

## Spring Training

As our beloved Toronto Blue Jays finalize their lineup for the start of the 2016 season, so too is the OSC, which recently published a lineup of regulatory initiatives in its Statement of Priorities. We discuss this and much more in our Spring edition of the AUM Law Bulletin.



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### 1. [OSC 2016/2017 Draft Statement of Priorities](#)

The Ontario Securities Commission (OSC) has published its annual draft statement of priorities, setting out specific initiatives that it will pursue in its upcoming fiscal year. There are many items of interest to the investment management community, briefly described below. Comments are being accepted on the draft until May 9, 2016.

Repeating comments from last year's statement of priorities, the draft suggests that a well-functioning investor/advisor relationship is critical to the economic well-being of Ontarians and to healthy capital markets. With that in mind, one OSC priority is to publish and conduct consultations on provisions to create a best interest standard, as well as consultations on reforms (or guidance) under National Instrument 31-103 – *Registration Requirements, Exemptions and Ongoing Registrant Obligations* (NI 31-103) to help improve the client/advisor relationship. The OSC also intends to finalize its analysis of advisor compensation practices. Interestingly, the draft statement of priorities indicates OSC Staff will identify those practices that appear inconsistent with current regulatory expectations. It is currently unknown whether identifying such practices will lead to reforms banning them.

### In Brief

The [2016 Investment Executive Regulators' Report Card](#) polled 109 CCOs and other company executives from firms regulated by self-regulating organizations (IIROC and MFDA), and by provincial regulators. Although the participants' perceptions of their regulators marginally improved from last year, they fared poorly across the board in the "awareness of dealers' regulatory burden" category. Survey participants felt that the recent, rapid pace of reform surpasses firms' abilities to meet compliance obligations. On a more favourable note, regulators received praise for their improved industry consultation process when introducing new policy and rules, and for making themselves more available to enquiries.

The OSC also telegraphed its intention to closely monitor the newly introduced changes to the exempt market regulatory regime to monitor market conduct. In addition, Staff will continue their targeted compliance reviews of high risk and new registrants, including online advice and portal business models. Registrants should expect a targeted review to include questions relating to their level of cyber security resilience, including measures for protection of personal investor data.

With respect to its enforcement efforts, mention is specifically made to implementing the proposed OSC Whistleblower Program, and beginning to use input from participants to pursue potential cases (see our [October 2015 bulletin](#) for more information on the proposed whistleblower policy).

We can also expect to see continued advancement on rules relating to the transparency of the fixed income market. Initiatives in this respect include the implementation of public transparency of fixed income trading data, specifically for corporate debt, with IIROC acting as the information processor. Rules with respect to over-the-counter derivatives continue to be a priority, including the introduction of a registrant regulation framework for derivatives market participants.

Similar to 2014, the OSC will be sending out a 2016 Risk Assessment Questionnaire (RAQ), with questions including the use of the new prospectus exemptions by registrants. Please stay tuned in this regard and [contact us](#) if you have any questions.

## 2. Have You Had Any Privacy Breaches?

Innovation, Science and Economic Development Canada has recently published a [consultation document](#) intended to solicit stakeholder comments for consideration as it prepares draft regulations for data breach requirements under the *Personal Information Protection and Electronic Documents Act* (PIPEDA). On June 18, 2015, the *Digital Privacy Act* amended Canada's private sector privacy laws. While most of the amendments made by the *Digital Privacy Act* are currently in force, the amendments creating a mandatory data breach reporting regime will not come into force until regulations setting out prescribed requirements have been enacted. Following the consultation process, the government will publish draft and final regulations in the Canada Gazette.

Please note that privacy laws for the private sector are not harmonized across all Canadian jurisdictions. For example, Alberta currently has in force mandatory data breach reporting requirements for all private sector organizations. Accordingly, it is important to assess a private breach on a case by case basis. Please contact a member of our [Regulatory Compliance Group](#) if you wish to learn more.

## 3. OSC Releases Report on Insider Reporting Compliance Review

Last month, the OSC published [OSC Staff Notice 51-726 Report on Staff's Review of Insider Reporting and User Guides for Insiders and Issuers](#) (the Notice), setting out the results of its review of the insider reporting practices of 100 reporting issuers and approximately 1,500 reporting insiders. Pursuant to National Instrument 55-104 *Insider Reporting Requirements and Exemptions* (NI 55-104) "reporting insiders" are usually required to file an initial insider report within 10 calendar days of becoming a reporting insider, and to file subsequent insider reports reflecting changes in an insider's holdings within five calendar days of a change. In this regard, the Notice noted that significant improvements are required with respect to the quality of insider reporting. In 70% of the issuers reviewed, the OSC found material discrepancies, including failure by reporting insiders to create or update insider profiles or to file insider reports on the System for Electronic Disclosures by Insiders. Deficiencies resulted from a variety of factors, including

### You should know...

The Canadian Securities Administrators (CSA) are encouraging investors to "**check before they invest**", to ensure they are obtaining investment advice from firms or individuals registered to provide such advice. Of particular concern is unregistered advice around binary options, as many of these platforms are based overseas and are not registered to conduct business in Canada. To check on the registration status of a firm or individual, investors can contact their [local securities regulator](#) or visit [AreTheyRegistered.ca](#). This is a good opportunity for registrants to check their own registrations and ensure their accuracy.

The OSC recently announced that a Barrie, Ontario man was **sentenced to 15 months in jail** by the Ontario Court of Justice after [an investigation](#) by the OSC's Joint Serious Offences Team. The man was convicted on two counts of unregistered trading, one count of unregistered advising and four counts of breaching cease trade orders imposed by the OSC.

### Did you know?

There is a legal requirement to provide **notice of changes affecting insurance**.

Changes may relate to:

- coverage
- deductible
- claim(s) made under the policy
- cancellation of policy

relying on third parties to make their filings, as well as unfamiliarity with the definition of “reporting insider” and “significant shareholder” in NI 55-104.

The Notice further notes that many insider-trading policies reviewed by the OSC did not properly restrict derivative-based transactions or the grant of stock-based compensation during “blackout periods” around regularly scheduled earnings announcements. The OSC notes that insider trading policies should prohibit such transactions during blackout periods in order to avoid scrutiny due to the timing of these transactions.

In order to help insiders and issuers avoid fines and other regulatory penalties, the Notice includes other recommendations that should be reviewed carefully, including by investment fund managers who report on behalf of their funds.

Please contact a member of our [Corporate Group](#) to discuss your reporting obligations.

Although there is no legal requirement to file evidence that the insurance has been renewed, instructions on the OSC’s electronic portal imply that evidence of renewal should be submitted nonetheless.

#### 4. Federal Budget Surprises for Corporate Funds

There were a few unexpected surprises for the investment fund industry in the federal budget presented on March 22, 2016. One measure impacts mutual fund corporations with multiple share classes, each representing a different investment portfolio. Currently, investors are permitted to “switch” between such classes on a capital gains tax-deferred basis. Proposed changes will eliminate such tax treatment as of October 1, 2016, such that any switches between classes will result in a disposition at fair market value. Switches can continue to be made between series of shares within the same class on a tax-deferred basis, if the only difference between the shares are with respect to management fees and expenses, and the shares provide exposure to the same investment portfolio. While such corporations can still be used to consolidate expenses and income, the impact on such vehicles and investors will be interesting to track. For additional information on the budget, please see information directly from the federal government’s website at [The Budget In Brief](#).

#### 5. Are You Thinking About an Internal Reorganization?

So, for “tax reasons”, you have been advised to reorganize your affairs in order to hold shares of your registrant through a holdco. And perhaps you have been advised to set-up a trust for “estate freeze” purposes.

As we well know, a registered firm must notify the regulators usually within 10 days after most changes to information regarding a Registered Individual, Permitted Individual or the registered firm flowing from the reorganization (i.e., directorships). A failure by a registrant to notify the OSC of such amendments may result in significant late fees or other regulatory action.

However, it is also important to know that an internal reorganization may also trigger pre-approval by the regulators. A registered firm must give the regulators 30 days written notice in accordance with subsection 11.10(2) “if it knows or has reason to believe that any person or company, alone or in combination with any other person or company, is about to acquire, or has acquired, for the first time, direct or indirect ownership, beneficial or otherwise, of 10% or more of the voting securities or other securities convertible into voting securities of (a) the registered firm; or (b) a person or company of which the registered firm is a subsidiary”. Again, this fun provision may capture your new holdco or trust, thereby subjecting a straightforward internal reorganization to pre-approval by one or more securities regulators.

If you are contemplating an internal reorganization, please [contact us](#) first.

#### 6. 81-729–Summary Report for Investment Fund and Structured Product Issuers

The [most recent annual report](#) from the OSC’s Investment Funds & Structured Products Branch describes its key activities and initiatives as well as emerging issues and trends. In addition to describing activities undertaken in 2015, the report outlines some expectations for the branch in 2016.

With respect to its ongoing examination of mutual fund fees, the report indicates that the findings from the research previously commissioned by the CSA, and comments gathered throughout the consultation

process will inform policy recommendations. The CSA expects to communicate its policy direction in the first half of 2016.

As part of the modernization of investment fund product regulation project, the CSA is continuing its long anticipated work on the final stage, which will create a separate regime for “alternative funds” (currently only generally applicable to commodity pools). At the same time, consideration is being given to whether amendments should also be made to National Instrument 81-102 – *Investment Funds* (NI 81-102) regarding the investment strategies of conventional investment funds. Work has begun on draft proposed amendments for an alternative funds regime, with a view to publishing the amendments for comment in mid-2016.

Continuous disclosure reviews of fund issuers have focused on topics including mutual fund portfolio liquidity, and fund-of-funds fees disclosure. Staff is continuing to monitor liquidity issues and may in future publish additional guidance if needed. Similarly, in their reviews, Staff has noticed errors in the calculation of the management expense ratio and trading expense ratio of fund of funds and may publish additional guidance to assist issuers with respect to regulatory expectations.

The report (and the team at AUM Law) also encourages fund managers to review the report issued by the CRR branch, [OSC Staff Notice 33-746 Annual Summary Report for Dealers, Advisers and Investment Fund Managers](#), which includes commentary on deficiencies from compliance reviews of registrants. Topics include non-delivery of net asset value adjustments, and non-compliance by fund managers of private investment funds of the prohibition on commingling fund assets with assets of the fund managers.

Please contact a member of our [Investment Funds Group](#) to discuss.

## 7. Sales Communications

Investment fund managers are reminded that language used in advertising and marketing materials is subject to certain requirements and restrictions outlined in Part 15 of NI 81-102. The following are a few items to keep in mind:

- A reference to an award is considered by OSC Staff to be a performance rating, and communications containing such references should comply with the requirements set out in NI 81-102.
- The sales communication requirements for mutual funds in Part 15 of NI 81-102 do not permit the use of a performance rating or ranking of a mutual fund that is based partially on a subjective component. An example of a subjective component would be the awardee's opinion of the quality of the manager of a fund. References to a manager's award are acceptable but not as part of a fund's rating or ranking.
- A slide deck used for presentation purposes can sometimes be considered an offering memorandum if securities are described in detail.
- Any claims made in sales communications should be corroborated and underlying assumptions should be made clear.
- Language that is unduly promotional, vague or exaggerated should be avoided. This includes statements such as “superior proven performance” or “superior risk adjusted performance”.
- If performance data is provided, it should be given equal prominence to any other performance data disclosed in the sales communication and not placed in the disclaimer at the end of the communication.
- The regulators do not support listing a client in advertising and marketing materials, even if the client consents.

Please contact a member of our [Investment Funds Group](#) for more information.

## News & Upcoming Events

We are proudly sponsoring this year's **Annual Focus Event on Registrant Regulation Conduct & Compliance**, taking place April 27-28. Attendees will have the opportunity to connect with 100+ regulators, compliance executives, industry stakeholders and legal experts. The summit also

9<sup>th</sup> Annual Focus Event on

### **REGISTRANT REGULATION** *Conduct & Compliance*

features an exclusive Q&A session with top regulators: OSC, AMF, ASC and BCSC.

The organizers are extending a 20% registration discount for friends of AUM Law (discount code AUM20). Visit the [conference page](#) for more details, or to register.

The **National Society of Compliance Professional's (NSCP) Canadian Conference** is fast approaching, with a primary focus on the challenges faced by compliance departments amidst increasing regulatory burden. The conference is taking place on Monday, April 4 at the St. Andrew's Club & Conference Centre. NSCP is extending a special offer of 75% off registration fees until 5:00 PM on Friday, April 1. Click [here](#) to register with the discount code CANADA75, or visit the [conference page](#) for more information. As previously mentioned, Erez Blumberger will be chairing a panel offering guidance on interacting with regulators and the implementation of new rules.

AUM Law primarily serves the asset management sector, with specific expertise in the regulatory and investment fund space. We strive to provide the most practical, forward-thinking advice and services, using a business model geared to efficiency, responsiveness and client service excellence. We are pleased to send you this summary of recent developments that may affect your business.



This bulletin is an overview only and it does not constitute legal advice. It is not intended to be a complete statement of the law or an opinion on any matter. No one should act upon the information in this bulletin without a thorough examination of the law as applied to the facts of a specific situation.