September 2017

Bulletin

Back to School in Full Gear

Is it just students? Not quite.

According to the Ontario Ministry of Education, there are approximately two million students across the province that go back to school every September. However, this statistic does not include regulators and their children (the regulations). With the number of proposed changes and regulations contemplated this month, this number could be much higher. Here is AUM Law's take on them.

In this bulletin

1. Charity as a Registrant: Not So Simple

Supporting a good cause can give you a great feeling and bring you closer to your community. However, as a registrant, you should always be mindful of what that donation "says" as it relates to an actual or perceived conflict. Consider the following example: A good friend of yours is playing in a charitable bowling tournament and is raising money as part of his involvement in the event. He asks you, an investment fund manager, for $250. It also happens that your good friend is an investment advisor that has, from time to time, recommended that clients invest in your fund.

In Brief

BREAKING NEWS: Ban on Binary Options

On September 28, 2017, the CSA announced a ban on binary options. This ban is a result of the implementation of Multilateral Instrument 91-102 *Prohibition of Binary Options*. Binary options are instruments where there is a payout based on satisfying a pre-determined condition typically tied to the performance of an underlying asset, often a currency, commodity, stock index, or share. Binary options have typically been used as a vehicle for fraud and offshore scams, and according to the CSA Chair, binary options are the leading type of investment fraud facing Canadians.

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First, we should note that there are no specific prohibitions on donations for investment fund managers who manage private funds. However, public mutual funds are subject to National Instrument 81-105 – Mutual Fund Sales Practices which could, in some circumstances, restrict the above mentioned donation.

For a private fund, the question of whether the donation is permissible under securities laws comes down to a conflicts consideration. When considering the example set out above, the question that ought to be asked is: "Would your friend be perceived as being obliged to you for the $250 donation such that he may recommend your fund in circumstances where such recommendation is not warranted?" While this is a conflict consideration primarily for your good friend as the investment advisor, you may also be caught up in a conflict dispute as the investment fund manager. A one-time nominal payment may not be seen as creating a conflict but what if it is an ongoing payment or a payment of a larger amount? It is prudent that you consider answers to these types of questions in advance.

2. Levelling the Playing Field or Higher Taxes?

On July 18, 2017, the Department of Finance released a consultation paper regarding *Tax Planning Using Private Corporations* (the Consultation Paper). While our expertise is in corporate and securities law, and we do not purport to be experts in tax law, these changes, if enacted as proposed, could have a significant impact on many of our clients (e.g., investment fund managers). Accordingly, there are three main areas discussed in the Consultation Paper with respect to taxation of private corporations that we would like to highlight.

First, the proposed changes would attack "dividend sprinkling" by applying a "split income" tax starting in 2018 on a dividend (effectively raising the tax rate on such income to the highest marginal rate) received by an individual derived from a business of a related individual (including through a corporation of which the related individual can exert influence) where the dividend is unreasonable having regard to such circumstances as the dividend recipient's labour and capital contributions to the business. "Dividend sprinkling" refers to the practice of lowering a family's aggregate income tax liability through a corporation paying dividends on a class or classes of shares held by family members who are in a lower tax bracket (as compared to the owner-manager).

Second, generally starting in 2018, the proposed changes would eliminate the ability to claim the Lifetime Capital Gain Exemption (i) on gains that accrued before the taxation year in which the individual turned 18 years old, (ii) on gains that accrued during the time that the subject property was held by a trust (subject to very limited exceptions), and (iii) to the extent that a taxable capital gain from the disposition of the subject property is subject to the "split income" tax discussed above. Under the proposals, a transitional rule would allow certain affected individuals to elect to realize, on a day in 2018, a capital gain in respect of eligible property by way of a deemed disposition for proceeds up to the fair market value of the property (resulting in an increase in cost basis of the property, thereby reducing taxable capital gains on a later sale) and to use their lifetime exemption with respect to the gain. However, in certain circumstances, minors cannot benefit from this transitional rule.

Third, the Consultation Paper discusses the taxation of passive investments inside a private corporation. While the federal government has not yet proposed legislation on this point, it appears that the federal government is exploring ways to remove the deferral advantage associated with a corporation using active business income to make passive investments. The Consultation Paper indicates that any such rules

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The use of the Words *Bank, Banker* and *Banking:* To be continued

On June 30, 2017, the Office of the Superintendent of Financial Institutions Canada (OSFI) issued Advisory 2017-01, which sets out how OSFI interprets and administers (a) the *Bank Act* restrictions on the use of the words "bank", "banker" and "banking" (known as the "**Bank Words**"); and (b) the exception that applies where the use of the Bank Words is not in relation to a financial services business.

The Bank Act restrictions that were initially proposed are two-fold:

(1) Every non-bank entity is restricted from acquiring, adopting or retaining a name that includes the Bank Words to indicate or describe a business in Canada or any part of a business in Canada; and

(2) Every non-bank person is restricted from using the Bank Words to indicate or describe a business in Canada or in any part of a business in Canada.

The exception to the restriction on the use of Bank Words means that non-bank persons can use the Bank Words. For example, a food bank whose sole business is to collect and stock food could use the phrase "food bank".

On August 11, 2017, the Department of Finance are intended to apply on a going forward basis (i.e., they are not intended to impact, as much as possible, existing passive investments held by a corporation).

If you might be impacted by the proposed changes, we advise you to speak with your existing tax advisor or reach out to us to help you connect with a tax specialist or otherwise assist you regarding any of your corporate needs.

We would also like to thank Ryan Morris, Partner at WeirFoulds LLP, for his contribution to this article.

3. OSC's Compliance and Registrant Regulation Branch (CRR) Annual Report: Our Takeaways

On July 11, 2017, the OSC published the Compliance and Registrant Regulation Branch's ("**CRR**") annual report: OSC Staff Notice 33-748 *Annual Summary Report for Dealers, Advisers and Investment Fund Managers* (the "**Report**").

CRR encourages registrants to read and use the Report to enhance their understanding of OSC's expectations of registrants and interpretation of regulatory requirements, understand the initial and ongoing requirements for registration and compliance requirements, review and raise awareness of new and proposed rules and other regulatory initiatives, and as a self-assessment tool to strengthen a firm's compliance with Ontario securities law.

The Report highlights areas of registrant outreach which are intended to strengthen Staff communication with registrants on compliance practices, including the Registrant Outreach Program and OSC LaunchPad. CRR also summarizes current trends in registration and highlights deficiencies identified through compliance reviews of registrants (including Staff's proposed acceptable practices to address them and unacceptable practices to prevent them), policy initiatives and other areas of focus for the 2017/18 fiscal year. Further, the Report summarizes the types of regulatory action CRR has taken when they have found serious non-compliance and misconduct at firms and by registered individuals. It also highlights cases of interest and provides additional resources for registrants. The following are some key takeaways from the Report:

1. **OSC areas of focus for upcoming compliance reviews:** CRR staff indicate in the Report that they will be focusing their compliance reviews this year in the following areas: firms who have a significant number of senior investors as clients; compliance with the new prospectus exemptions that came into force in fiscal 2016; fund expenses; funds that have large holdings in illiquid securities and their valuation procedures; high-risk firms identified from the 2016 Risk Assessment Questionnaire; and firms that participated in the "Registration as the First Compliance Review" program to assess their compliance after participating in the program.

We can assist you by preparing your firm for a compliance review.

2. **CRR involvement in regulatory projects that potentially impact the regulatory landscape in Ontario:** These initiatives involve: syndicated mortgages, targeted reforms and best interest standard projects, review of compensation practices and exempt market dealer activities and financial planning.

We have been following and will continue to follow these policy initiatives and will continue to bring you relevant updates.

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released a second consultation paper as part of its review of the federal financial sector framework. This paper seeks views on the *Bank Act* restrictions on the use of the Bank Words. As a result, OSFI is suspending the compliance expectations set out in its June 30 Advisory.

Once the Department of Finance has announced the outcome of its consultation on these restrictions, OSFI will communicate its revised expectations for compliance with the Advisory, as appropriate.

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The Importance of a Strong Expense Allocation Policy

In recent months, there has been an increased focus (both in the media and by the regulators) on incidences of overcharging clients in the Canadian investment management industry. Wholly owned subsidiaries of each of the Big Five banks entered into settlement agreements with the Ontario Securities Commission upon discovering that their clients were overcharged certain fees. While the settlements do not indicate dishonest conduct on the part of the firms, they focus on deficiencies in the systems of controls and supervision which form part of a firm's compliance system. An expense allocation policy can be a valuable tool to assist asset managers with identifying and allocating appropriate charges to the firm and to client accounts, including investment funds managed by the firm. A

3. **Common deficiencies in individual and firm registration filings:** The Report indicates that CRR continues to see non-disclosure of, or incorrect and incomplete information on, individual filings. CRR reminds firms that it is their responsibility to know the applicants they intend to sponsor registration and to keep abreast of changes to the information previously submitted by the individuals. CRR also reminds firms that individuals sponsored by the firm must not use misleading titles on the firm website or social media. Firms must ensure their personnel are aware that securities law prohibits holding oneself out to be in the business of trading or advising in securities unless the individual is registered or exempt from registration in accordance with Ontario securities law.
4. **Seniors and vulnerable investors**: The Report indicates that CRR will continue to place focus and compliance resources on conducting focused reviews of firms doing business with senior investors. CRR Staff has found that some PMs do not have written policies and procedures to adequately address the provision of investment advisory services to vulnerable investors. CRR intends to issue guidance and best practices for registrants who are dealing with senior investors to address the particular needs and issues unique to them. The Report recommends that firms review and assess their policies and procedures, including the adequacy of their processes used to identify and respond to issues unique to working with senior investors, and provides some suggested practices.

Please let us know if we can assist you with developing these policies and procedures or provide training on best practices for your staff.

5. **Lending firms**: CRR conducted reviews of a sample of "lending firms" as part of a sweep. Two firms reviewed were registered as IFMs, but based on their business model, did not need to be registered as an IFM.

We would be pleased to consult with firms that operate, or intend to operate, in a similar fashion to these lending firms to assess the appropriate registration categories given their business model.

6. **Marketing in public places**: In the Report, CRR reiterates Staff's expectation that marketing materials must comply with CSA Staff Notice 31-325 *Marketing Practices of Portfolio Managers*. Even an eye-catching "hook" in a public advertisement must comply with regulatory requirements. CRR indicates in the Report that it is not reasonable for firms to rely upon the "small print" at the bottom of an advertisement as a way to cure a potentially misleading marketing statement, particularly when the small print would only be seen briefly, partially, or if the person is directed to the firm's website for essential clarification.

We would be happy to review your marketing materials for compliance with securities law and CRR Staff guidance.

7. **Cybersecurity**: Cybersecurity is a current priority for the CSA. The CSA is currently reviewing the findings from a CSA-wide survey and has committed to provide registered firms with guidance about cybersecurity and social media practices in the upcoming fiscal year.
8. **Dealer deficiencies:** CRR Staff continues to find that dealers have inadequate books and records to demonstrate that they have conducted their own product due diligence. Further, CRR Staff has identified a number of individuals who act on behalf of a dealer and trade in securities without being registered to do so. EMDs must have processes in place to document KYP and monitor individuals sponsored by the firm. CRR Staff also found

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detailed expense allocation policy is an important component of your compliance system and can help prevent and detect instances of overcharging. If you would like to learn more about how we can assist you with developing a robust expense allocation policy tailored to your business, please contact us.

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Cryptocurrency: Where do we go from here?

On August 24, 2017, the Canadian Securities Administrators (CSA) published for comment CSA Staff Notice 46-307 *Cryptocurrency Offerings* (the "**Notice**"). The Notice provides guidance on initial coin offerings, initial token offerings and sales of securities of cryptocurrency investment funds.

The CSA's central theme in this Notice is that market participants must undertake an analysis whether their cryptocurrency offerings involve a sale of securities and when it does, the various registration and prospectus obligations applicable. The Notice also sets out certain items that market participants may want to disclose in their offering documents, such as how the coins/tokens will be valued on an ongoing basis and the ecosystem on which the coin/token operates.

Finally, the CSA focuses on investment funds that are set up to invest in cryptocurrencies. The CSA encourages market participants to consider and that registrants were not appropriately using prospectus exemptions. CRR Staff intends to provide additional guidance to assist registrants in their understanding and application of newer prospectus exemptions.

9. **Online Advisers:** As a result of compliance reviews of online (robo) advisers, CRR Staff identified deficiencies that are common among traditional portfolio managers and deficiencies unique to online advisers, such as inadequate written policies and procedures manuals, inadequate client statements, incorrect calculation of excess working capital, unsubstantiated marketing claims, and inadequate ratio of ARs to clients.

Common online adviser deficiencies included inadequate online KYC questionnaires, inadequate evidence to support that a system-recommended model portfolio was reviewed and approved for suitability by an AR and inadequate KYC update processes. Staff also found that some online advisers who did not have a comprehensive KYC questionnaire and/or software mechanisms as described in CSA Staff Notice 31-342 *Guidance for Portfolio Managers Regarding Online Advice*, did not always contact clients or prospective clients to have a meaningful discussion with them. Yet other online advisers did not maintain evidence to support that an AR had, in fact, a meaningful discussion with clients or prospective clients.

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conduct due diligence on cryptocurrency exchanges that will be used and to be mindful of certain valuation considerations and custody arrangements unique to cryptocurrencies.

We have conducted various analyses in this space; please reach out for any cryptocurrency initiative that your firm may be considering.

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We have worked with online advisers in developing appropriate KYC processes for their business model and would be pleased to work with you to tailor KYC policies and procedures for the online adviser space.

10. **Conflicts identified among certain advisers affiliated with IIROC member firms:** CRR Staff conducted a sweep of PM firms who are affiliated with an IIROC member firm and identified conflict of interest concerns, including those with respect to selecting brokers for executing trades on behalf of their managed account clients (including investment funds). CRR Staff found significant concerns with the practice of some PMs placing the majority of their managed account clients' trades with their affiliated dealers. The Report highlights the importance of establishing procedures and responding to conflicts of interest in a manner commensurate with a registrant's obligations to its clients.

11. **Common deficiencies for investment fund managers:** CRR Staff highlighted some common deficiencies among IFMs, including inadequate oversight of outsourced functions and service providers, inappropriate mutual fund sponsored conferences, inadequate insurance coverage and inappropriate use of trust accounts. Particularly, the Report noted instances of IFMs that were not complying with the requirement to hold fund assets separately from firm assets, and the requirement that fund assets be in designated trust accounts. Further, some IFMs did not maintain adequate records of supervision over client assets held in trust accounts. The Report provides some best
practices and highlights unacceptable practices.

12. **Disclosure of Outside Business Activity**: The OSC has previously issued guidance on the requirement for timely disclosure and consideration of conflicts with respect to OBAs. In the past year, CRR Staff have observed a number of instances where registrants and applicants for registration have failed to disclose, or were late in disclosing, positions of influence with religious and community organizations. Staff may recommend that "restricted client" terms and conditions be imposed on registrants conducting outside business activities that potentially pose a conflict of interest with their registerable activity.

We would be pleased to speak with you with respect to your (past or present) OBA reporting obligations.

4. AMF Summary of Oversight and Regulatory Activities: The First of its Kind in Québec

This Summary is part of the 2017-2020 Strategic Plan of the Autorité des marchés financiers (**AMF**) to assist corporate issuers in Québec better understand AMF's expectations with respect to various corporate and financial disclosure requirements. The Summary also highlights AMF's recent regulatory innovations.

First, the Summary provides a statistical overview of corporate issuers in Québec and their distributions in the public and exempt markets. It also sets out various findings regarding issuers' compliance with disclosure requirements.

Second, the Summary discusses deficiencies encountered over recent years in AMF's review of annual reports of issuers including MD&A, press releases, prospectuses and marketing material. The Report illustrates examples of non-compliant vs. compliant disclosure, supported by advice and AMF guidance.

Third, the Summary sets out AMF's issue-oriented reviews that it intends to pursue in 2017-2018, including disclosure of risks related to climate change, the impact of new IFRS rules, compliance with guidance on non-GAAP financial information, and the representation of women on boards and executive positions. The Summary also highlights AMF's focus on new legislation aimed at more transparency in the mining, and oil and gas industries in Québec, intended to detect and discourage corruption and to foster social acceptability of projects in these areas. The AMF wants corporate issuers to be aware that it tracks corporate transactions in real-time to check consistency over time of a company's disclosure documents. The AMF will also focus on certain issues that it will focus on regarding exemptive relief applications and new requirements for exempt distributions.

With this Summary, the AMF also offers a convenient table of its regulatory initiatives on financing and continuous disclosure obligations of companies.

Please contact us if you wish to discuss any matter of interest to you discussed in the AMF's Summary.

5. Mandatory Reporting To Come, But Not Here Yet!

On September 2, 2017, the Government of Canada published proposed new regulations ("**Regulations**") in the Canada Gazette, which provides an update and sets out details regarding the mandatory data breach reporting requirements ("**Data Breach Reporting Requirements**") under the *Personal Information Protection and Electronic Documents Act* ("**PIPEDA**").

On June 18, 2015, the Digital Privacy Act (also known as Bill S-4) amended PIPEDA in a number of areas. One of the key changes was the establishment of mandatory data breach reporting requirements. The Data Breach Reporting Requirements were passed in June, 2015 but are not yet in force.

With the implementation of Division 1.1 of PIPEDA, organizations that experience a data breach will have certain obligations including:

- the organization must determine if the breach poses a "real risk of significant harm" to any individual whose information was involved in the breach by conducting a risk assessment;
- if the organization considers that a breach is posing a real risk of significant harm, it must notify affected individuals and report to the Privacy Commissioner of Canada (the "**Commissioner**") as soon as feasible;
- the organization must notify any other organization that may be able to mitigate the harm to affected individuals; and
- the organization must maintain a record of any data breach that it becomes aware of and provide it to the Commissioner upon request.

The proposed Regulations list the categories of information that must be contained in a notification to affected individuals. This approach is intended to provide some certainty to organizations as to what is required, at minimum, to comply with the statutory requirements for notification. At the same time, it provides flexibility on the format, design and means of notification. This allows organizations to conduct notifications in line with established practices and expectations of their stakeholders. The proposed Regulations also identify certain commonly used forms of communication as appropriate means of direct notification to individuals.

Further, the proposed Regulations list the categories of information that must be contained in a report to the Commissioner and affirm that the purpose of data breach record-keeping is to facilitate oversight by the Commissioner and to ensure compliance with requirements, which may encourage better data security practices by organizations.

To this end, the Regulations will require organizations to maintain sufficient information in a data breach record to demonstrate that they are tracking data security incidents that result in a breach of personal information, and require that organizations hold data breach records for a minimum period of time, specifically 24 months. This allows the Commissioner to request and review the history of breaches experienced by a particular organization within a two-year window.

Stay tuned regarding the Data Breach Reporting Requirements coming into force.

6. Cryptocurrency: A 'Snap' on Developments

Cryptocurrency and the ways it can be used as a tool for investment has become a prevalent topic. In an effort to keep you apprised on how Canadian regulators have been adapting to this new investment tool, we thought it would be helpful to provide a high level summary of some of the regulatory developments that have occurred over the summer in this area. If you are looking for more detail regarding any items below, please feel free to contact us.

Regulatory Guidance Released Regarding Cryptocurrency:

In August, Staff of the Canadian Securities Administrators released guidance setting out that cryptocurrencies will often meet the definition of "securities" under Canadian securities laws, and where it does, registration and prospectus obligations may apply. We discuss this guidance in more detail in our *In Brief* article**,** *Cryptocurrency: Where do we go from here?*

impak Finance Launches the First, Regulator Approved, Canadian Initial Coin Offering:

In August, impak Finance obtained exemptive relief from both Québec and Ontario regulators to launch an initial coin offering by way of private placement under the offering memorandum exemption. Certain aspects of the exemptive relief included that impak Finance: (i) deliver an offering memorandum to each investor; (ii) does not have to register as an exempt market dealer but must still conduct know-your-client procedures for each investor; (iii) could sell to the general public as long as the investment amount was limited to $2,500; and (iv) must establish an independent governance body to set the conversion rate of the cryptocurrency into Canadian dollars.

First Block Capital Inc. becomes the First Registered Cryptocurrency Investment Fund Manager in Canada:

First Block Capital Inc. launched FBC Bitcoin Trust, an investment fund managed by First Block that invests exclusively in bitcoin. First Block was granted registration as an investment fund manager by the British Columbia Securities Commission and was the first to obtain registration with a disclosed intention to manage cryptocurrency funds.

First Block's registration includes certain terms such as it must notify the regulators each time they establish a new cryptocurrency investment fund, change investment objectives or change or add the type of cryptocurrency a fund invests in, that each investment fund has a custodian, and that First Block provide certain additional reporting to regulators including an annual independent auditor report and a quarterly report.

The developments set out above signal that Canadian regulators are willing to work with market participants to develop cryptocurrency initiatives. It is also evident that there is an expectation from market participants that cryptocurrency initiatives fit within existing Canadian securities law as opposed to being exempt from them.

7. When it Rains, it Pours: Here are a Set of New Obligations for Registrants

On July 27, 2017, the Canadian Securities Administrators ("**CSA**") adopted amendments (the "**Amendments**") to National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* ("**NI 31-103**") as well as the companion policy to NI 31-103 (the "**CP**"). According to the CSA, the Amendments are intended to promote stronger investor protection, clarify certain regulatory requirements and enhance certain market efficiencies. The Amendments come into force December 4th, 2017 with the exception of the custody amendments which come into force June 4, 2018.

We are highlighting below amendments clarifying the activities that may be conducted by exempt market dealers (the "**EMD Amendments**") and the amendments enhancing the custody requirements applicable to registered firms (the "**Custody Amendments**").

EMD Amendments

The EMD Amendments are intended to clarify that an exempt market dealer ("**EMD**") can only act as a dealer or an underwriter in the "exempt market" (i.e., where the distribution is made in reliance on a prospectus exemption). An EMD may not act as a dealer or underwriter in a distribution that is being made under a prospectus even if the investor would otherwise qualify for a prospectus exemption. An EMD can however participate in a private placement of securities of a reporting issuer. The CP has also been updated to provide further guidance on the activities that can be conducted by EMDs, including when an EMD can participate in a resale of securities.

In addition, the exemption from the dealer registration requirement that is often relied on by portfolio managers who issue securities of investment funds they manage to clients for which the firm has managed accounts, has been expanded. This exemption will now be available to portfolio managers if the investment funds are managed by the adviser or an affiliate of the adviser. Firms relying on this exemption should be aware that they are required to provide written notice of their reliance on this exemption to the regulators.

Custody Amendments

The Custody Amendments introduce new requirements for registered firms pertaining to custody arrangements. The Custody Amendments generally apply to registered firms that (a) hold or have access to cash or securities of clients of the firm or investment funds managed by the firm; or (b) direct or arrange which custodian will hold the cash or securities of such clients and/or investment funds.

The Custody Amendments do not apply to IIROC or MFDA member firms or to investment funds subject to National Instrument 81-102 -*Investment Funds* ("**NI 81-102**") as these entities are subject to their own specific custodian requirements. However, for other registered firms, the Custody Amendments impose obligations with respect to the entities that are permitted to act as custodian of client and investment fund assets, the due diligence expected to be conducted on custodians and the disclosure of custody arrangements. Each of these items are summarized briefly below.

Qualified Custodian

With some exceptions, the Custody Amendments require registered firms to appoint a "Canadian Custodian" or a "Foreign Custodian" to hold the cash or securities of clients and investment funds they manage. A "Canadian Custodian" generally includes banks listed in Schedule I, II or III of the *Bank Act* (Canada), Canadian trust companies that meet certain capital requirements, and IIROC firms that are permitted under IIROC rules to hold the cash and securities of a client or investment fund. A registered firm can appoint a "Foreign Custodian" only if using the Foreign Custodian is more beneficial to the client or investment fund than using a Canadian Custodian.

The Custody Amendments permit cash of clients or investment funds to be held at a Canadian financial institution (that may not otherwise be a "Canadian Custodian") and specify how cash and securities are to be held by the applicable custodian and by the firm (in the limited instances where a firm can self-custody).

Due Diligence

Further, in addition to exercising due skill, care and diligence in the selection and appointment of custodians, fund managers are expected to conduct a periodic review of their custodial arrangements for their funds, and to have a written custodial agreement in place.

Disclosure

The Custody Amendments expand the relationship disclosure obligations of registered firms to include disclosure to clients about where and how client assets are held and accessed, including any related risks and benefits. A registered firm that has access to client assets must provide disclosure regarding the manner in which it has access to the assets and the risks and benefits to the client arising from having such access.

The Custody Amendments are intended to codify existing custodial best practices. Accordingly, for a majority of registered firms, no major changes to existing custodial arrangements may be required. However, registrants should take the time to review their existing custodial arrangements as well as the updated guidance in the CP. We would be happy to assist you with ensuring that your policies, procedures and documentation reflect CSA's expectations for oversight of custodial arrangements and client disclosure obligations.

8. Pooled Fund-On-Fund Relief: An Update

In our June 2017 Bulletin, we reported on new conditions imposed by the Ontario Securities Committee (the "**OSC**") in recent fund-on-fund relief from the prohibited investment provisions applicable to investment funds in s.111 of the *Securities Act* (Ontario) (the "**OSA**") granted by the OSC ("**Fund-of-Fund Relief**"). Fund-of-fund relief is obtained from the OSC in relation to provisions that prohibit certain investments by investment funds, including the prohibition against an investment fund owning 20% or more of another investment fund.

One of those "new" conditions was that "a Top Fund will not invest in an Underlying Fund, unless the Underlying Fund complies with the provisions of National Instrument 81-106 – Investment Fund Continuous Disclosure ("NI 81-106") that apply to a "mutual fund in Ontario" as defined in the OSA". The OSC in the recent July 2017 Investment Fund Practitioner confirmed this new condition and clarified that the effect of the condition included in the Fund-of-Fund Relief is that when a pooled fund relies on the relief to invest in an underlying pooled fund organized under the laws of a Canadian jurisdiction where NI 81-106 does not apply, the underlying pooled fund must prepare annual audited financial statements and interim financial reports and deliver them to top fund investors, upon request. In certain Canadian jurisdictions, NI 81-106 does not apply to a mutual fund that is not a reporting issuer and without the "new" condition, an underlying fund would not otherwise be required under securities regulations to prepare annual audited financial statements and interim financial reports and deliver them to its investors and/or top fund investors.

The OSC did not confirm whether such condition will be imposed where underlying pooled funds are organized outside of the laws of a Canadian jurisdiction going forward. However, the OSC did request that filers with an underlying pooled fund that is organized outside the laws of a Canadian jurisdiction consider providing submissions as to the appropriate review of financial statements and how best to provide relevant financial information to top fund unitholders.

Frequently Asked Questions

> Question: Does T+2 Apply to You?

On September 5, 2017, securities markets in Canada and the United States transitioned to a T+2 settlement cycle. In Canada, the requirement to shorten the standard settlement cycle from T+3 to T+2 for equity and long-term debt market trades (including ETF trades) was implemented through amendments to National Instrument 24-101 *Institutional Trade Matching and Settlement*. Conventional mutual funds must also settle the purchase and redemption of mutual fund securities within T+2 (instead of T+3) and the Canadian Securities Administrators have adopted amendments to National Instrument 81-102 – *Investment Funds* ("**NI 81-102**") to codify this requirement (such amendments are expected to come into force on November 14, 2017). While there is no legal requirement to transition to a T+2 settlement period for hedge funds and other pooled funds not subject to NI 81-102, these fund managers may nevertheless want to determine whether a transition to T+2 settlement makes practical sense given the liquidity of their portfolios, documentation and other circumstances.

News & Events

Toronto Regulatory & Compliance Forum

AUM Law's very own **Jason Streicher** recently presented at the annual conference of the Portfolio Management Association of Canada on the Compliance Conundrum and associated regulatory filings. AUM Law continues to have a strong presence in the industry and stay on top of regulatory changes.