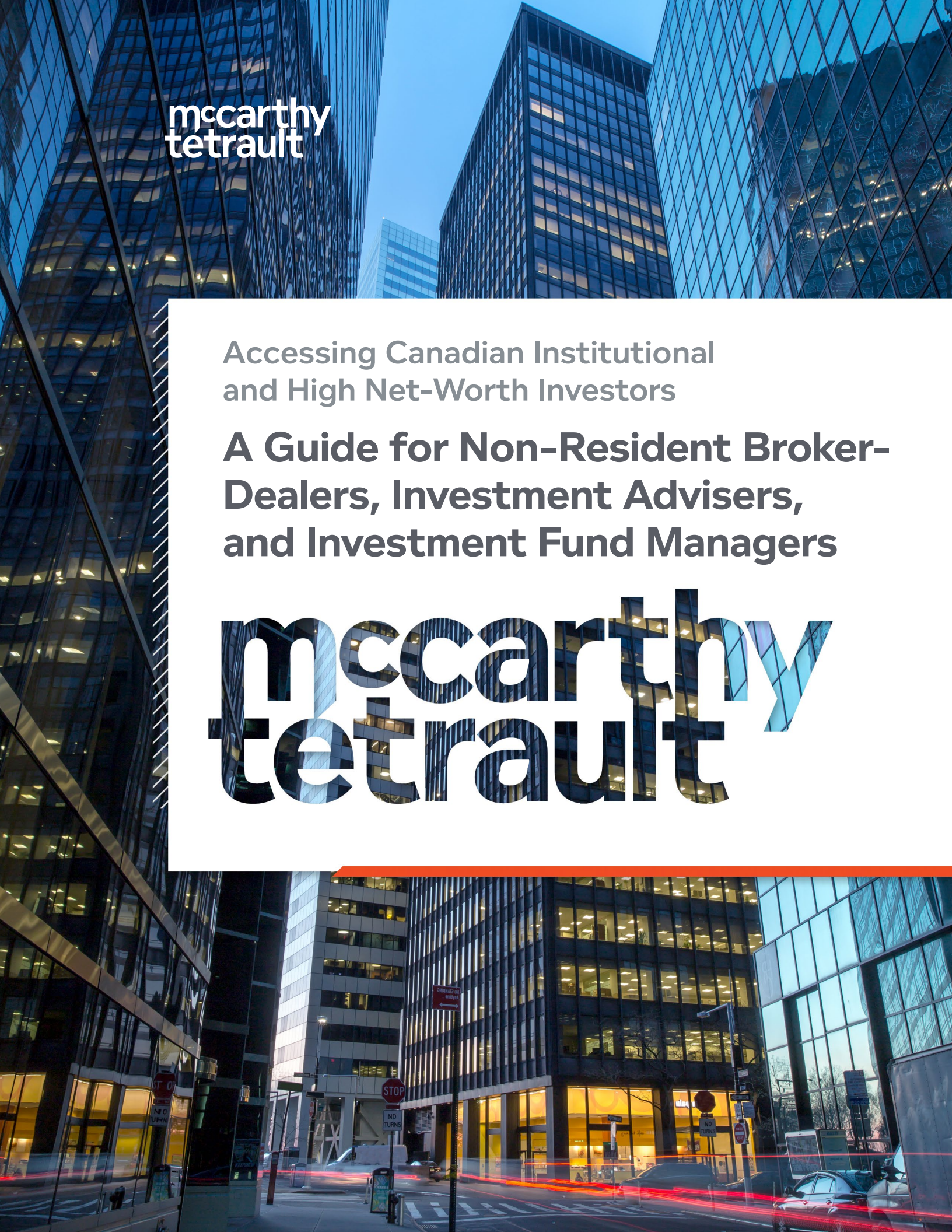

mccarthy tetrault

Accessing Canadian Institutional and High Net-Worth Investors

A Guide for Non-Resident Broker-Dealers, Investment Advisers, and Investment Fund Managers

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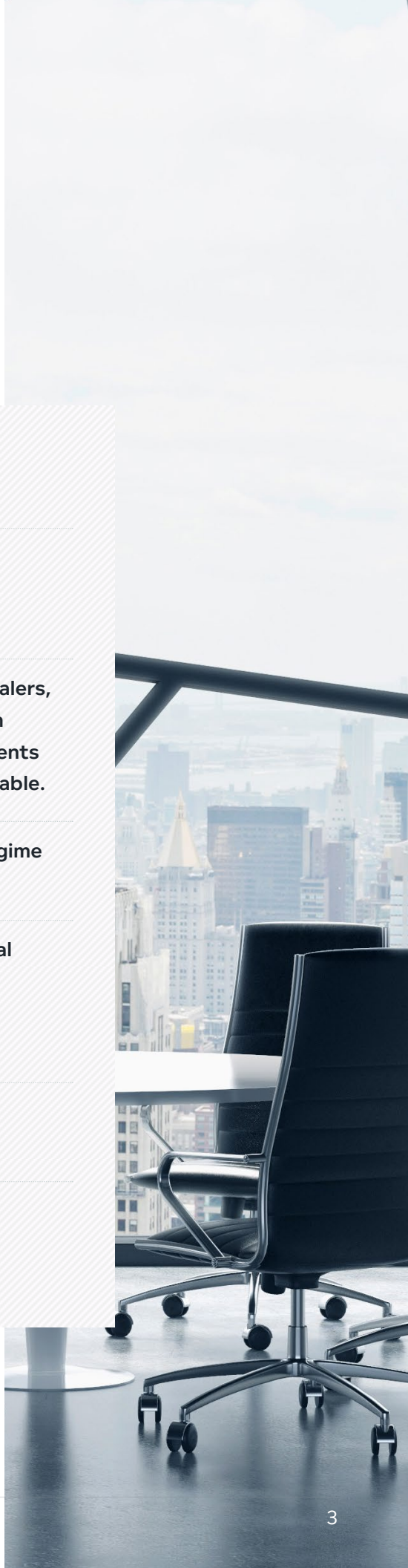
Accessing Canadian Institutional and High Net-Worth Investors

A Guide for Non-Resident Broker-Dealers, Investment Advisers, and Investment Fund Managers

Executive Summary

- Canadian securities law is provincial in origin but regulation and harmonization amongst provinces and territories makes it substantially national in scope.
- Non-resident securities businesses ("NRSB") that are broker-dealers, investment advisers or investment fund managers engaging with Canadian investors are subject to onerous registration requirements unless an exemption from such registration requirements is available.
- Canada has adopted a reasonably accommodating exemption regime for NRSBs to access institutional and high net worth investors.
- This paper outlines how NRSBs may access Canadian institutional and high net worth investors while staying in compliance with applicable securities and derivatives law, anti-money laundering law and economic sanctions law.
- Securities regulators are conducting spot audits on NRSBs to assess their compliance with the conditions of the exemptions.
- NRSBs seeking a Canadian compliance solution should read this paper and refer to the back page for a summary of our NSRB Annual Compliance Service.



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Introduction

Non-resident securities businesses ("NRSBs") are expected to comply with a myriad of securities, anti-money laundering ("AML"), terrorist financing and economic sanctions regulatory requirements. These requirements come into play when an NRSB seeks to:

- trade securities with an institutional or high-net-worth investor ("HNW") located in Canada
- provide advice in relation to securities to any such investor; or
- act as an investment fund manager of an investment fund sold to a Canadian investor.

Generally speaking, **Canada's borders are open to NRSBs seeking to access capital from institutions and HNW investors** without having to submit to the onerous Canadian registration requirements that would otherwise apply to NRSBs if the exemptions discussed herein were not available to them.

This Guide is intended to provide an overview of certain securities, anti-money laundering ("AML"), terrorist financing and economic sanctions regulatory requirements that must be considered and, if applicable, addressed by an NRSB. With securities regulators conducting random audits on NRSBs to ensure compliance with the conditions of the exemptions, the failure to comply has potentially severe consequences, such as administrative monetary penalties, reprimand and the removal of exemptions and public disclosure thereof of such consequences, which may raise regulatory reporting implications for the NRSB in its home jurisdiction.

Staying up-to-date with how to comply with Canadian securities, AML and economic sanctions laws is critical for NRSBs and McCarthy Tétrault LLP is pleased to offer an annual NRSB compliance service described at the end of this Guide to assist NRSBs in meeting these regulation requirements.

Considerations

This Guide presumes that the NRSB seeks to engage with Canadian clients without becoming registered as a broker-dealer, investment adviser or investment fund manager under Canadian securities laws.

This Guide should be used for informational purposes only for several reasons. First, it does not provide an overview of all securities, AML, terrorist financing or economic sanctions regulatory requirement that apply to NRSBs engaged in the above-described trading, advisory and investment fund management activities. Second, it does not provide an exhaustive description of the those regulatory requirements that are the subject of the overview provided. Third, this Guide does not provide any information or guidance in relation to the distinct regulatory frameworks that govern the conduct of trading, advisory and fund management activities in relation to commodity futures contracts, commodity futures options and other exchange traded or over-the-counter derivatives transactions in Canada. Any consideration of these distinct regulatory frameworks is beyond the scope of this article.

NRSBs that propose to engage in any trading, advisory or investment fund management activity in relation to securities, commodity futures contracts, commodity futures options or other exchange traded or over-the-counter derivative transactions are therefore encouraged to seek the advice of Canadian legal counsel before doing so.

All currency amounts that are referred to in this Guide are denominated in Canadian dollars.

The Canadian Securities Regulatory Framework

Jurisdictional Scope and Authority

Like the United States, Canada has a federal system of government whereby the authority to enact legislation is divided between the federal and the provincial and territorial governments. Unlike the United States, the Canadian securities markets are currently regulated solely by the provincial and territorial governments.[1] As a result, each of Canada's ten provinces and three territories has its own legislative scheme for regulating the securities market within its own provincial or territorial jurisdiction, and its own securities commission or regulatory authority (each a "Securities Regulator") for administering and enforcing such legislation. Securities regulatory requirements in Canada can therefore vary from jurisdiction to jurisdiction.

Canadian securities legislation generally regulates the trading of, and advising in respect of, securities within a province or territory by requiring those who engage in, or hold themselves out as being engaged in, the business of trading in, or advising in respect of, securities to become registered or licensed as a dealer or adviser, respectively. The legislation requires those who distribute securities to file a prospectus with, and obtain a receipt therefor from, the applicable Securities Regulator(s) unless:

a. the securities legislation provides for an express statutory exemption from the relevant requirement; or

b. an order or ruling can be obtained from the applicable Securities Regulator that exempts a trade, a security, or a person or company from the relevant requirement.

Canadian securities legislation also requires any person or company who acts as an investment fund manager in a province or territory of Canada to become registered as such with the relevant Securities Regulator unless it can act as an investment fund manager in reliance upon one of two exemptions, described below, that are available only in the provinces of Ontario, Quebec, and Newfoundland and Labrador.

For purposes of the dealer registration and prospectus requirements of Canadian securities legislation, the term "trade" is broadly defined to include any sale or disposition of a security for valuable consideration; any receipt by a registrant of an order to buy or sell a security; and any act, advertisement, solicitation, conduct, or negotiation directly or indirectly in furtherance thereof. The term "distribution" is defined, with reference to the term "trade," to include a trade in the securities of an issuer that have not been previously issued.

In an effort to harmonize Canadian securities laws, each of the thirteen Securities Regulators in Canada have, under rulemaking authority granted by the provincial and territorial governments, established numerous rules, referred to as national instruments, that operate in a substantially identical manner in each province and territory. National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* ("NI 31-103"), a national rule governing the registration of dealers, advisers and investment fund managers, is a key part of this harmonization effort.

Trading in Securities by a NRSB-Broker-Dealer

A NRSB that proposes to engage in the business of trading securities in Canada without becoming registered as a broker-dealer must rely upon one of a very limited range of dealer registration exemptions. The most relevant exemptions being the international dealer, registered dealer, and specified debt exemptions, each of which is described below.

International Dealer Exemption

A NRSB that is eligible to rely on the international dealer exemption may engage in the following trading related activities without having to become registered as a dealer in reliance upon section 8.18(2) of NI 31-103 (the "International Dealer Exemption"):

a. an activity, other than a sale of a security, that is reasonably necessary to facilitate a distribution of securities that are offered primarily in a foreign jurisdiction;

b. a trade in a debt security with a permitted client if the debt security;

- is denominated in a currency other than the Canadian dollar, or
- is, or was, originally offered primarily in a foreign jurisdiction and a prospectus has not been filed with a Securities Regulator for the distribution;

c. a trade in a debt security that is a foreign security[2] with a permitted client[3], other than during the security's distribution;

d. a trade in a foreign security with a permitted client unless the trade is made during the security's distribution under a prospectus that has been filed with a Securities Regulator;

e. a trade in a foreign security with an investment dealer; and

f. a trade in any security with an investment dealer that is acting as principal.

A NRSB is only eligible to rely upon the dealer registration exemption that is available pursuant to the International Dealer Exemption if all of the following terms and conditions apply:

a. the head office or principal place of business of the NRSB is in a foreign jurisdiction;

b. the NRSB is registered under the securities legislation of the foreign jurisdiction in which its head office or principal place of business is located in a category of registration that permits it to carry on the activities in that jurisdiction that registration as a dealer would permit it to carry on in Canada;

c. the NRSB engages in the business of a dealer in the foreign jurisdiction in which its head office or principal place of business is located;

d. the NRSB is acting as principal or as agent for the issuer of the securities, for a permitted client or for another NRSB; and

e. the NRSB has submitted to the relevant Securities Regulator(s) a completed Form 31-103F2.

In addition to the above-described terms and conditions, the International Dealer Exemption is not available to a NRSB in respect of a trade with a permitted client unless one of the following applies:

a. the permitted client is registered as a dealer or adviser under the securities legislation of a province or territory of Canada; or

b. the NRSB has provided the permitted client with notice (a "Client Notice") of the following:

- the NRSB is not registered in the relevant province or territory to make the trade;
- the foreign jurisdiction in which the head office or principal place of business of the NRSB is located;
- all, or substantially all, of the assets of the NRSB may be situated outside of Canada;
- there may be difficulty enforcing legal rights against the NRSB because of the above;
- the name and address of the agent for service of process of the NRSB in the relevant province or territory.

Registered Dealer Exemption

A second dealer registration exemption that is available to a NRSB is the registered dealer exemption that is available pursuant to section 8.5 of NI 31-103. Section 8.5 provides that the dealer registration requirement does not apply to a person or company in respect of a trade in a security if either of the following applies:

a. the trade is made through a registered dealer, if the dealer is registered in a category that permits the trade unless, in furtherance of the trade, the person or company solicits or contacts directly any purchaser or prospective purchaser in relation to the trade;

b. the trade is made to a registered dealer who is purchasing as principal, if the dealer is registered in a category that permits the trade.

The registered dealer exemption is not available to a NRSB engaged in the business of trading securities if it engages in any trading activity in Canada for which it is either not registered, or exempt from registration, as a dealer if it then directs the execution of that trade through a registered dealer. Such trading activity could involve directly contacting persons resident in a province or territory to solicit or market a purchase or sale of securities. Accordingly, if a NRSB acted in furtherance of a sale of securities by soliciting potential purchasers in a province and then executed the sales through a person or company registered as a dealer in the province, then the NRSB would not be able to rely on the registered dealer exemption for the purpose of conducting such sales.[4]

Specified Debt Exemption

In addition to the International Dealer Exemption and the registered dealer exemption described above, a person or company, a NRSB may engage in trading or distributing any of the following securities with or to any person or company without having to comply with the dealer registration requirement:

a. a debt security issued by or guaranteed by the Government of Canada or the government of a jurisdiction of Canada;

b. a debt security issued by or guaranteed by a government of a foreign jurisdiction if the debt security has a designated rating[5] from a designated rating organization[6] or its DRO affiliate[7]

c. a debt security issued by or guaranteed by a municipal corporation in Canada;

d. a debt security secured by or payable out of rates or taxes levied under the law of a jurisdiction of Canada on property in the jurisdiction and collectible by or through the municipality in which the property is situated;

e. a debt security issued by or guaranteed by a Canadian financial institution or a Schedule III bank, other than debt securities that are subordinate in right of payment to deposits held by the issuer or guarantor of those debt securities;

f. a debt security issued by the Comité de gestion de la taxe scolaire de l'île de Montréal;

g. a debt security issued by or guaranteed by a permitted supranational agency as defined in NI 31-103 if the debt securities are payable in the currency of Canada or the United States of America.

Trading or distributing any of the securities described above is not subject to either the dealer registration requirement or the prospectus requirement. Moreover, trading or distributing such exempt securities is also not subject to any post-trade filing requirements.

Advising in Securities by a NRSB-Investment Adviser

As described above, a NRSB that proposes to engage in the business of advising in securities in Canada without becoming registered as an adviser must rely upon one of a very limited range of adviser registration exemptions. The most relevant exemptions being: the international adviser, the international sub-adviser, and the general advice exemptions. These registration exemptions are discussed below.

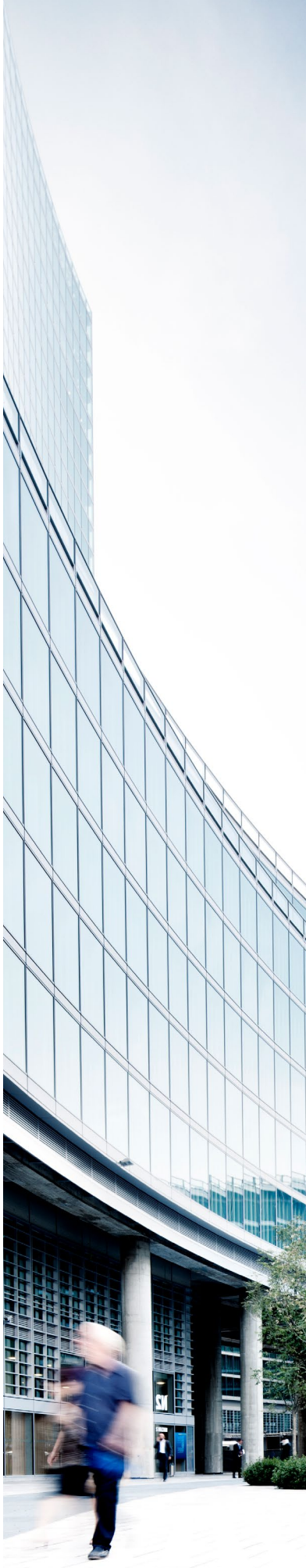
Before describing each of the above-described adviser registration requirements and exemptions, it should be noted that Ontario's look-through approach to adviser registration was abandoned effective September 28, 2009. As a result, an adviser to an investment fund that distributes its securities into Ontario is no longer required to address adviser registration requirements, and Ontario adviser registration requirements are, like all other provincial and territorial jurisdictions, generally applicable only to advisers who provide investment advice on a separately managed account basis to persons or companies, including investment funds, that are resident or otherwise located in Canada.

International Adviser Exemption

The international adviser exemption that is available pursuant to section 8.26 of NI 31-103 (the "International Adviser Exemption") is similar to the International Dealer Exemption because it permits a NRSB to act as an adviser to certain permitted clients subject to terms and conditions set out below that are similar to those described above with respect to the International Dealer Exemption provided that:

a. permitted clients[8] do not include a person or company registered as a dealer or adviser in any province or territory of Canada; and

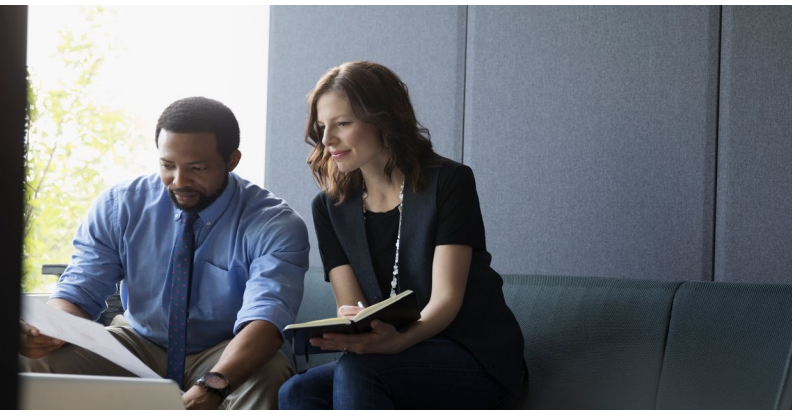
b. the NRSB does not provide advice in Canada in respect of securities of Canadian issuers except to the extent that such advice is incidental to its providing advice in respect of foreign securities.[9]



For purposes of the International Adviser Exemption, a permitted client is any person or company that is on the list of permitted clients as defined in NI 31-103 that is attached as *Schedule 1* other than registered dealers and advisers. Unlike the International Dealer Exemption, registered dealers and advisers are not considered permitted clients for purposes of the International Adviser Exemption.

A NRSB may only rely upon the International Adviser Exemption if all of the following terms and conditions apply:

- **a.** the head office or principal place of business of the NRSB is in a foreign jurisdiction;
- **b.** the NRSB is registered in a category of registration, or operates under an exemption from registration, under the securities legislation of the foreign jurisdiction in which its head office or principal place of business is located, in a category of registration that permits it to carry on the activities in that jurisdiction that registration as an adviser would permit it to carry on in the local jurisdiction;
- **c.** the NRSB engages in the business of an adviser in the foreign jurisdiction in which its head office or principal place of business is located;
- **d.** as at the end of its most recently completed financial year, not more than 10% of the aggregate consolidated gross revenue[10] of the NRSB, its affiliates and its affiliated partnerships was derived from the portfolio management activities of the person or company, its affiliates and its affiliated partnerships in Canada;
- **e.** before advising a client, the NRSB provides the client with a Client Notice; and
- **f.** the NRSB has submitted to the Securities Regulator a completed Form 31-103F2.



International Sub-Adviser Exemption

The international sub-adviser exemption that is available pursuant to section 8.26.1 of NI 31-103 (the "ISA Exemption") provides NRSBs with an exemption from the adviser registration requirement that is less onerous than the International Adviser Exemption described above. For purposes of the ISA Exemption, a sub-adviser is an adviser to either (i) a registered adviser, or (ii) a registered investment dealer that conducts its advisory activity in accordance with the IIROC dealer member rules applicable to managed accounts.

The ISA Exemption is available to any NRSB provided all of the following apply:

- **a.** the sub-adviser's head office or principal place of business is in a foreign jurisdiction;
- **b.** the sub-adviser is registered in a category of registration, or operates under an exemption from registration, under the securities legislation of the foreign jurisdiction in which its head office of principal place of business is located, that permits it to carry on the activities in that jurisdiction that registration as an adviser would permit it to carry on in the relevant Canadian jurisdiction;
- **c.** the NRSB engages in the business of an adviser in the foreign jurisdiction in which its head office or principal place of business is located;
- **d.** the obligations and duties of the NRSB are set out in a written agreement with the registered adviser or registered investment dealer;
- **e.** the registered adviser or registered investment dealer has entered into a written agreement with its clients on whose behalf investment advice is, or portfolio management services are, to be provided, agreeing to be responsible for any loss that arises out of the failure of the NRSB,
  - to exercise the powers and discharge the duties of its office honestly, in good faith and in the best interests of the registrant and each client of the registrant for whose benefit the advice is, or the portfolio management services are, to be provided, or
  - to exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances.

General Advice Exemption

In addition to the International Adviser and ISA Exemptions described above, an exemption from the adviser registration requirement is available for general or non-tailored advice the "GA Exemption") pursuant to section 8.25(2) of NI 31-103.[11] Section 8.25(2) provides that the adviser registration requirement does not apply to a NRSB that acts as an adviser if the advice the person or company provides does not purport to be tailored to the needs of the person or company receiving the advice. A NRSB that relies on the GA Exemption must comply with certain prescribed disclosure requirements if it recommends buying, selling or holding a specified security, a class of securities or the securities of a class of issuers in which certain related parties have a prescribed form of financial or other interest.

Acting As an NRSB-Investment Fund Manager – A Bifurcated Regulatory Framework

Under NI 31-103, any person or company that acts as an investment fund manager in a province or territory of Canada is required to become registered, or exempt from registration, as such with the relevant Securities Regulator(s).

Despite the harmonization objective underlying the adoption of NI 31-103 as a national instrument effective September 28, 2009, the Securities Regulators were unable to reach a consensus respecting the regulation of NRSB investment fund managers. NRSB investment fund managers must therefore contend with two distinct regulatory frameworks that now govern their activities in Canada. Multilateral Instrument 32-102 *Registration Exemptions for NRSB Investment Fund Managers* ("MI 32-102") governs the activities of NRSB investment fund managers in Ontario, Quebec and Newfoundland and Labrador (the "Instrument Jurisdictions") and Multilateral Policy 31-202 *Registration Requirement for Investment Fund Managers* ("MP 31-202") governs the activities of NRSB investment fund managers in all provinces and territories other than the Instrument Jurisdictions (the "Policy Jurisdictions").

MI 32-102—The Instrument Jurisdictions

MI 32-102 comprises the instrument itself, two forms, and a companion policy ("CP 32-102"). CP 32-102 provides guidance respecting the interpretation of MI 32-102. The interpretive guidance provided by CP 32-102 includes a description of the activities that will be considered to constitute acting as an investment fund manager for purposes of the investment fund manager registration requirement. According to CP 32-102, a person or company will be considered to be acting as an investment fund manager in an Instrument Jurisdiction if it directs or manages the business, operations, or affairs of one or more investment funds by engaging in some or all of the following activities:

- establishing a distribution channel for the fund;
- marketing the fund;
- establishing and overseeing the fund's compliance and risk management programs;
- overseeing the day-to-day administration of the fund;
- retaining and liaising with the portfolio manager, the custodian, the dealers, and other service providers of the fund;
- overseeing advisers' compliance with the investment objectives and the overall performance of the fund;
- preparing the fund's prospectus or other offering documents;
- preparing and delivering security holder reports;
- identifying, addressing, and disclosing conflicts of interest;
- calculating the net asset value of the fund; and
- calculating, confirming, and arranging payment of subscriptions and redemptions and/or dividends or other distributions.

If a NRSB is acting as an investment fund manager, it will become subject to the investment fund registration requirement of an Instrument Jurisdiction if one or more of the investment funds that it manages distributes, or has distributed, securities to residents of the Instrument Jurisdiction. If a NRSB person or company becomes subject to the investment fund manager registration requirement of an Instrument Jurisdiction, it must either apply to become registered as an investment fund manager in the Instrument Jurisdiction or rely upon one of two registration exemptions that are available pursuant to sections 3 and 4 of MI 32-102.

Section 3 of MI 32-102 provides that the investment fund manager registration requirement does not apply to a NRSB acting as an investment fund manager of one or more investment funds if the NRSB does not have a place of business in an Instrument Jurisdiction and if one or more of the following apply:

- none of the investment funds has security holders resident in the Instrument Jurisdiction; and/or
- neither the NRSB nor any of the investment funds has, at any time after September 27, 2012, actively solicited residents in the Instrument Jurisdiction to purchase securities of an investment fund.

Section 4(1) of MI 32-102 is more broadly cast than section 3 and provides for a permitted client exemption that is comparable to the International Dealer Exemption that is described above. Section 4 provides that the investment fund manager registration requirement does not apply to a NRSB if all securities of the investment funds managed by it that are distributed in an Instrument Jurisdiction are distributed in reliance upon a prospectus exemption to permitted clients only (the "International Investment Fund Manager Exemption").

For purposes of the International Investment Fund Manager Exemption, a permitted client is any person or company that is on the list of permitted clients as set out in section 1.1 of NI 31-103 other than permitted clients that are referred to in paragraphs (m) and (n) in that section. In lieu of the permitted clients referred to in paragraphs (m) and (n), a permitted client for purposes of the International Investment Fund Manager Exemption includes a registered charity under the *Income Tax Act* (Canada) that obtains advice on the securities to be traded from an eligibility adviser, as that term is defined in section 1.1 of NI 45-106 *Prospectus Exemptions*, or from an adviser registered under the securities legislation of the jurisdiction of the registered charity.

The International Investment Fund Manager Exemption contemplated by section 4(1) of MI 32-102 is not available unless all of the following apply:

- the NRSB does not have its head office or principal place of business in Canada;
- the NRSB is incorporated, formed, or created under the laws of a foreign jurisdiction;

- none of the investment funds is a reporting issuer in Canada;
- the NRSB has submitted to the relevant Securities Regulator(s) a completed Form 32-102F1 *Submission to Jurisdiction and Appointment of Agent for Service for International Investment Fund Managers;*
- the NRSB has provided each of its permitted clients with notice in writing of the following:
  - the investment fund manager is not registered in the relevant Instrument Jurisdiction to act as an NRSB;
  - the foreign jurisdiction in which the head office or principal place of business of the NRSB is located;
  - all or substantially all of the assets of the NRSB may be situated outside of Canada;
  - there may be difficulty enforcing legal rights against the NRSB as a result of the foregoing; and
  - the name and address of the agent for service of process of the NRSB in the relevant Instrument Jurisdiction(s).

Within ten days of the date on which a NRSB first relies on the International Investment Fund Manager Exemption in an Instrument Jurisdiction, the NRSB must file a completed Form 32-102F2 *Notice of Regulatory Action* with the Securities Regulator of the Instrument Jurisdiction. If there is any change to the information previously provided on a Form 32-102F2, notice of the change must be provided to the Securities Regulator within ten days of the change.

MP 31-202—The Policy Jurisdictions

Unlike MI 32-102, MP 31-202 adopts a principles-based approach to the regulation of investment fund managers that places primary emphasis on actually acting as an investment fund manager within a Policy Jurisdiction rather than having security holders resident in the Policy Jurisdiction. MP 31-202 does not provide any "bright line" exemptions from registration. Accordingly, for purposes of the investment fund manager registration requirements of the Policy Jurisdictions, a NRSB that acts as an investment fund manager must simply decide whether

it is, or is not, required to register as such based on the guidance provided by MP 31-202.

Like CP 32-102, MP 31-202 begins by identifying those functions or activities that are indicative of a person or company that directs or manages the business, operations, or affairs of an investment fund, and thereby acts as an investment fund manager for purposes of the investment fund manager registration requirements of the Policy Jurisdictions. The functions or activities that are identified by MP 31-202 are the same as the activities identified by CP 32-102 that are set out above.

MP 31-202 then goes on to provide that an investment fund manager is required to register in a Policy Jurisdiction if it directs or manages the business, operations, or affairs of an investment fund from a physical place of business in the Policy Jurisdiction or if its head office is located in the Policy Jurisdiction. If it does not have a physical place of business or head office in the Policy Jurisdiction, it will still be required to register if it engages in activities that result in its directing or managing the business, operations, or affairs of an investment fund in the Policy Jurisdiction.

According to MP 32-102, in determining whether registration is required, a NRSB must consider what functions or activities, if any, that it is directing from within a Policy Jurisdiction, and, for such purpose, no single function or activity is determinative. In particular, functions or activities that are tied to the presence of security holders, the solicitation of investors, or the distribution of securities in a Policy Jurisdiction are not activities that would give rise to investment fund manager registration, unless they are directed from within the Policy Jurisdiction and result in the person directing or managing the business, operations, or affairs of an investment fund in the Policy Jurisdiction.

Unregistered Investment Fund Manager Annual Fee—Ontario Only

A NRSB that relies on the International Investment Fund Manager Exemption is required to pay an annual capital markets participation fee under OSC Rule 13-502 – *Fees* due to its status as an unregistered exempt international firm relying on s.4.2 of MI 32-102. The capital markets participation fee is based on revenues earned in Ontario by a firm and is intended to represent a fee for a market participant's use of the Ontario capital markets. The fees are payable by check or wire transfer to the Ontario Securities Commission.

An unregistered investment fund manager is required to complete and file Form 13-502F4 electronically with the OSC by December 1 of each year and to pay the capital markets participation fee by December 31 of each year based on capital market activities in the financial year ending in the then current calendar year. Form 13-502F4 must contain a certification signed by the chief compliance officer of the unregistered investment fund manager, or, if the unregistered investment fund manager does not have a chief compliance officer, an individual acting in a similar capacity. If the unregistered investment fund manager's annual financial statements for its financial year ending during the then current calendar year have not been completed by December 1 of that calendar year, the unregistered investment fund manager is required, by December 1, to prepare Form 13-502F4, and, by December 31, pay the capital markets participation fee for the financial year based on a good faith estimate of its specified Ontario revenues as at the end of the financial year, and then, if necessary, adjust the fee paid in the manner described below.

If Form 13-502F4 is not filed on or before December 1, a late fee is payable of $100 per business day, subject to a maximum aggregate late fee of

a. $5,000 per calendar year; or

b. if the estimated specified Ontario revenues for the previous financial year are $500 million or greater, $10,000,

for all forms or documents required to be filed or delivered in the calendar year.

If the capital markets participation fee, or any additional fees in respect of the fee adjustment described below, is not paid on time, a late fee will be imposed of one-tenth of 1% per business day of the unpaid portion of the capital markets participation fee payable.

Unregistered Investment Fund Manager —Annual Notice of Continued Reliance

A NRSB that has relied on the International Investment Fund Manager Exemption at any time during the twelve-month period preceding December 1st of a year must provide the Securities Regulator in the relevant Instrument Jurisdiction with notice of the following by December 1st of that year:

- the fact that it relied on the International Investment Fund Manager Exemption; and
- for all investment funds for which it acts as an investment fund manager, the total assets under management, expressed in Canadian dollars, attributable to securities beneficially owned by residents of the Instrument Jurisdiction as at the end of the most recently completed month.

Annual Registration Exemption Filing Requirements

Annual Notice of Continued Reliance

It is a condition of both the International Dealer Exemption and International Adviser Exemption that a NRSB that has relied on either exemption during the twelve-month period preceding December 1st of a year must notify the applicable Securities Regulator(s) of such reliance by December 1st of that year.[12] There is no prescribed form for such notification and it can therefore be given by way of a letter or an email. In Ontario, a NRSB relying on either exemption is not required to comply with this notification requirement if it complies with the annual capital markets participation fee requirements described below. In Saskatchewan, Alberta, British Columbia and Manitoba, a fee is payable at the time the annual notification is provided.

Ontario Annual Capital Markets Participation Fee

In Ontario, a NRSB that becomes registered as a dealer, an adviser, or an investment fund manager, or that relies on the International Dealer Exemption or the International Adviser Exemption, is required to pay an annual capital markets participation fee that is comparable to the annual fee, described above, that must be paid by unregistered investment fund managers. Like the fee that is payable by unregistered investment fund managers, the annual capital markets participation fee payable by NRSBs relying on the International Dealer or International Adviser Exemption must be calculated by completing Form 13-502F4. Form 13-502F4 must be completed and filed electronically with the OSC, then printed, signed, and retained by the NRSB by December 1st of each year.

The amount of the capital markets participation fee that is payable by an exempt international dealer or adviser is based on the NRSB's specified Ontario revenue and is determined with reference to the capital markets participation fee table set out in OSC Rule 13-502 *Fees*.

Exempt NRSBs must generally pay their capital markets participation fees by check or wire transfer prior to December 31st. Registrant firms must generally pay their capital markets participation fee (along with annual registration fees payable in other Canadian jurisdictions where the firm is registered) electronically through the National Registration Database on December 31st.

Prospectus Requirements

As described above, an investment fund or private equity fund that proposes to distribute its securities in Canada must either qualify the distribution pursuant to a prospectus prepared and filed in accordance with applicable Canadian securities regulatory requirements or it must conduct the distribution

in reliance upon a prospectus exemption. The prospectus exemptions that are most commonly relied upon for capital raising purposes are the accredited investor exemption and the minimum investment exemption.

Accredited Investor Exemption

The accredited investor exemption (the "Accredited Investor Exemption") is available for distributions that are made to persons or companies who are accredited investors and who purchase the securities as principal.[13] A list of persons and companies that are considered accredited investors ("Accredited Investors") for purposes of the Accredited Investor Exemption is set out in section 1.1 of National Instrument 45-106 Prospectus Exemptions ("NI 45-106").

Minimum Investment Exemption

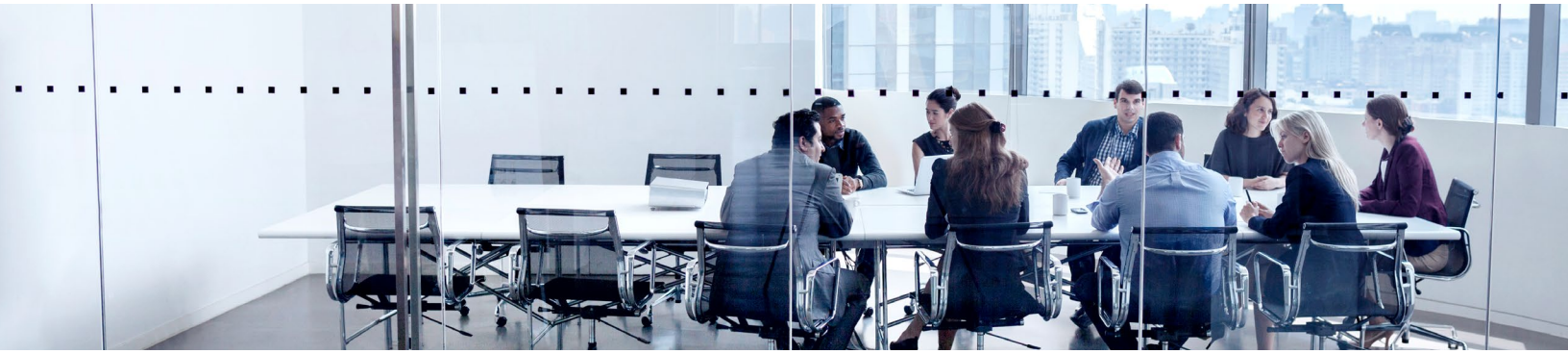
The minimum investment exemption (the "Minimum Investment Exemption") is available to accommodate distributions of securities that have an aggregate acquisition cost to the purchaser of the securities that is not less than CAD $150,000 paid in cash at the time of the distribution provided the purchaser purchases the securities as principal.[14] The Minimum Investment Exemption is only available in respect of the securities of a single issuer and is unavailable if the purchaser of the securities is an individual or was created, or is used, solely to purchase or hold securities in reliance upon the Minimum Investment Exemption.

Offering Memorandum Requirement

If an offering document is to be used to solicit sales of foreign securities, including securities of investment funds or private equity funds, that are to be distributed in Canada in reliance upon either the Accredited Investor Exemption or the Minimum Investment Exemption, the offering document will probably be considered an offering memorandum. Generally speaking, any material prepared in connection with such a private placement, other than a "term sheet" that is limited to describing the terms of the securities being issued rather than describing the business and affairs of the issuer, will be considered an offering memorandum. Purchasers who receive an offering memorandum have a statutory right of action for rescission or damages for any misrepresentation in the offering memorandum. In a number of provinces, the statutory right of action must be described in the offering memorandum and two copies of the offering memorandum must be delivered to the relevant Securities Regulator(s) within ten days of the distribution. If a foreign prospectus is used as an offering memorandum, it is common to attach a stand-alone Canadian "wrapper" to describe the statutory rights of action and to address other related disclosure requirements.

Exempt Trade Reporting and Filing Fee Requirements

If the securities of an issuer are distributed into a province or territory of Canada in reliance upon either the Accredited Investor Exemption or the Minimum Investment Exemption, the issuer is required to file a completed Form 45-106F1 exempt trade report with the applicable Securities Regulator(s) within ten (10) days of the distribution, and the filing of the report must be accompanied by the payment of a prescribed filing fee that varies from jurisdiction to jurisdiction. Alternatively, an investment fund can comply with the exempt trade reporting and filing fee requirements by filing the Form 45-106F1 and the related filing fee with the Securities Regulator(s) within thirty days of the end of the relevant calendar year end in lieu of the ten-day period noted above.



Registration Requirements Applicable to Offshore Private Equity Fund Offerings into Canada

When considering the application of the dealer registration and investment fund manager registration requirements to the offering of offshore funds into Canada, it is important to consider whether the collective investment vehicle is an investment fund or a private equity fund (a "PE Fund") for Canadian securities law purposes.

The dealer registration and investment fund manager registration requirements may apply to the offering of an offshore investment fund into Canada, but will not necessarily apply to offerings of offshore PE Funds into Canada.

For Canadian securities regulatory purposes, an investment fund is either an open end or closed end investment fund that offers liquidity, takes passive positions in securities, and does not try to exercise control or otherwise influence the day-to-day business of the investee issuer. Unlike investment funds, a PE Fund raises capital for the purpose of investing in issuers that are not publicly traded and becoming actively involved in the management of such issuers, often over a period of several years. As a result, persons or companies that invest in a PE Fund must generally agree to remain invested in the PE Fund for a period of time, and thereby agree to forego the liquidity that is generally characteristic of an investment in an investment fund.

Examples of active management in an issuer include a PE Fund having:

- representation on the board of directors;
- direct involvement in the appointment of managers; and/or
- a say in material management decisions.

The PE Fund looks to realize on the investment either through a public offering of the issuer's securities, or a sale of the business conducted by the issuer. At this point, the investors' money can be returned to them, along with any profit.

Investors rely on a PE Fund manager's expertise in selecting and managing the issuers in which it invests. In return, the PE Fund manager receives a management fee or "carried interest" in the profits generated from these investments. They do not receive compensation for raising capital or trading in securities. By contrast, investors rely on investment fund managers to manage an investment fund, but not to manage in any way the underlying businesses that are included in the investment portfolio of the investment fund.

Applying these considerations to the dealer registration and investment fund manager registration requirements, the Securities Regulators have, by way of interpretive guidance, advised that if a PE Fund manager is not compensated for either the raising or investment of money received from investors, and both the raising and investment of such money are occasional, the dealer registration requirement should not apply to the PE Fund manager in respect of its capital raising activities on behalf of the PE Fund. Similarly, the PE Fund manager would not be subject to the investment fund manager registration requirement because it would be managing a PE Fund rather than an investment fund.

If the PE Fund is not an investment fund and does not have more than 50 investors (excluding employees) it may be possible for the PE Fund to qualify for the private issuer exemption from the prospectus requirement where a distribution of securities is made to accredited investors in reliance upon the private issuer exemption (the "Private Issuer Exemption"). Where a distribution is made in reliance upon the Private Issuer Exemption there is no Form 45-106FI filing required.

This dealer registration and investment fund manager registration analysis may be different if the PE Fund engages in activities other than those described above.

Limited Partnership Securities Offerings

Some investment fund or private equity issuers are organized as limited partnerships. In some Canadian jurisdictions, this raises registration issues for the investment fund under limited partnership legislation. For example, the *Limited Partnerships Act* (Ontario) (the "LPA") provides that no limited partnership formed in a jurisdiction outside Ontario (an "extra-provincial limited partnership") shall "carry on business" in Ontario unless it has filed a declaration with the Ministry of Consumer and Business Services (the "Ministry"). An extra-provincial limited partnership is deemed to "carry on business" in Ontario if, among other things, it effects a distribution of its securities in Ontario by way of an offering memorandum in compliance with Ontario securities law.

The prescribed form of declaration requires disclosure of the name of the extra-provincial limited partnership, the nature of its business, the general partner's name and address, and the name of the extra-provincial limited partnership's attorney for service in Ontario. The declaration must be amended whenever there is any change in the information provided by it. It expires five years after its date of filing. The extra-provincial limited partnership must also sign a power of attorney appointing a person resident in Ontario to be the attorney and representative in Ontario of the extra-provincial limited partnership.

The general partner of an extra-provincial limited partnership must also maintain a current record of the limited partners. The record must set out the name of each limited partner, an address for service, and the amount of money and the value of other property contributed or to be contributed by the limited partner to the limited partnership. The attorney and representative in Ontario for the extra-provincial limited partnership must keep the record of limited partners. Any person would be able to inspect the record of limited partners during normal business hours of the limited partnership's attorney and representative, and may make copies of, and take extracts from, it. Every extra-provincial limited partnership must also keep at its attorney and representative in Ontario at the address stated in the power of attorney, copies of,

among other things, the partnership agreement, the declaration, and the power of attorney. Any partner may inspect any such documents that are required to be kept with the attorney and representative during normal business hours of the partnership's attorney and representative. Any person who has a business relationship with the partnership may inspect any of the documents (other than the partnership agreement) during normal business hours of the partnership's attorney and representative. There is no requirement under the LPA to file a copy of the partnership agreement with a governmental authority.

A failure to file the required documentation under the LPA would not affect the limitation of liability of limited partners of the extra-provincial limited partnership resident in Ontario, nor would that render void or voidable any contract entered into between the extra-provincial limited partnership and a holder of its securities in Ontario. The chief practical consequence of failing to file the required documentation is that the extra-provincial limited partnership and any member of the extra-provincial limited partnership would not be capable of maintaining a proceeding in an Ontario court without leave of the court.

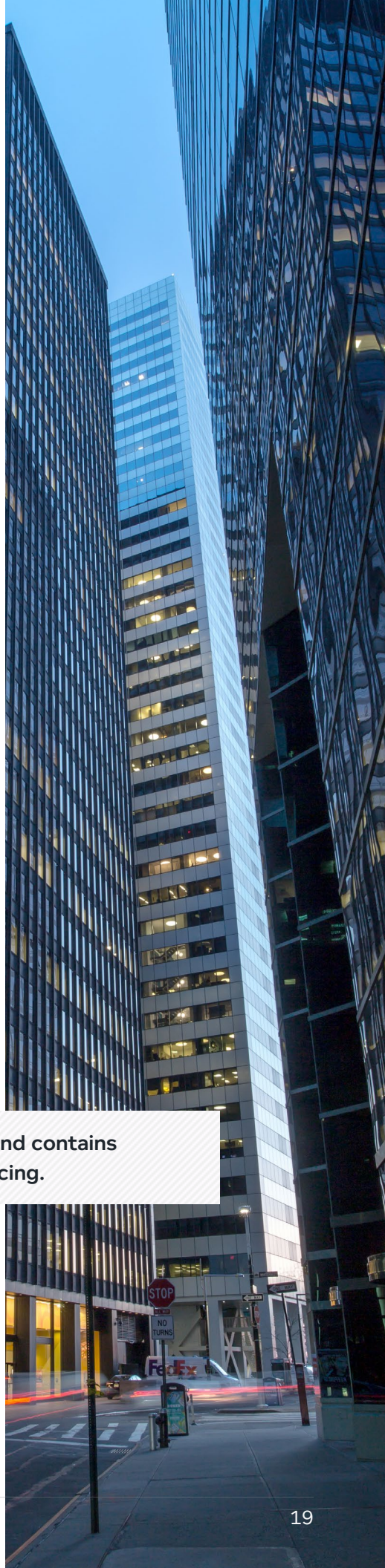
If an investment fund distributes securities in a Canadian jurisdiction outside Ontario, we recommend reviewing local requirements to determine whether the investment fund must be registered as an extra-provincial limited partnership in that jurisdiction.

Anti-Money Laundering and Terrorist Financing Regulation

NRSBs operating in Canada in reliance upon the International Dealer Exemption or the International Adviser Exemption are subject to the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act* (Canada) and its regulations, and to the oversight of the Financial Transactions and Reports Analysis Centre of Canada ("FINTRAC"), which has also issued detailed guidance applicable to securities dealers.

In addition, the *Criminal Code* (Canada) also applies to NSRBs and contains broad prohibitions against money laundering and terrorist financing.

Among other requirements, the PCMLTFA requires securities dealers to have in place a compliance program (including having in place compliance policies and procedures, a written training program, and a risk assessment and appointing a compliance officer), to perform effectiveness testing and to comply with certain customer identification, record-keeping and reporting requirements. In addition, the *Criminal Code* (Canada) also applies to NSRBs and contains broad prohibitions against money laundering and terrorist financing.



Economic Sanctions Requirements

NRSBs operating in Canada in reliance upon the International Dealer Exemption or the International Adviser Exemption are subject to certain monitoring and reporting requirements under Canada's federal economic sanctions and anti-terrorism legislation that list proscribed individuals and entities.

These lists are established under Canada's *Justice of Victims of Corrupt Foreign Officials Act (Sergei Magnitsky Law)*, the *Special Economic Measures Act, the United Nations Act*, the *Freezing Assets of Corrupt Foreign Officials Act*, and the *Criminal Code*. They are frequently updated as the government reacts to developments in international relations and global conflicts.

Depending upon the list in question, NRSBs are required to determine on a continuing basis whether they are in possession or control of property owned, held or controlled by or on behalf of the listed persons, and in some cases, submit monthly reports to their provincial regulators, for example Quebec's Autorité des marchés financiers or the Ontario Securities Commission. These reports stipulate that the NRSB is either not in possession or control of any such property or that they are in possession or control of such property, in which case they must also report the number of persons, contracts or accounts involved and the total value of the property. The Canadian securities regulators take the position that NRSBs subject to these requirements must screen all of their clients against these lists regardless of whether the clients are located in or outside of Canada.

As a result of amendments made effective March 4, 2019, a number of these sanctions measures also now require NRSBs to disclose without delay to the Commissioner of the Royal Canadian Mounted Police or to the Director of the Canadian Security Intelligence Service (i) the existence of property in their possession or control that they have reason to believe is owned, held or controlled by or on behalf of a listed person and (ii) any information about a transaction or proposed transaction related to such property.

We recommend that NRSBs carefully review their compliance policies and controls to ensure they satisfy the screening and reporting requirements set out in Canada's economic sanctions and anti-terrorism legislation.

Canadian Registration Compliance Services

We understand the complex maze of provincial and territorial legislation applicable to NRSBs and can help you navigate your way so that you can stay on the right side of the law. For a competitive annual fixed fee, you will gain access to our subscription service through which you will receive a tailored, evergreen memo of advice containing timely updates as changes in applicable regulation occur.

The updates will cover:

- How the NRSB may engage with Canadian investors in compliance with securities and derivatives law registration exemptions, anti-money laundering, terrorist financing and economic sanctions law
- Assistance in perfecting the registration exemptions
- Assistance in paying regulatory fees associated with the registration and prospectus exemptions
- Assistance in preparing all required client disclosures, including Canadian PPM wrappers and Canadian subscription supplements
- Assistance in preparing post private placement trade reports and payment of the associated regulatory fee
- Acting as the local agent for service in Ontario, Québec, British Columbia or Alberta as required by registration exemptions

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Endnotes

1	On May 26, 2010, the Canadian Minister of Finance released a draft of a proposed federal securities law (the "Proposed Federal Securities Act") that was intended to establish a comprehensive and uniform framework for the regulation of securities and derivatives trading and advisory activities throughout the country. Rather than introducing the Proposed Federal Securities Act to Parliament as a bill, the federal government referred it to the Supreme Court of Canada for the Court's opinion on the constitutional authority of the federal government to enact such legislation. The Supreme Court of Canada rendered its decision on December 22, 2011 and ruled unanimously that the Proposed Federal Securities Act is not constitutional because the federal government does not have the power to regulate comprehensively trading in securities pursuant to its general trade and commerce power under the *Constitution Act, 1867*. The Supreme Court of Canada noted that, although the federal government's power to regulate trade and commerce is broadly cast, it cannot be used in a way that denies the provinces the power to regulate local matters and industries within their boundaries. Subsequently, on September 19, 2013, certain provincial governments and the government of Canada agreed to establish a cooperative capital markets regulatory ("CCMR") system and they invited all other provinces and the territories to participate in the proposed system. The CCMR is a cooperative regulatory framework based on agreements between the federal government and participating provinces and territories that aims to replace the current securities regulatory regime with a single harmonized regime across all participating jurisdictions built on a model provincial statute and a more narrowly focused federal statute aimed at regulating national "systemic risks" affecting capital markets. On November 9, 2018, the Supreme Court of Canada ruled that the CCMR's proposed federal and provincial statutes were valid because they respected the delineation between the powers of the provinces and territories to regulate securities and the much more circumscribed powers of the federal government to regulate systemic risk, as determined by the Court in its 2011 decision. The Court also found that certain provisions in an inter-provincial agreement which speak to the making of regulations under the provincial and federal statutes and to amendments to the model provincial securities legislation do not abridge provincial legislative power but rather are subject to it and therefore valid under constitutional law. If and when the CCMR becomes effective, it would mark a significant change in securities regulation in Canada and would affect every major securities regulatory process and regime, including registration, prospectus qualification, insider trading, multi-jurisdictional applications for exemptive relief, derivatives regulation and enforcement. Current CCMR participants are Ontario, British Columbia, Saskatchewan, New Brunswick, Prince Edward Island, Yukon and the Federal Government. Nova Scotia has also announced its intention to join the CCMR. At least initially, the CCMR is expected to co-exist with and mesh with the rules of important non-participating jurisdictions, including Quebec and Alberta.
2	For purposes of section 8.18 of NI 31-103, a foreign security means a security that has been issued by an issuer incorporated, formed or created under the laws of a foreign jurisdiction and a security issued by the government of a foreign jurisdiction.
3	For purposes of NI 31-103, a permitted client is an entity or individual identified in section 1.2 of NI 31-103- essentially being institutions and high net worth individuals.
4	Section 8.5 of Companion Policy 31-103CP to NI 31-103.
5	"designated rating" has the same meaning as in paragraph (b) of the definition of "designated rating" in National Instrument 81-102 *Investment Funds*.
6	"designated rating organization" has the same meaning as in National Instrument 44-101 *Short Form Prospectus Distributions*.
7	"DRO affiliate" means an affiliate of a designated rating organization that issues credit ratings in a foreign jurisdiction and that has been designated as such under the terms of the designated rating organization's designation.
8	*Supra* note 3.
9	*Supra* note 2.
10	For purposes of the International Adviser Exemption, aggregate consolidated gross revenue does not include the gross revenue of an affiliate of the adviser if the affiliate is registered in a jurisdiction of Canada.
11	In Ontario only, the GA Exemption is found in section 34(1) of the *Securities Act* (Ontario). The wording of section 34(1) is noteworthy because it is more descriptive of the scope of the GA Exemption than section 8.25(2) of NI 31-103. Section 34(1) provides, in part, that the GA Exemption is available to a person or company that engages in, or holds himself, herself or itself out as engaging in the business of providing advice, either directly or through a publication or other media, with respect to investing in or buying or selling securities, including any class of securities and the securities of a class of issuers, that are not purported to be tailored to the needs of anyone receiving the advice.
12	Sections 8.18(5), 8.18(6), 8.26(5) and 8.26(6) of NI 31-103.
13	Section 2.3 of NI 45-106.
14	Section 2.10 of NI 45-106.

Securities Regulation and Investment Products

Market participants benefit from the Securities Regulation & Investment Products (SRIP) Group's comprehensive understanding of the regulatory landscape in Canada and the vast array of financial products and services in today's capital markets.

Our clients include both domestic and non-resident dealers, advisors, investment fund managers, commodity-futures merchants, commodity-trading managers, financial institutions, alternative trading systems and other market participants.

The SRIP Group was established in 2000 in response to the numerous market and regulatory developments that occurred throughout the 1990s. In particular, the dramatic growth of the investment management sector during that decade served as a catalyst for the proliferation of regulatory initiatives that led to the establishment of a comprehensive framework for the regulation of financial products and services in Canada. As a result of these developments, the present regulatory framework encompasses a diverse range of market activity that includes the development and dissemination of exempt and non-exempt financial products and services, the registration or licensing of dealers, advisors and alternative trading systems and the ongoing trading and advisory activities that are conducted by them. These regulatory requirements are complex and pervasive and can have a significant impact upon the way in which various market participants structure and operate their businesses.

The range of legal services that are provided by the SRIP Group generally fall into one of the following legal service categories:

- **Securities trading** – Regulatory requirements governing the trading of securities by investors, dealers, advisors, financial institutions, marketplaces and other market intermediaries.
- **Advisor regulation** – Regulatory requirements in relation to services and products offered by businesses and individuals engaged in offering investment counselling and portfolio management services.
- **Investment funds** – Assisting with the establishment, distribution, governance, day-to-day operations, restructuring and termination of investment funds, including mutual funds, pooled funds, closed-end funds, alternative-investment funds and labour-sponsored funds.
- **Transaction work** – Assisting with the conduct of transactions involving the establishment, sale, transfer, restructuring or merger of dealers, advisors and financial products and services.
- **Regulatory proceedings** – Advising on regulatory risks associated with particular trading and advisory activities, responding to compliance reviews, audits and information demands by regulators, responding to investigations and enforcement proceedings and assisting with securities firm bankruptcies, insolvencies and civil cases.
- **Anti-money-laundering and privacy** – Advising on compliance with Canada's recently amended anti-money-laundering rules and privacy regulations, including disclosing required information to the Financial Transactions and Reports Analysis Centre of Canada and developing anti-money-laundering and privacy programs.

Securities Regulation and Investment Products Group

Members of the SRIP Group are located in our firm's Toronto, Montréal, Calgary and Vancouver offices. We partner regularly with our firm's tax, banking, pension fund, litigation and merger and acquisition specialists to assist our financial services clients with the development of effective strategies for addressing the impact of Canadian securities, tax, pension, banking and other laws on the establishment and conduct of their operations in Canada.

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www.mccarthy.ca/en/insights/blogs/canadian-securities-regulatory-monitor

FURTHER READING

International Comparative Legal Guide to: Alternative Investment Funds 2020

International Comparative Legal Guide to: Public Investment Funds 2020

About Us

McCarthy Tétrault LLP is a premier full-service Canadian law firm advising on large and complex transactions and disputes for domestic and international clients. The firm has offices in every major business center in Canada, and in New York and London. The firm's industry-based team approach and depth of practice expertise helps our clients achieve exceptional commercial results.

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