash they may receive for the purchase of, or upon the redemption of, mutual fund securities. Those principal distributors and participating dealers are prohibited from commingling any cash so received with their other assets or with cash held for the purchase or upon the sale of securities of other types of securities. The

Canadian securities regulatory authorities are of the view that this means that dealers may not deposit into the trust accounts established under Part 11 cash obtained from the purchase or sale of other types of securities such as guaranteed investment certificates, government treasury bills, segregated funds or bonds.

(2) Subsections 11.1(2) and 11.2(2) of the Instrument state that principal distributors and participating dealers, respectively, may not use any cash received for the investment in mutual fund securities to finance their own operations. The Canadian securities regulatory authorities are of the view that any costs associated with returned client cheques that did not have sufficient funds to cover a trade ("NSF cheques") are a cost of doing business and should be borne by the applicable principal distributor or participating dealer and should not be offset by interest income earned on the trust accounts established under Part 11 of the Instrument.

(3) No overdraft positions should arise in these trust accounts.

(4) Subsections 11.1(3) and 11.2(3) of the Instrument prescribe the circumstances under which a principal distributor or participating dealer, respectively, may withdraw funds from the trust accounts established under Part 11 of the Instrument. This would prevent the practice of "lapping". Lapping occurs as a result of the timing differences between trade date and settlement date, when cash of a mutual fund client held for a trade which has not yet settled is used to settle a trade for another mutual fund client who has not provided adequate cash to cover the settlement of that other trade on the settlement date. The Canadian securities regulatory authorities view this practice as a violation of subsections 11.1(3) and 11.2(3) of the Instrument.

(5) Subsections 11.1(4) and 11.2(4) of the Instrument require that interest earned on cash held in the trust accounts established under Part 11 of the Instrument be paid to the applicable mutual fund or its securityholders "pro rata based on cash flow". The Canadian securities regulatory authorities are of the view that this requirement means, in effect, that the applicable mutual fund or securityholder should be paid the amount of interest that the mutual fund or securityholder would have received had the cash held in trust for that mutual fund or securityholder been the only cash held in that trust account.

(6) Paragraph 11.3(b) of the Instrument requires that trust accounts maintained in accordance with sections 11.1 or 11.2 of the Instrument bear interest "at rates equivalent to comparable accounts of the financial institution". A type of account that ordinarily pays zero interest may be used for trust accounts under sections 11.1 or 11.2 of the Instrument so long as zero interest is the rate of interest paid on that type of account for all depositors other than trust accounts.

PART 12 PUBLICATION OF NET ASSET VALUE PER SECURITY

12.1 Publication of Net Asset Value per Security - Subsection 13.1(4) of the Instrument requires a mutual fund that arranges for the publication of its net asset value per security in the financial press to ensure that its current net asset value per security is provided on a timely basis to the financial press. This provision ensures that a mutual fund takes steps to calculate the net asset value per security as quickly as is commercially practicable following the valuation date or time, and to make the results of that calculation available to the financial press as quickly as is commercially practicable. A mutual fund should, to the extent practicable, attempt to meet the deadlines of the financial press for publication in order to ensure that its net asset values per security are publicly available as quickly as possible.

PART 13 PROHIBITED REPRESENTATIONS AND SALES COMMUNICATIONS

13.1 Misleading Sales Communications

(1) Part 15 of the Instrument prohibits misleading sales communications relating to mutual funds and asset allocation services. Whether a particular description, representation, illustration or other statement in a sales communication is misleading depends upon an evaluation of the context in which it is made. The following list sets out some of the circumstances, in the view of the Canadian securities regulatory authorities, in which a sales communication would be misleading. No attempt has been made to enumerate all such circumstances since each sales communication must be assessed individually.

1. A statement would be misleading if it lacks explanations, qualifications, limitations or other statements necessary or appropriate to make the statement not misleading.

2. A representation about past or future investment performance would be misleading if it is

(a) a portrayal of past income, gain or growth of assets that conveys an impression of the net investment results achieved by an actual or hypothetical investment that is not justified under the circumstances;

(b) a representation about security of capital or expenses associated with an investment that is not justified under the circumstances or a representation about possible future gains or income; or

(c) a representation or presentation of past investment performance that implies that future gains or income may be inferred from or predicted based on past investment performance or portrayals of past performance.

3. A statement about the characteristics or attributes of a mutual fund or an asset allocation service would be misleading if

(a) it concerns possible benefits connected with or resulting from services to be provided or methods of operation and does not give equal prominence to discussion of any risks or associated limitations;

(b) it makes exaggerated or unsubstantiated claims about management skill or techniques; characteristics of the mutual fund or asset allocation service; an investment in securities issued by the fund or recommended by the service; services offered by the fund, the service or their respective manager; or effects of government supervision; or

(c) it makes unwarranted or incompletely explained comparisons to other investment vehicles or indices.

4. A sales communication that quoted a third party source would be misleading if the quote were out of context and proper attribution of the source were not given.

(2) Performance data information may be misleading even if it complies technically with the requirements of the Instrument. For instance, subsections 15.8(1) and (2) of the Instrument contain requirements that the standard performance data for mutual funds given in sales communications be for prescribed periods falling within prescribed amounts of time before the date of the appearance or use of the advertisement or first date of publication of any other sales communication. That standard performance data may be misleading if it does not adequately reflect intervening events occurring after the prescribed period. An example of such an intervening event would be, in the case of money market funds, a substantial decline in interest rates after the prescribed period.

(3) An advertisement that presents information in a manner that distorts information contained in the preliminary prospectus or prospectus, or preliminary simplified prospectus and annual information form, of a mutual fund or that includes a visual image that provides a misleading impression will be considered to be misleading.

(4) Any discussion of the income tax implications of an investment in a mutual fund security should be balanced with a discussion of any other material aspects of the offering.

(5) Paragraph 15.2(1)(b) of the Instrument provides that sales communications may not include any statement that conflicts with information that is contained in, among other things, a simplified prospectus. The Canadian securities regulatory authorities are of the view that a sales communication that provides performance data in compliance with the requirements of Part 15 of the Instrument for time periods that differ from the time periods for which performance data is required to be provided in a simplified prospectus under National Instrument 81-101 is not thereby in violation of the requirements of paragraph 15.2(1)(b) of the Instrument.

(6) Subsection 15.3(1) of the Instrument permits a mutual fund or asset allocation service to compare its performance to, among other things, other types of investments or benchmarks on certain conditions. Examples of such other types of investments or benchmarks to which the performance of a mutual fund or asset allocation service may be compared include consumer price indices; stock, bond or other types of indices; averages; returns payable on guaranteed investment certificates or other certificates of deposit; and returns from an investment in real estate.

(7) Paragraph 15.3(1)(c) of the Instrument requires that if the performance of a mutual

fund or asset allocation service is compared to that of another investment or benchmark, the comparison sets out clearly any factors necessary to ensure that the comparison is fair and not misleading. Such factors would include an explanation of any relevant differences between the mutual fund or asset allocation service and the investment or benchmark to which it is compared. Examples of such differences include any relevant differences in the guarantees of, or insurance on, the principal of or return from the investment or benchmark; fluctuations in principal, income or total return; any differing tax treatment; and, for a comparison to an index or average, any differences between the composition or calculation of the index or average and the investment portfolio of the mutual fund or asset allocation service.

13.2 Other Provisions

(1) Subsection 15.9(1) of the Instrument imposes certain disclosure requirements for sales communications in circumstances in which there was a change in the business, operations or affairs of a mutual fund or asset allocation service during or after a performance measurement period of performance data contained in the sales communication that could have materially affected the performance of the mutual fund or asset allocation service. Examples of these changes are changes in the management, investment objectives, portfolio adviser, ownership of the manager, fees and charges, or of policies concerning the waiving or absorbing of fees and charges, of the mutual fund or asset allocation service; or of a change in the characterization of the mutual fund as a money market fund.

(2) Paragraph 15.11(1)5 of the Instrument requires that no non-recurring fees and charges that are payable by some or all securityholders and no recurring fees and charges that are payable by some but not all securityholders be assumed in calculating standard performance data. Examples of non-recurring types of fees and charges are front-end sales commissions and contingent deferred sales charges, and examples of recurring types of fees and charges are the annual fees paid by purchasers who purchased on a contingent deferred charge basis.

(3) Paragraphs 15.11(1)2 and 15.11(2)2 of the Instrument require that no fees and charges related to optional services be assumed in calculating standard performance data. Examples of these fees and charges include transfer fees, except in the case of an asset allocation service, and fees and charges for registered retirement savings plans, registered retirement income funds, registered education savings plans, pre-authorized investment plans and systematic withdrawal plans.

(4) The Canadian securities regulatory authorities are of the view that it is inappropriate and misleading for a mutual fund that is continuing following a merger to prepare and use *pro forma* performance information or financial statements that purport to show the combined performance of the two funds during a period before their actual merger. The Canadian securities regulatory authorities are of the view that such *pro forma* information is hypothetical, involving the making of many assumptions that could affect the results.

PART 14 CALCULATION OF MANAGEMENT EXPENSE RATIO

14.1 Calculation of Management Expense Ratio

(1) Part 16 of the Instrument sets out the method to be used by a mutual fund in calculating its management expense ratio. The requirements contained in Part 16 are applicable in all circumstances in which a mutual fund calculates and discloses a management expense ratio. This includes disclosure in a sales communication, a simplified prospectus, an annual information form, financial statements or in a report to securityholders.

(2) Paragraph 16.1(1)(a) requires the mutual fund to use its "total expenses" for a financial year as shown in its income statement as the basis for the calculation of management expense ratio. Total expenses will include interest charges and taxes of all types, including sales taxes and GST, payable by the mutual fund. Brokerage charges are not considered to be part of total expenses as they are included in the cost of purchasing, or netted out of the proceeds from selling, portfolio assets.

PART 15 SECURITYHOLDER RECORDS

15.1 Securityholder Records - Section 18.1 of the Instrument requires the maintenance of securityholder records, including past records, relating to the issue and redemption of securities and distributions of the mutual fund. Section 18.1 does not require that these records need be held indefinitely. It is up to the particular mutual fund, having regard to prudent business practice and any

applicable statutory limitation periods, to decide how long it wishes to retain old records.

PART 16 EXEMPTIONS AND APPROVALS

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

16.2 Exemptions under Prior Policies

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

(2) The Canadian securities regulatory authorities are of the view that the fact that a number of small amendments have been made to many of the provisions of the Instrument from the corresponding provision of NP39 should not lead to the conclusion that the provisions are not "substantially similar", if the general purpose of the provisions remain the same. For instance, even though some changes have been made in the Instrument, the Canadian securities regulatory authorities consider paragraph 2.2(1)(a) of the Instrument to be substantially similar to paragraph 2.04(1)(b) of NP39, in that the primary purpose of both provisions is to prohibit mutual funds from acquiring securities of an issuer sufficient to permit the mutual fund to control or significantly influence the control of that issuer.

16.3 Waivers and Orders concerning "Fund of Funds" - The CSA in a number of jurisdictions have provided waivers and orders from NP39 and securities legislation to permit "fund of funds" to exist and carry on investment activities not otherwise permitted by NP39 or securities legislation. Some of those waivers and orders contained "sunset" provisions that provided that they expired when legislation or a CSA policy or rule came into force that effectively provided for a new "fund of funds" regime. For greater certainty, the Canadian securities regulatory authorities note that the coming into force of the Instrument will not trigger the "sunset" of those waivers and orders.

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