COMPANION POLICY 81-104CP TO NATIONAL INSTRUMENT 81-104 COMMODITY POOLS

PART 1 PURPOSE

1.1 **Purpose** - The purpose of this Policy is to clarify how National Instrument 81-104 (the "Instrument") integrates with National Instrument 81-102 Mutual Funds, and to bring certain matters relating to the Instrument to the attention of persons or companies involved with the establishment or administration of commodity pools.

PART 2 GENERAL STRUCTURE OF THE INSTRUMENT

2.1 **Relationship to Securities Legislation Applicable to Mutual Fund Instruments**

(1) The term "commodity pool" is defined in the Instrument as a mutual fund that is permitted to use or invest in specified derivatives and physical commodities beyond what is permitted by National Instrument 81-102. Commodity pools are subject to the ordinary mutual fund rules unless those rules are specifically excluded. Therefore, the Instrument contains only those provisions that are specific to commodity pools, and provisions applicable to all mutual funds, including commodity pools, are contained in National Instrument 81-102.

(2) Persons involved with the establishment or administration of a commodity pool are referred to the following rules:

1. National Instrument 81-102. That National Instrument contains general rules concerning the operation of mutual funds, all of which are applicable to commodity pools except as excluded by specific provisions of the Instrument.

2. The securities legislation relating to mutual funds of the jurisdictions in which a prospectus for the commodity pool will be filed. For example, commodity pools are subject to the financial statement reporting requirements for mutual funds, except as varied or supplemented in the Instrument.

3. The prospectus requirements of the securities legislation of a jurisdiction applicable to long form issuers generally, and mutual funds in particular. National Instrument 81-101 Mutual Fund Prospectus Disclosure states that commodity pools may not use the prospectus disclosure system created by that National Instrument.

2.2 **Derivatives Use** - The regime implemented by the Instrument is designed to allow commodity pools considerable freedom in entering into derivatives transactions. Commodity pools are not subject to sections 2.7 and 2.8 of National Instrument 81-102, which contain most of the rules governing specified derivatives used by mutual funds. Commodity pools, however, remain subject to the main investment restrictions and rules governing investment practices contained in National Instrument 81-102 that do not relate directly to derivatives or commodity transactions. In particular, commodity pools remain subject to paragraphs 2.6(b) and (c) of National Instrument 81-102, which prohibit mutual funds from purchasing securities on margin or selling securities short, unless permitted by sections 2.7 or 2.8 of that National Instrument. These provisions allow a commodity pool to purchase securities on margin or sell securities short only to the extent that a pool would be considered to do so when entering into a specified derivatives transaction in compliance with the requirements of sections 2.7 or 2.8 of National Instrument 81-102.

PART 3 LIMITED LIABILITY

3.1 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. The CSA consider this a very important and essential attribute of funds. This is especially important in the context of commodity pools. One of the most important rationales for the existence of commodity pools is that they enable investors to invest indirectly in certain types of derivative products, particularly futures and forwards, without putting more than the amount of their investment at risk. A direct investment in some derivative products could expose an investor to losses beyond the original investment.

(2) Mutual funds structured as corporations do not raise pressing liability problems because of the limited liability regime of corporate statutes.

(3) Mutual funds 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 statute and case law concerning when limited partners can lose their limited partner status, including the Quebec Civil Code, varies from province to province. Therefore, paragraph 10.2(l) of the Instrument requires each commodity pool to disclose risks associated with the loss of limited liability of a limited partner that has invested in a commodity pool structured as a limited partnership; proper compliance with this requirement will involve disclosure of risks associated with the jurisdictions in which the prospectus is filed. Mutual funds structured as trusts may also raise liability issues in some contexts. Paragraph 10.2(l) of the Instrument also requires disclosure of risks associated with the structuring of a commodity pool as a limited

partnership or as a trust in relation to the possibility that purchasers of commodity pool securities may become liable to make an additional contribution beyond the price of the securities.

(4) The CSA expect that commodity pools will be structured in a manner that provides as much assurance as possible to their securityholders that securityholders will not be at risk for more than the amount of their original investment. The CSA recommend that commodity pool promoters and managers consider other ways, apart from the structuring of a pool, to limit the liability of securityholders. For example, commodity pools could attempt to enter into contracts only if the other party to the agreement agreed to limit recourse under the agreement to the assets of the pool. In addition, managers of commodity pools structured as limited partnerships should consider whether a securityholder meeting could cause limited partners to lose limited liability status.