

MSC Notice 2001-24

MANITOBA SECURITIES COMMISSION

REQUEST FOR COMMENTS ON THE APPROPRIATE USE OF AFTER-TAX CREDIT PERFORMANCE DATA BY LABOUR-SPONSORED INVESTMENT FUNDS

Purpose of Notice

The Commission is seeking comments on the appropriate use of after-tax credit performance data by labour-sponsored investment funds. Responses to and comments received on this Notice will be considered by the Commission in its formulation of a policy regarding the appropriate use of after-tax credit performance data.

The Issue

National Instrument 81-102 Mutual Fund (“NI 81-102”) and its Companion Policy (“NI 81-102CP”) regulate the operation of mutual funds which includes labour-sponsored investment funds or LSIFs. Part 15 of NI 81-102 Sales Communication and Prohibited Representations sets out the rules regarding sales communications, performance data, advertisements, performance measurement periods, calculation of performance data, including identifying prohibited disclosure and representations. Part 2 of 81-102CP provides comments on the definitions of performance data, public medium and sales communication contained in NI 81-102. Part 13 of 81-102CP Prohibited Representations and Sales Communications provides guidance regarding misleading sales communications and other provisions.

“Sales communication” means a communication relating to, and by, a mutual fund or asset allocation service, its promoter, manager, portfolio advisor, principal distributor, a participating dealer or a person or company providing services to any of them, that is made to a securityholder of the mutual fund or participant in the asset allocation service or to a person or company who 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. “Advertisement” is defined as a type of sales communication. However, such information is not considered to be a sales communication if it is contained in a prospectus, annual information form, financial statements, trade confirmations or statements of account.

Generally, sales communications shall not be untrue or misleading, include any statement that conflicts with information that is contained in the prospectus of a fund and must be calculated and disclosed in compliance with the provisions of NI 81-102.

After-tax credit performance data or “ATCPD” is performance data for time periods after which shareholders of a LSIF can redeem their shares without re-payment of tax credits that takes into account such tax credits.

Essentially, the issue is whether or not performance data that purports to illustrate the return earned by an investor who has held an investment in a LSIF for a prescribed period of time which takes into account the tax credits received by that investor, is appropriate.

Alternative Solutions to this Issue

There are three potential solutions to this issue, as follows:

1. Prohibit the use of ATCPD in any fashion. Only true performance based rates of return for a fund should be permitted.

This position is based on the argument that ATCPD does not reflect true fund performance and is an artificial number which will potentially mislead the investing public. It also puts undue emphasis on a one-time tax credit.

2. Permit the use of ATCPD in shareholder communications only. The use of ATCPD in more broadly based advertisements, brochures and other forms of sales communications would be prohibited.

The limited use of ATCPD would be subject to the following conditions:

- The actual performance of the LSIF for the same period must be shown and must be given more prominence than the ATCPD. The LSIF should also explain that this performance data constitutes the actual performance of the investments made by the LSIF.
- The LSIF gives prominent and complete explanation of the meaning of the ATCPD. The explanation should describe that shareholders who bought their shares before the applicable time periods received one-time specified tax credits (the time period and the tax credits should be quantified in the explanation) and that those shareholders can now redeem their shares without repayment of those tax credits. The explanation should also emphasize that this information is relevant only to those specific investors who received the tax credit. If the tax credit and redemption timing changed in recent years, the changed timing and tax credits should also be referred to.
- The LSIF calculates its ATCPD consistently in accordance with the following formula. Specifically, from the net asset value per share of the LSIF on the first day of the applicable period, deduct the relevant tax credit percentage from that number and use the reduced number as a starting figure in calculating “standard performance” using the required formula established by NI 81-102.
- Tax credits vary from province-to-province. The ATCPD is relevant only for shareholders who lived in Manitoba at the time they purchased the shares.

Depending on whether the other provincial regulators permit disclosure of ATCPD, if the LSIF decides to give shareholders in other provinces this information, specific provincial tax credits and redemption timing will have to be taken into account.

This position is based on the belief that this information is relevant once the applicable re-payment time period has expired for those investors who had bought prior to the time period. Accordingly, ATCPD should not be provided in advertisements or other forms of sales communications, other than shareholder communications and should not be provided for any periods prior to the expiration of the applicable redemption re-payment period. Essentially, ATCPD provides meaningful information to existing shareholders but only for a time period after which shareholders of the LSIF can redeem their shares without penalty.

It should be noted that this is the position of staff of the Securities Commissions of Alberta, Saskatchewan, Ontario and Nova Scotia. This is also the position supported by staff of the Commission.

3. Permit the unrestricted use of ATCPD in shareholder communications and all forms of sales communications.

This position is based on the argument that such information is meaningful to existing and prospective investors, and any concerns regarding the information being misused or misleading can be dealt with by way of disclaimers and explanatory notes.

Comments Requested

The Commission is seeking comments on this issue which it will consider in finalizing its policy regarding the appropriate use of ATCPD.

Comment Period

The comment period will run for sixty days and will end on October 7, 2001. Comments should be submitted to:

The Manitoba Securities Commission
1130 – 405 Broadway Avenue
Winnipeg, MB R3K 1X6

Attention: R. B. Bouchard, C.A.
Director – Corporate Finance

Date of Notice

August 7, 2001