



Ontario
Securities
Commission

Commission Des
valeurs mobilières
de l'Ontario

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VIA SEDAR

January 16, 2002

Fraser Milner Casgrain LLP

Attention: Dan Dishy

Dear Sirs/Mesdames:

**Re: Tuscarora Energy Growth Fund Inc.
MRRS Exemptive Relief Application dated December 3, 2001 pursuant to
National Instrument 81-102 Mutual Funds; SEDAR Project No. 407520;
Application #1301/01**

Pursuant to a MRRS application dated December 3, 2001 (the "Application"), you applied to the regulator in each of the provinces and territories with exception of Quebec (the "Decision Makers") for an exemption on behalf of Tuscarora Energy Growth Fund Inc. (the "Fund") pursuant to subsection 19.1 of National Instrument 81-102 - Mutual Funds ("NI 81-102") from the applicability of Part 7 of NI 81-102 in relation to incentive fees.

In the Application, the Fund represented the following:

1. The Fund is a corporation incorporated under the *Canada Business Corporations Act* by articles of incorporation dated November 1, 2001.
2. The Fund is a labour-sponsored venture capital corporation under the *Income Tax Act* (Canada).
3. The Fund is a mutual fund as defined in subsection 1(1) of the Securities Act (Ontario) (the "Act") and in securities legislation of each of other provinces and territories of Canada, with the exception of Quebec. A preliminary prospectus for the Fund dated November 2, 2001 has been filed with the Decision Makers. An amended and restated preliminary prospectus dated November 21, 2001 was also filed with each of the Decision Makers and also with Quebec (the "Prospectus"). The Fund will, upon the issuance of a receipt for a (final) prospectus, distribute securities in every province and territory of Canada
4. Front Street Capital Inc. will be the manager of the Fund (the "Manager") and Tuscarora Investment Management Inc. will be the investment advisor of the Fund (the "Investment Advisor").

5. As disclosed in the Prospectus, "eligible investment" means an investment which, at the time of purchase, qualifies as an investment in an eligible business as defined in the *Income Tax Act* (Canada). Eligible investment excludes liquid investments.
6. For the purpose of the relief in this letter, "income" means all interests, dividends, fees, capital gains and other distributions received by the Fund from its investment in eligible investments.
7. The Investment Advisor will be paid a performance bonus (the "Performance Bonus") by the Fund based on the realized gains and the cumulative performance of the portfolio of eligible investments of the Fund. The Prospectus discloses that before the Performance Bonus can be paid on the realization of any eligible investment, the portfolio of eligible investments must have:

- (a) earned sufficient income to generate a rate of return on the Fund's eligible investments as a whole in excess of a cumulative annualized threshold return of 6%; for this purpose, the income on eligible investments includes realized and unrealized investment gains and realized and unrealized losses earned and incurred since the inception of the Fund;
- (b) earned income from the eligible investment which provides a cumulative investment return at an average annual rate in excess of 6% since the date of the investment; and
- (c) fully recouped an amount equal to all principal invested in the eligible investment.

Subject to all of the above, the Performance Bonus will be an amount equal to the lesser of

- (i) 20% of all income earned from the eligible investment, and
- (ii) the portion of that amount that does not reduce returns to shareholders on the investment portfolio below a cumulative annualized threshold return of 6%.

For the purposes of subparagraph (a) above, a "cumulative annualized threshold return of 6%" means a total return across all investments held in the Fund's eligible investment portfolio of 6% per annum, compounded from the time the investments were made until the time the performance bonus calculation is made. For the purposes of subparagraph (b) above, a "cumulative investment return at an average annual rate in excess of 6%" means a total return on the particular investment being divested greater than 6%, compounded since the date of that investment until the time the Performance Bonus calculation is made.

8. The Performance Bonus does not conform to the requirements of section 7.1 of NI 81-102. The Performance Bonus is based on realized gains and the cumulative performance of the venture portfolio (and not in relation to a benchmark). The Performance Bonus is not based on the total return of the Fund because liquid investments are not included in the Fund's portfolio of eligible investments and because the quantum of the Performance Bonus is calculated on an investment-by-investment basis.
9. The Fund is designed to encourage the public to invest in a vehicle that makes venture capital investments. The making of venture capital investments is substantially different from the types of investments generally made by public mutual funds.

10. The basis for payment of the Performance Bonus, as described in paragraph 7 (the “Incentive Arrangement”), is appropriate in light of the nature of venture capital investing and is consistent with the incentives used in the venture capital industry, and in particular, in private venture capital funds. The Fund believes that it needs to be able to offer an incentive fee arrangement similar to those of other venture capital funds in order to attract the necessary professional expertise to be able to carry out the investment operations and its mandate.
11. The Fund will not pay the Performance Bonus on any partial disposition of an eligible investment unless and until the Fund receives (from all dispositions of that investment on a cumulative basis) an amount equal to at least the full amount of the principal invested in the entire eligible investment.
12. The (final) prospectus of the Fund will:
 - (a) fully disclose that the Investment Advisor considers the Performance Bonus and the Incentive Arrangement to be appropriate given the disclosed investment objectives and strategies of the Fund;
 - (b) provide an explanation of why the Performance Bonus and the Incentive Arrangement are appropriate for the Fund; and
 - (c) provide an explanation of the Performance Bonus calculation for partial dispositions of an eligible investment.

This letter confirms that, based on the information and representations contained in the Application, and for the purposes described in the Application, the Decision Makers hereby exempt the Fund from Section 7.1 of NI 81-102 in respect of the Performance Bonus and Incentive Arrangement disclosed in the Prospectus, provided that the Fund will include in its (final) prospectus full, true and plain disclosure as described in paragraph 12 above.

The relief provided herein is conditional upon compliance with all other applicable provisions of NI 81-102.

Yours truly,

Merilyn Dasil

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