## We're Not Kitten Around

February is a short month, but at AUM Law we aren't short of news. To lift your bleak, mid-winter blues, we've got a Valentine's Day kitten, plus useful information about family offices, preparing for the OSC's risk assessment questionnaire, and managing your firm's personal trading compliance program. We've also got news about developments in Canada's anti-money laundering and anti-terrorist financing regime, IOSCO's standards for liquidity risk management for investment funds, British Columbia's musings on Fintech, real estate investment programs, and updates to the OSC's grass policies for issuers with U.S.-based marijuana activities and for whistleblowing in-house counsel.

**In this bulletin:**

In Brief: CSA Revises Its Pot Policy



### 1. It's a Family Affair, or Is it? Registration Considerations for Family Offices

In tribute to Family Day this month, we think it's a good time to discuss family offices.

A family office is a private wealth management advisory firm that typically offers a total, outsourced solution to managing the investment and other financial affairs of an affluent individual or family. Broadly speaking, there are two types of family offices: single family offices, which manage the wealth of (you guessed it) a single family, and multi-family offices, which manage the wealth of multiple families and possibly other clients.

### In Brief

**CSA Revises Its Pot Policy**

Last month, we advised you to stay tuned for an update from the Canadian Securities Administrators' *Staff Notice 51-532 Issuers with U.S. Marijuana-Related* Activities. The CSA's review was triggered by the United States Attorney General's rescission in late 2017 of its forbearance approach to the enforcement of federal laws regarding marijuana.

The CSA published revised Staff Notice 51-532 (Revised Notice) on February 8. Among other things, the Revised Notice calls for prominent disclosure in offering documents (including bold, boxed text on the cover page) about the illegal nature of

A question that often arises is whether the family office and certain of its employees need to be registered with the Ontario Securities Commission. Generally, the Securities Act (Ontario) requires an individual or entity that engages in the business of "advising others" with respect to investing in, or buying or selling securities, to register as an adviser, unless a registration exemption is available.

Some family offices take the position that they do not have to register as an adviser because they are not advising "others". Rather, they are advising and making investment decisions in respect of the family office's own proprietary capital. Although this position may be tenable in some circumstances, we caution that any registration analysis is very fact-specific and must be assessed in light of the factors identified in *Companion Policy to National Instrument 31-103 – Registration Requirements, Exemptions and Ongoing Registrant Obligations*. Moreover, Canadian securities regulators have provided limited guidance on the distinction between acting for one's own account versus acting for another's account in the context of a family office. For multi-family offices in particular, it may be quite challenging to persuade regulators that the office is not in the business of advising others.

Another thing to consider is that the registration analysis may need to be revisited as the family served by the family office evolves. For example, if the family grows in size and/or one or more members relocate to other jurisdictions, new regulatory considerations may arise. AUM Law has deep experience in this field. Please contact us if we can assist you in conducting or updating a registration analysis for your family office.

***In Brief cont'd***

marijuana under U.S. federal law and the potential risks associated with the issuer's operations. It also expands the list of specific, prominent disclosures that the OSC expects issuers to make in their offering documents if they have U.S.-based marijuana-related activities or direct involvement in cultivating or distributing marijuana in the U.S. These include disclosure about the risks and uncertainties of investing in the marijuana industry.

If you plan on raising capital or investing in this industry, we would be pleased to speak with you about these issues.

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### 2. Get Ready for the RAQ

Ontario Securities Commission (OSC) staff have begun notifying chief compliance officers of registrants that they will receive a risk assessment questionnaire (RAQ) on April 18. The OSC uses the information collected from these bi-annual questionnaires as part of its risk-based supervision program.

Registrants must submit the completed questionnaire to the OSC by May 30, 2018, after their Ultimate Designated Person (UDP) has certified the contents as complete, accurate, free from any misstatements and not misleading in any respect. If you are registered with the OSC as an investment fund manager and you manage prospectus-exempt investment funds, you also will receive the Prospectus-Exempt Fund Form, which you must complete and submit by June 30, 2018. Both the questionnaire and fund form are asking for information for the period ending December 31, 2017.

We encourage registrants to start planning for this exercise now by allocating resources to gather the needed information and draft responses, as well as scheduling time with key individuals including the UDP to review and sign off on the completed questionnaire. AUM Law has had extensive experience helping firms prepare their 2014 and 2016 RAQs. If you would like us to help you complete this year's RAQ, please contact us.

### 3. Personal Trading Reviews

Under Canadian securities legislation, registered firms are expected to have personal trading policies in place. Among other things, the firm's chief compliance officer (CCO) must maintain and consistently update a restricted securities list (*i.e.*, a list of securities that employees may not trade at a given time), as well as pre-approve each separate personal trade requested by employees of the firm. Additionally, the firm's CCO must obtain and review the brokerage statements of each of the firm's employees every month to verify that employees have only made pre-approved trades or trades that fall outside the scope of the firm's policy. In the course of a regulatory audit, the Ontario Securities Commission (OSC) and other Canadian securities regulators typically test a firm's compliance with its personal trading policies and the adequacy of the records it keeps in this regard.

Ensuring that employees are adhering to your firm's personal trading policy requires staffing, can be time-consuming, and often raises concerns among employees about confidentiality when employee account

statements are reviewed internally. To ease the burden of this exercise, AUM Law can conduct personal trading reviews for you.

### 4. CSA Revises Its Guidance on Reporting Obligations Related to Suppression of Terrorism and Canadian Sanctions (STCS)

As we reported in November 2017, two new Canadian federal sanctions provisions were adopted that impose monthly reporting obligations on securities firms. On February 22, 2018, the Canadian Securities Administrators (CSA) published *Staff Notice 31-352 Monthly Suppression of Terrorism and Canadian Sanctions Reporting Obligations* (Notice 31-352), a revised monthly reporting form, and a companion guidance document (STCS Guide). Together, Notice 31-352 and the STCS Guide:

- provide a general overview of Canada's regulatory measures against terrorist financing and against financial dealings with certain sanctioned individuals; and
- outline the current regulatory requirements (including compliance and reporting obligations) that flow from this regime and apply to registrants, exempt dealers and exempt advisers.

Notice 31-352 states that although CSA staff will strive to ensure the STCS Guide is current and includes all federal provisions requiring monthly STCS reports, it is the responsibility of each registrant, exempt dealer and exempt adviser to comply with the relevant federal regulations at all times. The penalties for doing business with an individual or entity named in any of the federal lists can be severe. AUM Law can assist you with your compliance obligations in this area. Please contact us for more information.

### 5. Have Your Say on Canada's AML/ATF Regime

On February 7, the Department of Finance published the *Discussion Paper Reviewing Canada's Anti-Money Laundering and Anti-Terrorist Financing Regime*. The paper is intended to support Parliament's upcoming study of the Proceeds of Crime (Money Laundering) and Terrorist Financing Act (PCMLTFA). The PCMLTFA requires such a review every five years and the last review was completed in 2013.

The paper notes that the money laundering and terrorist financing environment has evolved substantially in the past five years. For example, on the technology front:

- Developments in virtual currencies offer new ways to move value with anonymity;
- New financial technologies (Fintech) are changing how Canadians interact with the financial system;
- Digital identity recognition can facilitate the customer due diligence process; and
- Reporting entities can use technology (Regtech) to better understand and mitigate their risks and/or meet their obligations under the framework.

The paper also identifies potential regulatory gaps in the Canadian AML/ATF regime and indicates that the government is considering policy measures that improve the PCMLTFA and related regulations while striving to minimize the compliance burden and cost of measures required to detect and deter money-laundering and terrorist financing activities.

The comment period closes on April 30, 2018. AUM Law will monitor the progress of Parliament's review of this regime. Please contact your usual lawyer at AUM Law if you wish to discuss the proposed measures in more detail.

### 6. OSC Getting Real About Real Estate

The Ontario Securities Commission's Investor Office recently published "Investing in Real Estate". The article notes that low interest rates have increased the popularity of real estate investing as people have looked for higher rates of return than they may be able to achieve through conventional instruments such as stocks and bonds.

The article also describes different ways of investing in real estate. One approach is to invest in a mortgage investment entity (MIE), also known as a mortgage investment corporation, or MIC. MIEs pool money from investors to lend to people who may not be able to obtain a mortgage from traditional lenders like banks or

credit unions. The loans form the MIE's portfolio and can include residential mortgages, commercial mortgages and land mortgages. Investors purchase a security issued by the MIE, typically in the form of shares, limited partnership units, or trust units. These securities derive their value from the value of the underlying pool of mortgages. The OSC article stresses some of the risks that might be involved when investing in MIEs including the lack of liquidity, security and the lack of guarantees, high risk loans, declines in investment value, and the low priority of some loans.

The OSC's publication of this article suggests that real estate investments are an area of investor protection concern for the regulator. For anyone considering creating a MIE, there are a number of regulatory, corporate and securities law questions that must be considered. These were discussed in AUM's February 2016 article Mortgage Investment Corporations in a Nutshell. AUM Law can assist businesses wishing to create a MIE and can assist existing MIEs with their regulatory, corporate, and securities law questions.

### 7. OSC Seeks to Clarify How Whistleblower Policy Applies to In-House Counsel

The Ontario Securities Commission ("OSC") released for comment on January 18, 2018 proposed revisions to its *OSC Policy 15-601 Whistleblower Program* (the "Policy") to clarify the OSC's position on how the Policy applies to in-house counsel.

Currently, the Policy indicates that in-house counsel are ineligible for a monetary whistleblower award for reporting misconduct to the OSC in situations where counsel learned of the applicable information while acting in a legal capacity for the employer at issue. However, there are exceptions to that ineligibility, for example, where, in-house counsel has reasonable basis to believe that:

- disclosure is necessary to prevent a substantial injury to the financial interest or property of the entity or investors, or
- the subject of the submission is engaging in conduct that will impede an investigation.

Since the Policy was issued in 2016, some people have expressed concern that the Policy's wording permits in-house counsel to receive whistleblower awards in circumstances where disclosure of information would contravene the lawyer's obligations to keep information confidential and maintain solicitor-client privilege. The OSC has stated that it was never the intention of the Policy to encourage or allow lawyers to forego these duties. Nevertheless, the OSC has decided to clarify the Policy.

The proposed changes are intended to make it clear that in-house counsel who receive information while acting in a legal capacity, and then report such information under the Policy in breach of their applicable local bar or law society rules, won't be eligible for the monetary award.

As the OSC emphasizes in its Request for Comment, this change only applies to in-house counsel who received the relevant information while "acting in a legal capacity". Therefore, lawyers should consider in what capacity they were acting for their company when they learned of the information. If they were fulfilling a non-legal role, it is possible that they would be eligible for the whistleblower monetary award upon disclosure and use of the information as provided in the Policy, since such disclosure would not breach solicitor-client privilege rules if the solicitor-client relationship did not exist in the circumstances. However, it often unclear in what capacity a lawyer is acting at any given time while in the role of in-house counsel, and so care should still be taken.

The comment period closes on March 20, 2018. If you wish to discuss the Request for Comment or the OSC's Whistleblower Program in general, please reach out to your usual lawyer at AUM Law.

### 8. Fintech Regulation: A Myriad of Things

On February 14, the British Columbia Securities Commission published Notice 2018/01 *Consulting on the Securities Law Framework for Fintech Regulation* (the Notice). Although the Notice invites comment on British Columbia's capital market structure and its Fintech industry, the issues have wider relevance to Canadian capital markets as a whole.

The BCSC is seeking input on a wide range of issues including the following:

- Models for initial coin offerings (ICOs) and potential factors to consider in deciding whether an ICO is a distribution of securities subject to securities regulation;

- Factors to consider in deciding whether or not a virtual currency is an investment contract subject to securities regulation.
- Whether the regulatory framework for start-up crowdfunding should be relaxed (*e.g.*, by increasing the limits on the amount of capital that can be raised under the exemption);
- The impact of initial coin offerings (ICOs) on crowdfunding;
- The risks that online advisers face in relying on third parties to conduct certain Know-Your-Client (KYC) responsibilities and how these risks might be managed; and
- Regulatory concerns for firms that manage cryptocurrency funds (such as the potential for arbitrage due to less government oversight, price volatility around trading cryptocurrencies, custodial challenges when dealing with cryptocurrencies, and security and anti-money laundering risks).

The BCSC also is soliciting feedback on broader issues regarding future state of the Fintech industry and the regulation related to it, and in particular how to facilitate innovation and identify new technologies and their impact in the securities markets.

We look forward to seeing stakeholder input on all these pertinent issues raised and will continue to monitor developments in Canadian capital markets. If you think your business may intersect with these themes and wish to discuss the Notice in more detail, please reach out to your usual lawyer at AUM Law.

### 9. IOSCO Updates Its Recommendations for Liquidity Risk Management by Investment Funds

Since the financial crisis, policymakers, the asset management industry and various observers have paid considerable attention to liquidity risk management. In January 2017, the Financial Stability Board (FSB) asked the International Organization of Securities Commissions (IOSCO) to review its existing guidance (published in 2013) to address the potential liquidity mismatch between fund investments and the terms and conditions for redemptions of open-ended collective investment schemes (CIS). Responding to that request, IOSCO conducted a review of regulatory standards among its members, a study of industry practices and held a public consultation in 2017 on potential enhancements to its policy recommendations.

On February 1, 2018, IOSCO published its final report, *Recommendations for Liquidity Risk Management for Collective Investment Schemes* (2018 Report). The 2018 Report, which focuses on open-ended CIS, re-affirms IOSCO's prior guidance and includes new recommendations on:

- Consideration of underlying liquidity throughout the entire lifecycle of the fund (design, pre-launch, launch and ongoing operations);
- Alignment between asset portfolio and redemption terms;
- Availability and effectiveness of liquidity risk management tools;
- Fund level stress testing;
- Disclosure to investors; and
- Contingency planning.

The 2018 Report also includes examples of what IOSCO considers to be best practice, descriptions of regulatory approaches in a wide range of developed and emerging markets, and extensive references to related policy studies. This information may be of interest to chief compliance officers and ultimate designated persons.

Although IOSCO's standards do not have the force of law, IOSCO "expects securities regulators to ensure the effective implementation of the recommendations and promote their application by responsible entities." Accordingly, we can expect Canadian securities regulators to take action, at the policy and/or supervisory levels, if they conclude that the IOSCO standards exceed Canadian standards in any significant way.

AUM Law will monitor and report on further developments in this area.

## News & Events

### HFM Canada Operational Leaders' Summit

AUM Law's very own Chris von Boetticher moderated a panel at the recent HFM Canada Operational Leaders' Summit on February 12, 2018. Chris led the European Regulatory Masterclass, which focused on topics such as the potential impact of the European MiFID II and Global Data Protection Regulation (GDPR) on Canadian firms. AUM Law continues to have a strong presence in the industry and stays on top of regulatory changes.

### AUM Law Contributes to Lexis Practice Advisor® Canada

As leading Canadian practitioners in the area of securities law for the asset management industry, AUM Law is proud to contribute to Lexis Practice Advisor® Canada's Investment Funds and Registration topics in its Securities Module. Lexis Practice Advisor® Canada is a practical, online resource designed to assist legal professionals with an exclusive range of content including practice notes, precedents, checklists, flow charts and "how-to" guides for moving matters forward.