

ANNEX A

SUMMARY OF COMMENTS AND RESPONSES TO THE PROPOSED AMENDMENTS TO

NATIONAL INSTRUMENT 31-103 *REGISTRATION REQUIREMENTS, EXEMPTIONS AND ONGOING REGISTRANT OBLIGATIONS*

AND

COMPANION POLICY 31-103CP *REGISTRATION REQUIREMENTS, EXEMPTIONS AND ONGOING REGISTRANT OBLIGATIONS*

Introduction

The Canadian Securities Administrators (the CSA) received 24 comment letters on the proposed amendments to National Instrument 31-103 - *Registration Requirements, Exemptions and Ongoing Registrant Obligations* (NI 31-103) and Companion Policy 31-103CP *Registration Requirements, Exemptions and Ongoing Registrant Obligations* (NI 31-103 CP). The amendments relate to the registration requirement for international investment fund managers without a head office in Canada and domestic investment fund managers with a head office in one jurisdiction of Canada who also carry out investment fund manager activities in another jurisdiction of Canada (non-resident investment fund managers). The amendments were published for comment on October 15, 2010 (the October 2010 Proposal). This appendix consolidates and summarizes the material comments and our responses by theme.

Comments outside the scope of the October 2010 Proposal

We have not provided responses to the comments we received that are fact specific or outside the scope of the October 2010 Proposal, including:

- registration fees
- national regulator
- redundancy of the investment fund manager registration requirement
- revisiting the definition of permitted client in section 1.1 of NI 31-103
- exemptions for federally regulated financial institutions in CSA jurisdictions other than Ontario

1. Registration Requirement

Jurisdictional authority

Many commenters suggested that based on the legislative provisions, an entity is only required to register in those jurisdictions where it carries out some investment fund manager activities.

In addition, some commenters did not agree that the ownership of securities of an investment fund, by a resident in a jurisdiction should require investment fund manager registration, as this is not consistent with the statutory formulation of the investment fund manager registration requirement.

A number of commenters suggested that the CSA's proposed interpretation of the investment fund manager registration requirement was too broad and that the CSA should adopt a more narrow interpretation.

Some commenters are of the view that the October 2010 Proposal expands the meaning of "acting as an investment fund manager" by mixing in concepts related to distribution of and trading in securities, which they consider inappropriate given that distribution and trading are concepts that apply to dealers and not to the functions of an investment fund manager.

We agree that there has to be activity in the jurisdiction to establish a sufficient connection between the entity and the jurisdiction to require registration as an investment fund manager. Further, the activity has to relate to the functions of an investment fund manager. Accordingly, we have revised our interpretation of the investment fund manager registration requirement. Under our revised interpretation, an entity is required to register if it carries on the activities of an investment fund manager in a jurisdiction and the presence of security holders and the solicitation of investors no longer automatically requires an entity to register as an investment fund manager.

Active solicitation

Some commenters were of the view that the requirement to register as an investment fund manager should not be based on whether or not an investment fund manager or the investment fund actively solicited the purchase of the fund's securities in a jurisdiction because:

- the "active solicitation" test relates to the distribution of securities, not to "acting as an investment fund manager"
- marketing activities, including solicitation do not constitute directing the business, operations or affairs of an investment fund
- if an investment fund manager is actively soliciting in a jurisdiction it will be required to register as a dealer, accordingly imposing investment fund manager registration is duplicative and imposes additional unwarranted costs
- responding to unsolicited or administrative queries from current or prospective investors may be considered "active solicitation" and require registration

We agree. Accordingly, we have revised our interpretation of the registration requirement and investment fund managers are not required to register based on the presence of security holders and solicitation of investors in our jurisdictions.

Investment fund manager registration does not reduce the risks to investors

Some commenters indicated that the investment fund manager registration requirement does not reduce the risks to investors associated with investment in an investment fund that would justify the additional financial and administrative burdens.

We do not agree. We implemented the investment fund manager category of registration to address the ongoing operational risks of managing a fund. In order to be registered, an investment fund manager will be required to meet certain criteria, and once registered, will have to comply with various regulatory requirements, including capital, insurance, financial reporting and proficiency requirements. Registered investment fund managers will also be subject to ongoing obligations to establish and maintain internal controls and risk management systems. These requirements aim to ensure that the investment fund manager has adequate resources and systems in place to carry out its functions.

Some commenters were of the view that requiring an investment fund manager to register in jurisdictions in which they do not carry out investment fund manager activities does not enhance regulatory oversight or investor protection. They also noted that there is other regulatory oversight and tools, which more appropriately address risks to investors, including:

- each dealer who trades securities of a fund in a jurisdiction is required to be registered in that jurisdiction
- investment funds distributed by prospectus are subject to review of disclosure materials given to investors in a jurisdiction
- regulators can deny the use of exemptions, cease trade securities of a fund or refuse to issue a receipt for a prospectus

We agree and have accordingly revised the registration requirement so that an entity is only required to register if it carries on the activities of an investment fund manager in a jurisdiction.

Investment fund manager registration in multiple jurisdictions of Canada

Some commenters suggest that requiring an investment fund manager to register in jurisdictions in which it does not actually carry out investment fund manager activities, does not enhance regulatory oversight and investor protection. These commenters are of the view that registration in multiple jurisdictions is not without additional cost and administrative burdens, which will put additional strain on the financial and time resources of an investment fund manager.

We agree. Under our revised interpretation of the registration requirement, an entity is only required to register if it carries on the activities of an investment fund manager in a jurisdiction. This is consistent with the registration of dealers and advisers in each jurisdiction where they trade securities or act as an adviser. We note that if registration is required in multiple

jurisdictions, NI 31-103 provides harmonized regulatory requirements for investment fund managers and the passport system and passport interface provide administrative efficiencies.

Some commenters are of the view that despite the administrative efficiencies associated with the passport system, an investment fund manager should only be required to register in one jurisdiction, based on its head office location. That the requirement to register in multiple jurisdictions will result in increased regulatory filing fees and other costs without significantly adding to regulatory oversight.

We note that our revised interpretation of the registration requirement will only require an entity to register if it carries on the activities of an investment fund manager in a jurisdiction. Again, this is consistent with the registration of dealers and advisers in each jurisdiction where they trade securities or act as an adviser.

“Look through” and “flow through”

Several commenters are of the view that the requirement for an investment fund manager to register based on the residency of investors in the fund contradicts the CSA’s position that it will not “look through” an investment fund. They also noted that this approach is inconsistent with the approach taken by the CSA with respect to portfolio managers of investment funds, who are not required to register in each jurisdiction where the fund is distributed.

Some commenters are of the view that the client of an investment fund manager is the fund, consistent with that fact that the duty of care owed under securities legislation and National Instrument 81-107 *Independent Review Committee for Investment Funds* is to the investment fund and not individual security holders. They also noted that this approach is consistent with the recognition by the CSA that the adviser’s client is the fund, and the advice given does not flow through to investors in the fund. Accordingly, they do not think that the requirement to register based on whether the fund has security holders in a jurisdiction is correct.

Under our revised interpretation of the registration requirement, an entity is not required to register based merely on the presence of security holders and the solicitation of investors in a jurisdiction.

2. Exemptions from the investment fund manager registration requirement

Commenters raised numerous concerns with the international investment fund manager exemption set out in the October 2010 Proposal, including:

- the condition that total assets of all funds managed by the investment fund manager that are attributable to Canadian security holders must be less than \$50 million (the asset threshold) may:
 - make the exemption meaningless as most international investment fund managers will exceed this low limit
 - require an international investment fund manager to register as a result of market conditions or transactions in fund securities unrelated to subscriptions by Canadian investors, such as periodic redemptions by non-Canadian investors.

- result in fewer investment options for Canadian investors, as investment funds may choose to withdraw from the Canadian market
- result in investment funds forcing contractual rights of redemption on Canadian investors
- the calculations required to monitor compliance with the asset threshold are unworkable
- the asset threshold should not apply to an international investment fund manager that distributes the securities of its investment funds only to permitted clients, because these are highly sophisticated clients who have resources to perform their own due diligence and assess the ongoing services of the investment fund manager
- the exemption is inconsistent with the exemptions in NI 31-103 available to international dealers and advisers because it requires monitoring of the value of the securities beneficially owned by Canadian investors, whereas the exemptions for international dealers and advisers focus on the type of security, type of client and in the case of advisers, their revenues in Canada
- that the condition requiring an investment fund be formed or created in a foreign jurisdiction is not relevant

We agree that the exemption for international investment fund managers had numerous issues that made it unworkable. We narrowed our interpretation of the registration requirement, which in most cases makes the exemption no longer necessary. We note that an international investment fund manager is no longer required to register based on the presence of security holders and solicitation of investors in a jurisdiction. However, if they are required to register under our narrower interpretation of the registration requirement, we do not think it is appropriate that they be exempt on the basis that the fund they manage only distributes to permitted clients.

Investment fund managers regulated in their home jurisdiction

Some commenters are of the view that the CSA should tailor the regulatory framework with respect to investment fund managers that are also registered or regulated by their home jurisdiction or with their local regulator, or create a new exempt category of registration requiring mandatory disclosure.

We do not agree. Given the different regulatory approaches for investment fund regulation in foreign jurisdictions, we are not proposing that regulation in the home jurisdiction should be the basis for an exemption. Further, as we now propose a narrower investment fund manager registration requirement, an international investment fund managers will only be required to register if it carries on the activities of an investment fund manager in our jurisdictions.

3. Regulatory burden

Limited investment opportunities for Canadian investors

Several commenters are of the view that the increased regulatory burden of an international investment fund manager having to register in Canada is not justified. These commenters have suggested that the increased regulatory burden may deter the presence of international investment funds in Canada, and reduce investment choices and opportunities for Canadian investors.

We designed the investment fund manager category of registration to address risks associated with managing a fund by imposing regulatory requirements, including capital, insurance, financial reporting and proficiency, which aim to ensure that the investment fund manager has adequate resources to carry out its functions. We are of the view that where an entity carries on the activities of an investment fund manager in our jurisdictions it has an appropriate connection to our jurisdictions to require registration. However, as the requirement to register is no longer based merely on the presence of security holders and the solicitation of investors in a jurisdiction, many international investment fund managers will not need to register.

Proficiency and other registration requirements

Some commenters are of the view that international investment fund managers will not be able to satisfy the registration requirements under the October 2010 Proposal including those relating to compliance, capital, insurance, financial reporting and proficiency requirements particularly because some requirements are unique to Canada.

We do not agree. There are currently many foreign entities registered in other categories of registration that are subject to the registration requirements of NI 31-103, including the compliance, capital, insurance, financial reporting and proficiency requirements. However, we will consider applications for exemptive relief from certain registration requirements for international investment fund managers on a case-by-case basis, where appropriate. Further, as we no longer require an investment fund manager to register based merely on the presence of security holders and the solicitation of investors in a jurisdiction, many international investment fund managers will not need to register.

Financial reporting

Some commenters are of the view that complying with the financial statement reporting obligations, particularly the requirement to prepare financial statements in accordance with Canadian GAAP is burdensome for international investment fund managers.

We do not agree. Section 3.15 of National Instrument 52-107 - *Accounting Principles and Auditing Standards* recognizes acceptable accounting principles other than Canadian GAAP for foreign registrants.

4. Other comments

Notice of non-resident status

With respect to the proposed requirement that registered investment fund managers without a head office in a jurisdiction provide notice of their non-resident status to security holders of the fund they manage, commenters were of the view that this notice requirement:

- should not apply to domestic non-resident investment fund manager, given the principle of reciprocal enforcement between Canadian jurisdictions
- is only appropriate for international investment fund managers
- imposes unnecessary expense, without any commensurate benefit
- will infer that an investment fund managed by an investment fund manager resident in a jurisdiction is less risky

We are not proposing to revise NI 31-103 to require this notice. Based on our revised interpretation of the registration requirement, an investment fund manager will only need to register in a jurisdiction if it directs or manages the business, operations or affairs of an investment in that jurisdiction and accordingly, we would not expect many registered investment fund managers would be non-resident. Also, we do not think that investment fund managers have a relationship with the security holders of the funds they manage that make this notice necessary.

Outsourcing

One commenter suggests that the non-resident registration requirement, for an investment fund manager that outsources or delegates its investment fund manager activities to a service provider in a jurisdiction other than where it has a physical place of business, is not consistent with the existing NI 31-103CP guidance on outsourcing and does not provide additional protections.

We agree that the delegation of certain functions by an investment fund manager, on its own, would not require the investment fund manager to register in the jurisdiction where the service provider is located. However, the investment fund manager is responsible for these functions and must supervise the service provider. Further, if an entity delegates or outsources activities to a service provider to such a level that the service provider is directing or managing the business, operations or affairs of an investment fund in the jurisdiction, then the service provider must also register as an investment fund manager.

Competitive advantage for international investment fund managers

One commenter is of the view that entities that are not required to register as investment fund managers, particularly foreign entities, will have a competitive advantage over entities that are required to register.

The investment fund manager registration requirement does not relate to the regulation of competition; it only requires an entity to register if it is conducting investment fund manager activities within a jurisdiction.

Transition

Some commenters have expressed that it is unrealistic to require certain non-resident investment fund managers to be registered by September 28, 2011.

NI 31-103 was amended effective July 11, 2011 to extend the temporary exemption from registration, until September 28, 2012 for investment fund managers registered in the jurisdiction of Canada in which its head office is located and for international investment fund managers that do not have a head office in a jurisdiction of Canada. We plan to issue parallel orders so that investment fund managers will not need to register by September 28, 2012; they will only need to apply for registration by that date.

List of commenters

- Alternative Investment Management Association
- BlackRock, Inc.
- BNP Paribas Investment Partners Canada Ltd.
- Borden Ladner Gervais LLP
- Brandes Investment Partners & Co.
- Canadian Imperial Bank of Commerce
- Canadian Pension Plan Investment Board
- Capital International, Inc.
- Davies Ward Phillips & Vineberg LLP
- Fidelity Investments Canada ULC
- GreyStone Managed Investments Inc.
- Invesco Trimark Ltd.
- Managed Funds Association
- Marathon Asset Management LLP
- McMillan LLP
- Orbis Investment Management Limited
- Pension Investment Association of Canada
- Portfolio Management Association of Canada
- RESP Dealers Association of Canada
- Stikeman Elliott LLP
- The Canadian Advocacy Council for Canadian CFA Institute Societies
- The Investment Adviser Association
- The Investment Funds Institute of Canada
- Veronica Armstrong Law Corporation