ANNEX B

SUMMARY OF COMMENTS ON THE DECEMBER 2013 PROPOSAL AND RESPONSES

This annex summarizes the written public comments we received on the December 2013 Proposal and our responses to those comments.

This annex contains the following sections:

1. Introduction

2. Responses to comments received on the Rule and the Companion Policy

3. Responses to comments received on NI 33-109 and its forms

We received no comments on the amendments to NI 52-107 and 52-107CP.

Please refer to Annex A *Summary of changes to the Instrument* for details of the changes we made in response to comments.

1. Introduction

Drafting suggestions

We received a number of drafting suggestions and comments. While we incorporated many of these suggestions, this document does not include a summary of all the drafting changes we made.

Categories of comments and single response

In this annex, we consolidated and summarized the comments and our responses by the general theme of the comments. We have included section references for convenience.

2. Responses to comments received on the Rule, 31-103CP and forms

Personal corporations

Many commenters requested the ability to use personal corporations for their dealing representative activities. The comments are beyond the scope of the Amendments.

Definition of permitted client [section 1.1]

A commenter suggested we include a number of entities that are not currently captured in the definition but merit consideration as “permitted clients”. The comment is beyond the scope of the Amendments.

Application of the business trigger to start-ups [section 1.3 of the Companion Policy]

We received a number of comments about the application of the business trigger to start-up companies and companies that do not yet have an active business, as well as their directors, officers, employees and professional service providers. We revised the guidance as a result, but note that frequency is a factor in determining whether trading activity is for a business purpose.

Proficiency

Chief compliance officers of exempt market dealers [section 3.10]

Some commenters recommended additional proficiency requirements for chief compliance officers (CCOs) of exempt market dealers. Other commenters indicated their view that the 12 months of relevant securities experience requirement is not tailored to exempt market dealers and that, from a perspective of personnel, the requirement would constitute a barrier to entry.

In our view, the experience requirement for CCOs of exempt market dealers is consistent with the proficiency principle articulated in section 3.4 of the Rule. The CCO of a dealer firm must have the education, training and experience that a reasonable person would consider necessary to perform the activity competently, and the ability to design and implement an effective compliance system. We carefully considered the 12 months of relevant securities experience requirement in light of comments received, and concluded that it aligns with our mandate to provide protection to investors and to foster fair and efficient capital markets and confidence in the capital markets.

Some commenters requested guidance on CCOs acting for more than one exempt market dealer and lawyers acting as CCOs. The comments are beyond the scope of the Amendments.

One commenter suggested continuing education requirements and proficiency requirements for chief financial officers. The comments are beyond the scope of the Amendments.

Relevant investment management experience [sections 3.11 and 3.12]

Two commenters asked for a review of the registration categories for client relationship managers who do not carry out portfolio management activities and may work for a different business unit. The review of registration categories is beyond the scope of the Amendments.

Commenters also asked for additional guidance on career development for associate advising representatives. The Rule does not mandate the associate advising representative category as an apprenticeship category. Our understanding is that some firms register employees as associate advising representatives so they can perform a variety of tasks, not necessarily because they wish to become advising representatives. Some firms register an individual as an associate advising representative, who will work at the firm while completing proficiency requirements (for example, completing prescribed exams or gaining additional experience), which are needed to seek registration as an advising representative.

In all instances, the experience must be relevant to the registration category sought and cannot be limited to a subset of duties that the individual is permitted to engage in by the firm. Investors should be able to expect that an individual acting on behalf of the portfolio manager when providing advice or exercising discretionary authority meets the proficiency requirements for this category. Firms can implement a number of measures to ensure that their employees are qualified for registration as associate advising representatives or advising representatives, for example:

- screen and hire individuals who are qualified for the registration category (for example, when recruiting an individual, conduct due diligence on their previous securities experience)

- develop individuals internally by encouraging them to engage in a wider variety of activities under supervision (for example, research and analysis of securities)

The guidance set out in the Companion Policy aims to strike a balance by providing greater clarity while maintaining flexibility to allow us to continue to carefully assess applications for registration on a case-by-case basis.

Alternative course providers [Part 3 Division 2]

Several commenters suggested we broaden the current examination options. While the CSA recognizes that more work needs to be done to identify potential improvements to proficiency requirements for registered individuals, that work is beyond the scope of the Amendments.

One commenter proposed that relief from registration requirements be more transparent by, for example, posting a notice on the regulator's website. This would provide precedents and information about alternative experience and proficiencies that have been considered acceptable. The comment is beyond the scope of the Amendments.

Exempt market dealer activities

Participation in prospectus offerings [section 7.1]

The comments indicate that the words "whether or not a prospectus was filed in respect of the distribution" in subparagraph 7.1(2)(d)(i) and language in the Companion Policy may have been interpreted broadly by some market participants to allow exempt market dealers to be involved in prospectus offerings. As a general matter, we believe the appropriate dealer registration category for participating in prospectus offerings is the investment dealer category. We do not believe, as a matter of policy, that it makes sense to allow the exempt market dealer category to develop further into a competing platform for issuers that wish to make prospectus offerings. The CSA intends to examine further what activities an exempt market dealer should be permitted to conduct and may propose further amendments in the future. These further amendments may make a distinction between firms registered as both portfolio managers and exempt market dealers that may want to participate in prospectus offerings of investment funds, and other exempt market dealers. In the interim, we are not making any changes to subparagraph 7.1(2)(d)(i).

In response to other comments, we also revised the language in the Companion Policy to make it consistent with the wording in subsection 7.1(5) and explained that exempt market dealers must not participate in a resale of securities traded on a marketplace unless the transaction requires reliance on a further exemption from the prospectus requirement.

Acts in furtherance of trade and referrals

Registered dealers or dealing representatives may engage in acts in furtherance of a trade that are limited to referring a client trade, in a security they are not permitted to trade under their category of registration to a dealer registered in a category that permits the trade. The referring dealer may not engage in any other acts in furtherance of the trade, including making statements about the merits of the security or making recommendations or otherwise representing to the purchaser that the security is suitable for the purchaser.

We added guidance in section 13.8 of the Companion Policy to describe some activities exempt market dealers may, and may not, engage in.

Prime brokerage

A commenter requested guidance on the regulation of international prime brokerage activities. The issue of prime brokerage is beyond the scope of the Amendments. We encourage firms to refer to the guidance in section 1.3 of the Companion Policy to assess whether registration is required.

Transition

In response to comments that a transitional period was necessary to allow for changes in business models, we propose a six-month transition period before amendments to subsection 7.1(5) prohibiting exempt market dealer activity in marketplace securities become effective.

Investment fund complexes [section 7.3 of Companion Policy]

One commenter asked for clarification about the Companion Policy guidance on investment fund complexes. We confirm that simply setting up a fund as a limited partnership does not require the general partner to seek exemptive relief. Whether the general partner of a fund structured as a limited partnership is an investment fund manager is a question of fact. The trigger for investment fund manager registration is a functional one based on the activities carried out. If the general partner is actively involved in the direction of the business, operations or affairs of the fund, then registration (or relief) will be required.

To clarify instances where more than one investment fund manager may require registration within a fund group, we have revised the language in section 7.3 of the Companion Policy under the heading *Investment fund complexes or groups with more than one investment fund manager*. This is a fact-specific analysis based on the activities carried out by the various entities within the group to determine which entity (or entities) is acting as an investment fund manager.

We have also removed the factors we will consider in granting relief. Although these factors may be relevant, whether relief is appropriate will also be fact-specific.

Exemptions from the requirement to register [Part 8]

Prohibition on use of exemptions while registered [sections 8.01, 8.22.2 and 8.26.2]

Some commenters thought the prohibitions were too wide. We point out that the prohibitions only apply to exemptions in the Rule for activities the firm would be permitted to carry out under its category of registration. A mutual fund dealer, for example, could rely on the exemptions in section 8.15 and 8.21 of the Rule, because these sections provide exemptions for trades in securities a mutual fund dealer is not permitted to trade under its category of registration.

The prohibitions do not apply to exemptions provided by legislation, such as subsection 3(4) of the *Securities Act* (Québec).

The rationale for the prohibitions is to ensure that all registrable activity carried out by a registrant complies with securities law. Allowing registered firms to conduct some of their activity under an exemption could create client confusion, raise oversight issues, and may impact the firm's continued fitness for registration or its ability to manage its business risks. We agree there is less risk when the activities are in different jurisdictions from the jurisdiction in which the firm is registered. We have amended the section to prohibit reliance on an exemption in the local jurisdiction in which the firm is registered.

One commenter questioned how this applies to the ability or inability of an IIROC dealer to set up a separate exempt market dealer firm. The Amendments are not intended to impact that ability or inability.

Trades through or to a registered dealer [sections 8.5 and 8.5.1]

Some commenters felt the restriction against solicitation or direct contact was impractical, given how business is conducted. We point out that the exemption is only intended to permit acts in furtherance of a trade that do not involve soliciting or direct contact in relation to that trade. Meetings with clients that do not involve acts in furtherance of that trade and presentations about brands or strategies with no mention of specific securities may not be solicitation or direct contact in relation to that trade.

This exemption is only necessary if a person is in the business of trading. We encourage reference to section 1.3 of the Companion Policy, which sets out guidance on when a person is in the business of trading, to determine if their activities trigger the registration requirement. Depending on the circumstances, transmission, negotiation and settlement of documentation and client relations or administrative type contact may not amount to being in the business of trading.

In response to a comment, we added section 8.20.1 to mirror the exemption with respect to exchange contracts.

International dealer and international adviser [sections 8.18 and 8.26]

Commenters were generally in favour of reverting to the pre-2011 use of "permitted client" rather than the more restrictive "Canadian permitted client".

One commenter thought the existing exemption posed a risk to the Canadian securities industry if a foreign dealer failed to act in accordance with safeguards in Canadian regulation. We think the terms of the exemption are appropriate for the activity it permits.

One commenter suggested permitting dealers relying on the international dealer exemption to trade inter-listed securities. The comment is beyond the scope of the Amendments.

Short-term debt [section 8.22.1]

Commenters did not feel the restriction of the exemption to permitted clients only was warranted. Since an examination of the use of current exemption orders revealed that this type of trading generally occurs with permitted clients, we think it is an appropriate limitation.

A commenter felt a transition period would be necessary to address the practical implications of the amendments; we agree, and there will be a six-month transition period.

Sub-adviser [sections 8.26.1 and 13.17]

Commenters felt the "chaperoning" requirement was unnecessary. We agree, and have removed the requirement that was proposed in paragraphs 8.26.1(1)(c) and 13.17(2)(c).

One commenter requested guidance about the due diligence to be conducted for affiliated sub-advisers. We expect registered firms to exercise sufficient due diligence to ensure they are meeting their obligations to their clients, including their suitability obligations. The due diligence should also be sufficient to ensure a sub-adviser is meeting its obligations to exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances.

Acquisition of a registered firm's securities or assets [sections 11.9 and 11.10]

IIROC members

One commenter considered the requirements unnecessary for IIROC members. We do not agree. An IIROC member is still a registrant under securities legislation and is not exempt from the application of sections 11.9 and 11.10.

The review of acquisition notices by the regulators is based on different criteria from those of IIROC. Acquisition notices give regulators an opportunity, before transactions are completed, to address ownership issues that could affect a firm's continued fitness and suitability for registration.

Internal reorganizations

One commenter was concerned that the removal of the exceptions that were in paragraph 11.9(3)(a) and subsection 11.10(3) would require notices of internal reorganizations. The amendments are consistent with the outcome we seek, which is that only initial acquisitions of 10% tranches are subject to regulatory approval. Filing with the principal regulator only is designed to simplify the process and reduce delays.

Estate freezes and other tax-driven transactions

A commenter requested further clarification in connection with estate freezes and other tax-driven transactions whose effective date may precede the filing date. We recommend that in such cases the notice be filed as soon as possible and include a description of the effective date and all relevant information.

Acquisition of foreign registrants

Some commenters expressed concern about the requirement for notices about acquisitions of a foreign registrant. This change was made so that the regulator would have notice of acquisitions that may have an impact on the local firm's continuing fitness for registration, for example, staffing resources and compliance.

Financial condition [Part 12]

Net asset value adjustments

Some commenters suggested we add a materiality threshold for reporting net asset value adjustments. We have declined to do so even though most investment fund managers use 0.5% of the net asset value as the materiality threshold. However, we

expect investment fund managers to have a policy that clearly defines what constitutes a material error that requires an adjustment. In some cases, 0.5% may not be the appropriate threshold.

One commenter gave detailed comments about Form 31-103F4. We have revised the form where we agreed with those comments.

Exempt market dealer capital requirements

A commenter felt exempt market dealer capital requirements should be aligned with IIROC requirements. The comment is beyond the scope of the Amendments.

Form 31-103F1

A commenter suggested including money market funds from international jurisdictions other than the USA as part of working capital. We disagree with such a broad amendment and will continue to review exemption applications on a case-by-case basis.

Conflicts of interest [section 13.4 of Companion Policy]

Individuals who serve on a board of directors

Having ownership in a holding company is a business activity that requires disclosure, because it allows an individual to perform, control or indirectly influence business activity.

One commenter felt the guidance on acting as a director focused too narrowly on access to confidential information. The guidance in the Companion Policy is intended to deal specifically with a registrant's conflict of interest with respect to confidential information acquired as a director of a reporting issuer. We remind registrants that it is their responsibility to comply not only with securities laws but also with all applicable laws, including for example, corporate or tax laws.

Individuals who have outside business activities

Several commenters felt the new guidance in the Companion Policy was too broad. The disclosure of outside business activities, including positions of power or influence where the activity places the registered individual in contact with clients or potential clients, including positions where the registrant handles investments or monies of the organization, whether the registered individual receives compensation or not, is necessary to allow the firm and the regulator to conduct a meaningful assessment of an individual's fitness for registration, at the time of the application and on an ongoing basis. We require disclosure to ensure protection from unfair, improper or fraudulent practices for investors (and in particular, clients or potential clients who may be vulnerable). The disclosure is connected with the registered individual's work because the registered firm and the individual acting on its behalf are expected to (i) identify conflicts of interest that should be avoided, (ii) determine the level of risk a conflict of interest raises, and (iii) respond appropriately.

A registered firm must take reasonable steps to identify and respond to existing material conflicts of interest. We agree firms are responsible for implementing and monitoring their policies and procedures to ensure conflicts of interest are effectively managed. This includes effectively monitoring the outside activities of their registered and permitted individuals. The Amendments do not prohibit outside business activity; instead, it is up to the registered firm to determine whether there is a potential conflict of interest and whether it can be properly controlled before approving the activity (refusing approval is the last resort).

In the course of our reviews, we have identified firms that did not adequately discharge these obligations. Often, the deficiencies were associated with the firm's finding that the activity did not require disclosure. The activities were a source of potential conflict and included paid and unpaid roles with charitable, social and religious organizations where the individual was in a position of influence or in contact with clients or potential clients, or handled the investments or monies of the organization.
We encourage registered firms to implement, monitor and enforce appropriate policies and procedures to ensure compliance with securities legislation.

The CSA will continue to carefully monitor the disclosure submitted to assess both the suitability of each registered individual and the registered firm's response to existing or potential conflicts of interest.

One commenter suggested passive investments are outside the scope of outside business activity that requires reporting. We agree passive investments need not be disclosed.

3. Responses to comments received on NI 33-109, 33-109CP and forms

Business location

Comments received suggested the threshold for where records are kept was very low. The definition of "business location" is intended to capture places where a firm conducts its business. This includes where representatives interview and interact with clients, as well as where client records are kept.

If a firm lists a private residence as a business address and it uses that address to conduct its registered business, it is appropriate for the regulator to be able to attend at that residence as part of its oversight of the firm's activities.

We would not consider firm documents or records that can be accessed from a residence as a result of remote online access to be records that are "kept at the residence".

Other comments

We received other comments on NI 33-109 and its forms. The comments are beyond the scope of the Amendments.