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May 29, 2008

Via Email

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Alberta Securities Commission
Saskatchewan Financial Services Commission
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
New Brunswick Securities Commission
Registrar of Securities, Prince Edward Island
Nova Scotia Securities Commission
Superintendent of Securities, Newfoundland and Labrador
Registrar of Securities, Northwest Territories
Registrar of Securities, Yukon Territory
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Dear Sirs/Mesdames:

Re: Proposed National Instrument 31-103 *Registration Requirements*, Companion Policy and Related Forms Published for Comment on February 29, 2008

We are pleased to provide the members of the Canadian securities administrators (CSA) with comments on the above-noted proposed instruments (the Proposed Rule, the Proposed Policy and collectively, the Proposals).

These comments are those of lawyers in BLG's Securities and Capital Markets practice group and do not necessarily represent the views of individual lawyers, the firm or our clients, although we have incorporated feedback received to date from certain of our clients into this letter. Our comments follow the general format of the Proposed Rule and contain more substantive comments, as well as some drafting comments.

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Our comments on proposed National Instrument 45-106 *Prospectus and Registration Exemptions* follow in a separate letter, although given our focus on reviewing the Proposals, we have not provided many detailed comments on this National Instrument.

Other than reviewing the CSA responses to comments we made in 2007 on two forms, we have not provided detailed comments on the proposed amendments to National Instrument 31-102 *National Registration Database* and to National Instrument 33-109 *Registration Requirements* since we believed our time would be better spent focusing on the Proposals. We respectfully request that the comment period on the latter proposed amendments be extended by at least another month and we ask that the CSA broadcast this extension by publication of a notice describing the same. Given the amount of material that was published at the end of February (close to 1,000 pages of printed type), we found that the ninety-day comment period was insufficient to allow us to review all of the proposed instruments with our clients. We urge the CSA not to take the lack of comments on these proposed instruments to be necessarily agreement with the proposed changes.

We have also provided the Ontario government with comments on the draft amendments to the Ontario Securities Act that were published for comment on April 25, 2008 and are attaching a copy of that letter for your information.

We were pleased to comment on the first version of the Proposals that was published for comment in February 2007 and note that the CSA favourably responded to certain of those comments in this second version of the Proposals. We appreciate the CSA's careful consideration of our earlier comment letter. To the extent that we repeat our earlier comments, we have provided additional explanation as to the importance and significance of the comment, so that the CSA can fully appreciate our reasons for raising the comment a second time.

Support for the CSA's General Direction

We fully support the goal of the CSA with the overall Registration Reform Project: to harmonize, streamline and modernize the registration regime across Canada and to create a flexible and administratively efficient regime with reduced regulatory burden.

To the extent that the Proposals will create a nationally uniform set of rules that would govern the "fit and proper" requirements and conduct rules for registrants, as well as any applicable exemptions for specified industry participants, we believe that the Proposals are a very positive regulatory development. Today, in order to properly advise our clients, we must keep track of not only differing rules in the various provinces that apply to the same activity or registrant, but even more troubling, different interpretations and methods of administering regulations, rules and legislation that may be substantively the same in each province. Today's regulatory regime creates inefficiencies, regulatory burdens and increased costs for our clients that are unjustified in the context of the Canadian capital markets.

1. **Concerns about Lack of Uniformity in Approach**

We urge the CSA to move forward with the Proposals with a view to ensuring that each jurisdiction passes uniform legislation and rules, and, even more importantly, that staff in each jurisdiction administer and interpret the legislation and rules in a uniform and consistent fashion.

As we noted in our first comment letter on the Proposals, most securities industry participants in Canada are not "local" market participants, given that for the most part, securities are sold to all Canadians in every province and territory and industry participants often participate in the markets in many of those jurisdictions. To the extent industry participants today distribute securities or advise on securities in a limited number of provinces or territories, they generally do so to avoid having to deal with all regulators and all laws in all provinces and territories. We see no need for *any* local rules or regulation and, particularly, no need for any differing interpretations or administrative positions (particularly unwritten administrative positions) by different regulators.

We are increasingly concerned that the above-noted goals of the CSA will not be met. We described our concerns with the draft Ontario legislation in the attached comment letter. We know that many of the other provincial governments are considering bringing into force different legislation and certain of the CSA members are "opting out" or proposing different rules for their province. In fact, in the Notice alone, we counted over ten different significant circumstances where a member or members of the CSA propose to make a rule that is different from the other members of the CSA. In most cases, the policy rationale behind the perceived need for such differences is not explained in any great detail, so that we are left essentially to guess at the reasons why the "problems" that the different rules are designed to solve differ from one province to another.

We fundamentally do not agree that any inherently different problems exist in the securities industry in one province from another that would justify differences in rules. We assume that the reason for the differences is that one (or more) securities regulatory authority takes a different philosophical view of the issue than the majority. As we note above, any differences between provincial securities regulation only serves to increase the costs of doing business in Canada, which we submit is not a positive development, particularly when these differences are based solely on philosophical opinions as to the particular issue at hand held by different regulatory staff in the applicable provinces.

2. **Registration of Mutual Fund Dealers (section 2.1) – Trading in Mutual Funds, Scholarship Plans and Deposit Instruments**

Section 2.1 as drafted allows a mutual fund dealer to trade in "mutual funds" and labour sponsored investment funds. In most provinces and territories, the reference to LSIFs will be redundant, since LSIFs are clearly considered to be "mutual funds" by most members of the CSA.

Our reading of this section, which we believe is legally correct and appropriate from a regulatory policy perspective, is that a mutual fund dealer would be permitted to trade in a security of any issuer that falls within the definition of "mutual fund" provided for in

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securities legislation. This would allow mutual fund dealers to trade in securities of the following issuers:

- Mutual funds that comply with both National Instrument 81-101 and National Instrument 81-102 (so-called "conventional mutual funds");
- Commodity pools governed by National Instrument 81-102 and National Instrument 81-104;
- Labour sponsored investment funds in those provinces that consider them to be mutual funds (the other provinces would specifically permit this trading via the Proposed Rule);
- Mutual funds that are distributed pursuant to a prospectus exemption (i.e. the mutual fund issuing the securities would need to ensure that a prospectus exemption existed in respect of the trade by the mutual fund dealer); and
- Exchange-traded funds to the extent they are considered "mutual funds" under securities legislation.

A mutual fund dealer would need no other registration in order to carry out the above-noted trades.

However, according to the Proposals, a mutual fund dealer would need to be also registered as a scholarship plan dealer to trade in securities of a scholarship plan and also as an exempt market dealer to trade in any other securities that are being distributed pursuant to a prospectus exemption.

The Proposals are silent on whether the securities regulators would prohibit a mutual fund dealer from dealing in financial instruments that are not considered "securities" under securities legislation, including deposit instruments, such as GICs and principal protected notes, and specialized financial products, such as high interest bank accounts, provided that the dealer complied with the rules of the MFDA.

Given our understanding of the current varying and inconsistent administrative positions taken by various members of the CSA about the ability of mutual fund dealers to distribute exempt products and mutual funds that are not conventional mutual funds, we submit that it is critical that the CSA carefully ensure that the Proposed Rule permits mutual fund dealers to trade in the above-noted securities. For the reasons set out below, in our view, mutual fund dealers should be permitted to distribute "mutual funds", scholarship plans and financial instruments that are not considered securities under securities legislation pursuant to their registration as mutual fund dealers, in full recognition of the extensive regulatory influence of the MFDA, as well as current industry practice.

Accordingly, we urge the CSA to:

(a) Clarify the ability of mutual fund dealers and their representatives to trade in securities of any issuer that is a "mutual fund" under securities legislation. This would include mutual funds that are distributed pursuant to prospectus exemptions ("pooled funds"). No additional registration as an exempt market dealer would be necessary. We recommend this clarification be provided in the Proposed Policy. We made this comment in our letter commenting on the first version of the Proposals and the CSA appeared to agree with this comment – please see comment 173 of the Summary of Comments.

(b) Permit, via the Proposed Rule, mutual fund dealers and their representatives to trade in securities of scholarship plans without being also registered as scholarship plan dealers. We agree with the approach of the British Columbia Securities Commission and l'Autorité des marchés financiers in allowing mutual fund dealers in their respective provinces to also trade in scholarship plans, given the similarities between mutual funds and scholarship plans.

(c) Clarify, in the Proposed Policy, that mutual fund dealers and their representatives are permitted to deal in the financial instruments that are not considered securities under securities legislation that we note above, provided they comply with the rules of the MFDA. No additional registration as an exempt market dealer would be required to deal in these financial products, which is consistent with the fact that these financial products are not "securities" and accordingly securities regulators have no jurisdiction over them. This would permit a mutual fund dealer to continue to deal with its clients in GICs, PPNs and high interest savings accounts, along with other deposit instruments.

(d) Remove any impediment to the above in any local regulation of any province and territory and remove any reference to additional proficiency requirements to distribute the above-noted products that may be found in any CSA rule (including local rules) – this would include revising National Instrument 81-104 to remove the specific additional proficiency requirements for mutual fund dealers to distribute commodity pools.

In our view, the mutual fund dealer registration category should permit registered firms to distribute securities of mutual funds and scholarship plans, whether on a public or exempt basis and financial products that do not fall within the purview of securities regulators, such as, deposit instruments and PPNs. In all cases, we believe that the regulatory oversight of mutual fund dealers, when coupled with the proficiency required of mutual fund dealer representatives, is sufficient to cover the securities noted above and no additional registration or proficiency is necessary. We see no investor protection or other regulatory need to require mutual fund dealers and their representatives to seek additional registration – in some cases in two additional dealer categories (scholarship plan dealers and exempt market dealers). Requiring this additional registration will only

serve to increase the costs to an already overburdened, but essential, segment of our Canadian securities industry.

We acknowledge the response of the CSA to this comment, which we (and many others) made in our 2007 letter commenting on the first version of the Proposals (comments 170–178 of the CSA's Summary of Comments), but we urge the CSA to consider our comments again, given the importance of this comment to the Canadian mutual fund distribution industry. We do not understand the responses of the CSA to the effect that the distribution of these securities is different in substance to the distribution of mutual funds and that registration categories and terms are tailored to specific purposes. With respect to the latter response of the CSA, in virtually all respects the "fit and proper" and "conduct" rules that apply to mutual fund dealers is higher than for exempt market dealers and scholarship plan dealers; additionally, mutual fund dealers must be members of the MFDA and subject to its considerable regulation and regulatory influence.

Comments 3 and 4 below are intrinsically related to this comment 2 and must be considered together by the CSA.

3. Registration of Mutual Fund Dealers (section 2.1) – Trading in Exempt Securities

In addition to the submissions we make in our comment 2, we strongly urge the CSA to permit mutual fund dealers that are members of the MFDA to trade in securities that are distributed under prospectus exemptions without the necessity of requiring these firms to become registered as exempt market dealers. As we outline in comment 2, mutual fund dealers are subject to self-regulatory oversight and a regulatory regime that is more than sufficient, in our view, to monitor their exempt market activities. Any additional registration requirement is an additional regulatory burden, since additional personnel, compliance efforts, legal and audit costs and management time will have to be expended to obtain and maintain this registration. In our view, given that most, if not all, of the fit and proper requirements and conduct rules that apply to mutual fund dealers are higher and more substantive than for exempt market dealers, requiring mutual fund dealers to also be registered as an EMD, adds absolutely no additional investor protection, but merely imposes yet another "regulatory hoop" for mutual fund dealers to jump through.

If the CSA are of the view that their oversight of the Canadian capital markets would be enhanced if the members of the CSA were aware of all participants who trade in the exempt marketplace (we understand that this underpins the CSA's reasoning for requiring registration of EMDs), we respectfully submit that a more measured and appropriate regulatory response would be to require MFDA members to make a simple one-time notice filing with the MFDA and/or their principal regulator outlining their intentions to trade in exempt products. However, we point out part of the MFDA's oversight of their members includes monitoring their exempt market activities, which in our view, negates the necessity for the CSA to monitor this (i.e. their delegated SRO carries out this monitoring).

4. Registration of Mutual Fund Dealers (section 2.1) – Trading in Exempt Mutual Funds (Pooled Funds)

In our comment letter on the first version of the Proposals, we commented on the implications of any restriction on the ability of mutual fund dealers to trade in mutual funds distributed pursuant to prospectus exemptions. If, notwithstanding our comment 2 above, the CSA is of the view that pooled funds cannot be traded by mutual fund dealers, then clarification of this position should be included in the Companion Policy (although as noted above, we strongly disagree with that position). Also if this latter position is taken by the CSA, then we are of the view that it is essential for the CSA to provide transitional guidance to the industry in respect of the current billions of dollars of investments in pooled funds held by clients who have accounts with mutual fund dealers. Similarly, if the CSA intends to restrict the ability of mutual fund dealers to deal in financial products that are not securities (PPNs, GICs and other deposit instruments) (again, we strongly urge the CSA to NOT take this position for the reasons outlined above), then it will be incumbent on the CSA to provide transitional guidance on their expectations for mutual fund dealers who have clients with these financial products in their accounts.

5. **Registration of Exempt Market Dealers (section 2.1)**

In our view, the proposed lack of harmonization of the rules that will apply to exempt market dealers in British Columbia and Manitoba is troubling. We do not understand why there should be, in effect, two standards of regulation of exempt market activities within these provinces. Those investors who choose to engage in their exempt market activities with a firm that is based and registered as an EMD in another Canadian province or territory will have their dealer registered in their province and under the oversight of the BC or Manitoba securities regulator, as the case may be. If such investor chooses to work with a firm that is only registered in British Columbia or Manitoba (depending on where the investor lives), then that investor will be dealing with a firm that has no regulatory oversight. We see no reason for this distinction.

6. **Exemption From Dealer Registration for Advisers (section 2.2)**

In our letter on the first version of the Proposals, we provided several comments regarding section 2.2 of the Proposed Rule, none of which, in our view, were satisfactorily answered by the CSA.

In our view, the following changes should be made to section 2.2:

(a) The terminology used should be made more precise and consistent with existing securities regulatory terminology.

(b) The exemption should reflect realities of the marketplace and the close relationships between affiliated financial services entities.

(c) The exemption should be expanded to permit advisers to trade in securities of "pooled funds" with accredited investors, or at a minimum, fully managed accounts they manage and institutional

and other investors who qualify under the new definition "permitted client".

(d) Subsection (2) should be deleted, as imprecise and vague regulation. A portfolio manager often may enter into an investment management agreement with its clients with the intent that the only investment that will be made with that account is in one or more of the pooled funds managed by that portfolio manager (because this form of managing clients' money is more efficient and cost effective than separate segregated money management). Subsection (2) would seem to disallow this relatively common business structure.

(e) Subsection (3) should be deleted, as unnecessarily burdensome regulation.

(f) It should provide for an exemption from the requirement to be registered as an investment fund manager in this context, for the same reasons as the exemption from registration as a dealer. Please see the CSA's response 191 in the Summary of Comments – we were unable to find the agreed upon exemption carried forward into the Proposed Rule. IDA members with discretionary authority (and exempt from adviser registration under section 2.5) should also be exempted from having to be registered as investment fund managers in these circumstances. We made this latter comment in our first comment letter, but do not believe the CSA responded to it.

As we outline in our letter providing the CSA with comments on proposed National Instrument 45-106, given this provision, the Ontario Securities Commission should delete subsection (q)(ii) from the definition of accredited investor in National Instrument 45-106 as the regulatory concerns previously identified for this "opt-out" are, in our view, outdated, speculative and based on erroneous assumptions about the portfolio management industry. If a registration exemption exists, so too should a prospectus exemption and vice versa.

We believe that section 2.2 should read as follows:

> "The dealer registration requirement does not apply to a registered adviser, or an adviser that is exempt from registration under section 8.16 and the investment fund manager registration requirement does not apply to these advisers or to an IDA member that is exempt from registration as an adviser under section 2.5, that trades *[this is a defined term under securities legislation]* in a security of a mutual fund *[this is a defined term under securities legislation]* with an accredited

investor or a fully-managed account[1] *[these are defined terms under securities regulation]* if:

(a) the mutual fund is distributed to the accredited investor or fully managed account pursuant to an exemption from the prospectus requirements in the local jurisdiction;

(b) the investment fund manager of the mutual fund is the adviser or an affiliate of the adviser; and

(c) unless a permitted client *[the new definition in the Proposed Rule]*, the accredited investor has a fully-managed account with the adviser that is managed directly by the adviser and the fully-managed account is managed directly by the adviser."

As we pointed out in our 2007 comment letter, if an adviser chooses to manage its clients' money more efficiently in pooled funds (mutual funds) and has as clients individuals who are accredited investors and hence a prospectus exemption is available, we see no reason why the adviser needs to obtain other dealer or investment fund manager registrations (with their applicable regulatory burdens), merely so it can fulfil its primary function of managing client assets. We believe that this should be the case whether a "permitted client" buys the pooled fund by subscription outside of a managed account or if an accredited investor or other investor buys the pooled fund within a managed account as the sole investment or within a managed account as one of many investments.

Whether or not the client is a discretionary or non-discretionary client of the adviser, the adviser has full K-Y-C and fiduciary duties. Pooled funds merely package the advice into a product format, but do not change the fact that the client is purchasing, and the adviser is providing, essentially advisory and portfolio management services.

7. Investment fund manager category (section 2.6) – *Drafting Comment*

As a drafting matter, given that the phrase "investment fund manager" is defined in securities legislation (in Ontario, in section 1.1 of the Securities Act), the phrase "being a person or company that is permitted to direct the business, operations or affairs of the investment fund" is unnecessary. Leaving this phrase in the Proposed Rule adds considerable confusion as to the intentions of the CSA – we doubt that the CSA wish to add a new definition in light of the existing definitions. Similarly the reference in section 2.8 of the Proposed Policy to a "definition" that mirrors the above phrase is incorrect and for the above-noted reasons should be deleted or amended to refer to the correct definition. Alternatively, the CSA should ensure that the national definitions rule is amended to include a consistent definition for "investment fund manager" and references in the Proposed Rule to definitions of investment fund manager should be to this term defined in the national definitions rule.

[1] Alternatively, if the CSA believe that trading with any "accredited investor" is too broad a dealer exemption, the term "accredited investor" should be deleted, but the references to fully managed account or permitted client retained. Notwithstanding this, we urge the CSA to consider as broad as possible dealer exemption – again to "fit" with the prospectus exemptions.

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8. **Investment fund manager category (section 2.6)**

In our comments on the first version of the Proposals, we asked the CSA to clarify that the scope of being in the business of "investment fund manager" is not to be interpreted so broadly as to require trustees of investment funds to be registered simply because of the trustee's powers over and responsibilities towards a fund, where a separate entity acts as fund manager and actually carries out the functions. Similarly, for funds structured as limited partnerships, the general partner should not be required to register as an investment fund manager where it has delegated management of the limited partnership to a separate management company. We strongly recommend this be clarified, given the discussion in section 1.4.3 of the Proposed Policy in the context of "advising" as it relates to general partners of limited partnerships. We believe the CSA purports to respond to this comment in comment 566 of the Summary of Comments, but we urge the CSA to re-consider this comment in light of section 1.4.3. We are not suggesting the CSA impose an "exemption" in the Proposed Rule, merely to clarify the situation in the Proposed Policy for investment fund managers in similar fashion as for advisers.

(a) In our comments on the first version of the Proposals, we also recommended that the CSA clarify what kind of marketing and dealing activities investment fund managers can carry out without triggering a dealer registration requirement (whether mutual fund dealer or exempt market dealer). We were primarily interested in the CSA confirming in the Proposed Policy that wholesaling activities carried on by investment fund managers does not equate to being in the business of "trading in securities". The CSA responded to this comment with additional commentary in section 2.8.1 of the Proposed Policy, however we find the discussion in this commentary to be confusing and contradictory. The first paragraph "in general…" with the three bullets should be deleted and the second paragraph retained. This second paragraph coincides with our understanding of the law to date, as well as the CSA's application of the law.

(b) We had also asked the CSA to confirm that if an adviser causes a top fund to invest in a bottom underlying mutual fund (whether managed by the same manager or not), in a fund of fund relationship, that this would not mean that the adviser is "in the business of trading in securities" and hence required to register as a dealer, in addition to its registration as an adviser. This is an important point for many in the fund industry, and we note that the CSA purports to respond to this point at comment 565 and we urge the CSA to include the response in the Proposed Policy.

(c) We acknowledge favourably the commentary contained in section 2.8 of the Proposed Policy regarding the jurisdictions where registration will be required for investment fund managers. We believe that this discussion is very helpful, but we note that the draft Ontario legislation (for example) is not written in this fashion. Is this something that the CSA considers needs further clarification via rule or can industry participants rely on the Companion Policy to structure their affairs?

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9. **Individual categories – Dealing and Advising Representatives (section 2.7)**

We fully support the wording changes, both in the Proposed Rule and in the draft Ontario legislation, that clarify that a representative of a registered dealer and adviser can be in a principal-agent (independent contractor) relationship with the dealer/adviser, in addition to a more traditional employment relationship. Consistent with this confirmation, we urge the CSA to ensure that the word "employment" is not used anywhere in the Proposals in the context of representatives of dealers or advisers (we found one such reference in section 4.4 of the Proposed Policy).

However, we were disappointed, as were many of our clients, that the CSA have decided to not proceed to consider how best to allow for "incorporated salespersons" at this time. Given the importance of this issue for dealers (and not just mutual fund dealers) in their recruitment and retention of qualified representatives, we believe that this matter is of critical importance and we believe that an appropriate legal structure can be developed that will ensure appropriate investor protection, while also allowing increased flexibility and tax efficiencies for representatives.

In the interim until a definitive position is taken, we strongly recommend that the CSA clearly permit, via the Proposed Rule or by some other mechanism, representatives of **all** registered dealers to direct commissions to be paid to their personal holding corporations, on the same conditions as recently put into place by the Manitoba Securities Commission.

We know that the approach taken to this matter is not currently uniform across Canada, but given the importance of this issue, we strongly recommend that the CSA work to permit the most permissive scheme through amendments to the Proposed Rule. We believe that the approach adopted by the Manitoba Securities Commission is one that will work in practice, at least in the interim.

10. **Individual categories – Dealing representatives (section 2.7(a)) – *Drafting Comment***

To be consistent with the dealer registration trigger of "being in the business of trading", we suggest that the corresponding individual registration category terminology be consistent and accordingly the term "dealing representative" should be amended to "trading representative".

11. **MFDA membership for mutual fund dealers (section 3.2)**

We strongly recommend that the Proposed Rule codify the "standard" exemption that has been given to many registered mutual fund dealers (who are primarily in, or affiliated with an entity that is in the business of an investment fund manager) since the start-up of the MFDA. These entities will need assurance that their existing exemption continues after the Proposed Rule comes into force, and to ensure this exemption continues, and also to lessen the burden on any new entity that may need this exemption in the future, we recommend that the "standard" exemption simply be codified into the Proposed Rule. At a minimum, the Proposed Rule has to exempt those who already have an exemption from this new section 3.2.

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12. **Exceptions for SRO Members (section 3.3)**

While we agree with the exemptions provided for SRO members set out in section 3.3 of the Proposed Rule, we believe that the list of exemptions does not go far enough. Given that the SROs have extensive rules regarding complaint handling, KYC, referral arrangements and record-keeping and record retention, we believe that exemptions should also be granted in these areas. In our view, given the overall complexities of the Canadian regulatory regime, industry participants should not be required to review two sets of regulations on the same subject area in order to determine appropriate compliance.

13. **Advising Representatives (sections 4.11 and 4.12 of the Proposed Rule)**

We acknowledge favourably the amendments proposed by the CSA with the term "relevant investment management experience" used in both sections 4.11 and 4.12 of the Proposed Rule, along with the explanation as to what this experience might entail contained in section 4.4 of the Proposed Policy.

We believe that, while helpful, the Proposed Policy discussion does not go far enough, particularly for individuals who seek to be registered as an advising representative or associate advising representative so that they can provide client relationship services to the adviser. These individuals often have a strong marketing and people management and service focus, coupled with strong securities/economic/finance knowledge and background, but may not have the traditional (classical) proficiency required for registration as advising representatives. These individuals generally provide a combination of services to clients of the adviser; some that would bring them into the realm of "advising" and others that do not. In the past we have experienced a great deal of difficulty in actually getting these individuals registered in an advising capacity since they have different skill sets than individuals who qualify as advising representatives and often do not possess the mandatory educational requirements. It is often difficult to shoehorn these individuals' unique skills and experience into the advising representative or associate advising representative categories. In any event they are often not really providing "advice" in the *classical* sense, since they do not manage a portfolio and really do provide "relationship management" services.

In order to account for the above issues, we recommend that section 4.4 of the Proposed Policy include in the discussion of "relevant investment management experience" the following concepts:

(a) For associate advising representatives performing client relationship functions, it will be sufficient if they have experience similar to that outlined in the second and third bullets under the discussion of "relevant experience" as used in section 4.4(2). In our experience, many client relationship managers gain their experience and skills necessary to be successful in the role of client relationship managers in this context.

(b) For all advising representatives, recognition that relevant investment management experience includes working in an advising capacity with another adviser, <u>including as an associate advising representative or client</u>

relationship manager. This latter point is very important and is currently embodied in existing regulation and should be carried forward.

(c) For all advising representatives, recognition that relevant investment management experience includes research and analysis of fixed income securities and investment fund securities, as well as equity securities. We, together with our clients, have spent countless hours explaining to registration officers at the various securities commissions that this type of experience is just as valid to demonstrate proficiency, as research and analysis of equity securities. We recommend this be clearly stated in the Proposed Policy.

14. Advising Representatives (sections 4.11 and 4.12 of the Proposed Rule)

Certain of our clients have asked us to urge the CSA to entrench in the Proposed Rule, the proficiency exemptions that have been granted by certain members of the CSA to allow an individual who has a Masters of Business of Administration from an accredited school of business and the requisite work experience to become registered as an associate advising representative, without necessarily having a full CFA. Certain members of the CSA have granted these exemptions where the individual holds an MBA, but not a CFA, and has the required work experience. Our clients believe it is justified for the CSA to codify these exemptions into the Proposed Rule.

15. **Investment fund managers – chief compliance officers (section 4.15) – *Drafting comment***

We appreciate the attention paid by the CSA to our earlier comments about the need for tailoring of the proficiency requirements of a CCO of an investment fund manager so that the experience of these individuals with the investment fund manager is appropriately recognized. However, we believe that the reference to "registered" in section 4.15(b)(iii) is incorrect, given that no investment fund manager is today "registered" in that capacity. As drafted, no-one would be able to rely on this provision. We note this reference is not found in section 4.15(a)(iii), which we believe is correctly drafted.

16. **Capital requirement – Investment fund managers (section 4.18)**

(a) We note that the CSA appear to have responded to one of our comments made in our comment letter on the first version of the Proposals regarding Line 9 – Less Market Risk proposed in proposed Form 31-103F1 – Calculation of Excess Working Capital. We suggested that using the IDA margin rules would not necessarily provide an accurate assessment of market risk. We were unable to find where this comment was specifically responded to by the CSA in the Summary of Comments, but we note that the Form now describes the different margin rates that the CSA wishes registrants to use in calculating excess working capital. We were unable to find any explanation about the margin rates proposed by the CSA and urge the CSA to provide this explanation. For example, why are public

mutual funds being margined at 50 percent of their value? This would appear to be a very arbitrary determination of market risk.

(b) Our clients are confused about what information to include in response to Line 11, which requires inclusion of total amounts of guarantees. We believe this should be modified to require inclusion of only the amounts that are due in any particular year – it does not seem reasonable to include the full amounts guaranteed, if the guarantee could not be called upon in a year for this full amount. Our clients are also unclear about where letters of credit fall in this working capital calculation, as well as guarantees given by one registrant to another affiliated registrant's debt. It does not seem reasonable to have to include the debt for one registrant, as well as the guarantee of that debt by the other registrants. The Proposed new Form must also take into account the recent accounting changes which requires companies that provide guarantees to account for the fair value of the guarantee on their balance sheets. Our clients have explained that it would be double counting to also have to include this guarantee on the Form when calculating excess working capital.

(c) If the CSA retain the concept of "market risk" and the margin rates indicated, we recommend that portfolio managers and investment fund managers be permitted to include the investments that they have in their proprietary investment funds for the purposes of computing capital adequacy. Schedule 1 refers to "public" mutual funds; we recommend that this be amended to include all investment funds, whether public or private. Please see comment 292 in the Summary of Comments. We do not understand, or agree with the CSA's explanation of earlier comments to this effect found in comment response 596. There is absolutely no difference between the market risk in a public mutual fund and a pooled fund (a privately placed mutual fund), nor are there any liquidity risks, given that the nature of a mutual fund is that it is redeemable on demand.

17. **Delivering financial information – investment fund manager (section 4.30)**

We continue to believe that there is no regulatory principle behind the specific and different regulatory filings and requirements that apply only to investment fund managers in light of the other regulation that applies to investment funds and their managers, including:

(a) annual and quarterly NAV adjustment reports

(b) annual and quarterly financial statements and

(c) annual and quarterly working capital calculations.

We do not understand the additional risks that apply to investment fund managers (again given the other extensive regulation of investment funds and their managers) that would justify the additional quarterly reporting that does not exist for registered advisers.

Given that, for the large majority of mutual fund managers in Canada, calculation of NAV is outsourced to a small number of major service providers, we recommend that a better explanation of what the CSA will consider constitutes a "NAV adjustment" requiring reporting to the regulators be included in the Proposed Policy. Certainly, it would be in order to provide for a materiality or reasonableness standard for this reporting, which the CSA appears to agree with (see comment 325 in the Summary of Comments). We strongly recommend that the CSA explain what they will do with these reports – will they be public documents? Who will be reviewing them? Where will they be maintained? Although the CSA respond to these comments in the Summary of Comments (at 322 and 325), we believe that it would be in order for the CSA to provide a more complete discussion of these issues in the Proposed Policy.

We strongly recommend that the CSA consult with the fund industry and the applicable service providers on the issue of reporting of NAV adjustments before finalizing this particular rule.

18. **Preparation of financial statements (section 4.32)**

We described in our comment letter on the first version of the Proposals that submitting unconsolidated financial statements for advisers and dealers (non-SRO) may prove difficult, in particular for many offshore registrants. We recommend that the Proposed Rule allow consolidated audited statements to be provided, together with the unaudited financial statements of the relevant operating registrant that have been reviewed by auditors. We made this comment in our comment letter on the first version of the Proposals, but are unable to find where the CSA responded to it, although the CSA allude to unconsolidated statements in comment 327 of the Summary of Comments. We do not feel that this comment response addresses our earlier comment.

19. **Know Your Client (section 5.3)**

(a) Notwithstanding the CSA's partial response to our earlier comment on paragraph 5.3(1)(b) [comment response 346], we continue to assert that a mutual fund dealer or a scholarship plan dealer should not have to "ascertain whether a client is an insider of an issuer", given the nature of the securities these dealers distribute. This comment is particularly relevant since the CSA changed this requirement from "reporting issuers" to any "issuer". We submit that regulation should not require collection of irrelevant information from investors that have no bearing on what a dealer and its representatives will or will not recommend to those investors. To do so only achieves greater regulatory burdens and increased costs.

(b) Subsection 5.3(4) of the Proposed Rule will require a registrant to take reasonable efforts to keep the information required under section 5.3 "current". Notwithstanding the additional discussion about this concept in section 5.2 of the Proposed Policy, we believe this subsection does not add anything to the new inclusion of paragraph 5.3(1)(c) and therefore should be deleted. To leave in subsection (4) will invite confusion.

(c) We note that the additional flexibility given to registrants who deal with permitted clients contained in subsection 5.3(5) will not apply, in our view, erroneously, to registered mutual fund dealers or investment dealers who are SRO members. Given that section 5.5 does not apply (through the operation of section 3.3), these dealers cannot take advantage of the flexibility contained in subsection 5.5(3), which means that (from a drafting perspective) subsection 5.3(5) cannot apply. We urge the CSA to redraft this provision to permit dealers that are members of SROs the same flexibility when dealing with permitted clients that other dealers have.

We have heard that the IDA plans to revise IDA Policy 4 to permit certain institutional clients to waive suitability, but not all clients that would fall within the definition of "permitted client". We see no difference in principal between an SRO-dealer and a non-SRO dealer in this regard and urge the CSA to ensure consistent regulation amongst dealers in this area.

(d) We do not understand why the Proposed Rule is not harmonized with the rules of the SROs. We know that the IDA has already published proposed new rules relating to KYC and suitability and that the MFDA is planning to publish its proposed rules. We do not understand why three regulatory bodies are separately devising rules in these areas without any attempt (or any attempt that has been made public) to harmonize those rules. This is another example of a lack of uniformity that does not serve to advance the efficiency of the Canadian capital markets.

20. Providing relationship disclosure information - SROs (section 5.4)

In our view, the CSA must ensure that the SROs' versions of proposals designed to implement the client relationship model, including the RDI, is consistent with that being proposed by the CSA. We do not understand why clients should receive a different experience depending on which registrant they decide to work with. We believe that it should be the CSA that maintains ultimate control over the proposals of the SROs – this responsibility should not rest solely with the regulated self-regulatory association.

We are disappointed that we have not had the benefit of reviewing the MFDA's proposals for implementing the client relationship model before being required to submit our comments on the Proposals.

21. **Providing relationship disclosure information – Specific Comments (section 5.4)**

In our comment letter on the first version of the Proposals, we recommended that the CSA consider how the RDI fits with the equity disclosure requirements presently provided for in National Instrument 81-105. We recommend that the RDI take the place of these disclosure and consent requirements, given the technical difficulties experienced by many in the industry with NI 81-105, particularly with keeping up with changes in share structures and obtaining client consent prior to putting through a trade. We do not see where the CSA responded to this comment in the Summary of Comments.

We strongly recommend that subsection 5.4(7) be expanded to exempt any registrant who deals with a permitted client from having to provide that client with RDI. We fail to see any difference in regulatory principle between an EMD and any other registrant in this regard.

22. **Section 5.7 – Margin**

We were unable to find any explanation from the CSA on their regulatory intentions behind proposing this section. We understand from various CSA staff presentations that the CSA have determined that EMDs should not trade in securities where leverage is an investment feature. We have not found this restriction in any provision of the Proposals. Does the CSA believe that this section would prevent an EMD from so trading? If so, we find the section quite non-transparent as to this meaning and in our view, an EMD would be justified in not understanding this section would restrict these trades. We also point out, that if the CSA so intend this restriction for EMDs, section 5.7 is written as applying to all registrants (non-SRO members). We urge the CSA to (i) clarify that section 5.7 is not intended to go so far as to deal with the financial products that registrants deal with for their clients, (ii) if considered necessary, provide a specific rule that would prevent EMDs from trading in leveraged products and (iii) confirm that this latter specific rule does not apply to other registrants.

23. **Records – general requirements and Records – form, accessibility and retention (sections 5.15 and 5.16)**

Paragraph 5.16(4)(b) imposes a requirement to maintain documentation for seven years from the date a client "ceases" to be a client. Dealers who operate in client name will find this concept difficult and will benefit from a definition of when a "client" ceases to be a client. The definition should be based on activity or contact between the dealer/representative and the client and not on receipt of compensation (e.g. trailer fees) from the fund managers.

We urge the CSA to provide guidance around record keeping in respect of electronic mail and other recent technological forms of communication. We understand the SEC is currently clarifying this in the United States.

We made the above-noted comments in our 2007 comment letter to the CSA, but were unable to find where these comments were responded to, so we have raised them again, given that no changes were made in response to them.

24. Statement of Accounts and portfolio – (section 5.22)

The requirements for quarterly statements of account are new requirements that will impose significant additional burdens on dealers, primarily mutual fund dealers and scholarship plan dealers, that are not justified in the circumstances, particularly where those dealers have provided their clients electronic, pass-word protected access to their accounts on a real-time basis. These dealers currently mail out annual statements of account (mutual fund dealers also send quarterly statements to clients whose securities are held in "nominee name" under the rules of the MFDA), which we expect are retained by investors, together with their confirmation of trades and their account documentation.

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In response to similar comments made by industry participants on the first version of the Proposals, the CSA explain that they "disagree" and that quarterly reporting "is a reasonable standard". We urge the CSA to reconsider this point having regard to the regulatory burden and the lack of a demonstrated need for this increased reporting. Mailing three additional statements of account to the thousands of investors can be expected to cost in the neighbourhood of $200,000++per annum for firms, which we believe the CSA would agree is not an insignificant amount and would impose significant regulatory and environmental burdens on the financial services industry. We ask the CSA to consider whether this increased cost (which will be borne either by industry participants or investors) is justified in the context of these dealers and their investors.

25. **Ultimate designated person – functions and Chief Compliance Officer – functions (sections 5.24 and 5.25)**

We urge the CSA to clarify that the same individual can act as the CCO for registrants that are affiliated where regulated functions are separated out into separate corporations. Given the registrants' close affiliation, we believe this clarification is vital. We see nothing in the Proposed Rule that would prevent this, but given our understanding of staff's administration of the current CCO rules and the reference in section 2.9.2 of the Proposed Policy to "case-by-case" applications for relief, we believe that we would benefit from a clear statement of regulatory intention that this will be permitted. In considering this comment, we point out that section 6.3 would appear not to prevent one individual from being the CCO of affiliated registrants.

26. **Complaints Handling – Division 7 (sections 5.27-5.32)**

We expect that questions will arise as to when a complaint arises and when it can be said to be resolved. For example, if a registrant concludes that there is no wrongdoing on its part and informs a client of its conclusion, is this complaint resolved? Absent a client taking a positive action to indicate agreement with the conclusion - something that we see as unlikely - how will a registrant know if there is resolution? We believe that once a registrant has come to some conclusion which does not entail the acceptance of a client's position and has informed the client of that conclusion, that should be seen as "resolution" unless the client advises in writing within a specific time period of his or her intention to take further action or steps with regard to the complaint.

We continue to be very concerned about section 5.30 of the Proposed Rule. For non-SRO members, what dispute resolution service does the CSA expect registrants to "participate in"? This is a very vague, unexplained proposed rule that will have far-reaching implications. In our view, considerable additional consultation is required before implementation of this proposed rule.

What will the regulators do with the complaint handling reports sent in (presumably in paper form) to each regulator where the registrant is registered? This question should be answered by the CSA in the interests of transparent rule making.

We made these comments in our 2007 comment letter, but were unable to locate where the CSA responded to them. We are raising these comments again given their importance to our clients and the fact that the rules remain essentially unchanged.

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27. **Notice to Clients (section 5.33)**

Section 5.33 applies to "registrants", which will include investment fund managers. It is not clear to us what this provision is intended to achieve, particularly given that many managers of investment funds will only be registered in Ontario. Does the CSA expect investment fund managers to send to "each client" [each investor in a fund] a written notice? If this is considered important by the CSA, we recommend that this kind of notice be incorporated somehow into RDI (although we recognize that investment fund managers are exempt from having to prepare RDI). Without some modification, we believe section 5.33 will impose completely unnecessary and unjustified burdens on registrants, and particularly on investment fund managers.

28. **Identifying and responding to conflicts of interest (section 6.1)**

While we agree with subsection 6.1(4), we believe it must also exempt advisers who act as advisers or sub-advisers to investment funds subject to NI 81-107. These entities are swept into the ambit of NI 81-107 through the definition of "entity related to the manager" contained in NI 81-107. Given the different phraseology used in section 6.1 from that used in NI 81-107 (which we believe in itself is not desirable), we believe industry participants must clearly understand what rules apply to them or not.

29. Prohibition on Certain Managed Account transactions (section 6.2)

Section 6.2 of the Proposed Rule appears to be a revision to section 118 of the Ontario Securities Act and the equivalent provision in other securities legislation. However there are differences between the two pieces of regulation.

We appreciate that the Ontario government proposes to delete section 118 from the Ontario Securities Act, but we question whether the other provincial legislators have done the same. Unless the equivalent legislation is deleted, we believe that the Proposed Rule should exempt industry participants from the applicable legislation if they comply with the Proposed Rule. It will be very difficult, from a compliance perspective, to have a duplicate rule contained in a regulatory instrument that is differently drafted or even the same as a legislative provision.

While we believe that the drafting of section 6.2 is much improved in this version of the Proposed Rule, we continue to note several flaws with section 6.2:

(i) Investment fund managers and mutual funds are not exempted from its scope as applicable, in ways dealt with in National Instrument 81-107. Does this mean that if an investment fund manager and/or a fund has an exemption under NI 81-107 from securities regulation that it must again apply for an exemption under section 6.2 of the Proposed Rule? This would not be a good result. We do not believe the CSA addressed this comment, other than by saying that these issues would be dealt with in revisions to NI 81-107. Given that these revisions have not been published for comment (which we believe would be essential under rule-

making), we recommend that this exemption be provided for in the Proposed Rule.

(ii) Similarly, if a registrant has already been exempted from section 118 (or equivalent section in other applicable legislation) in respect of a continuing activity, will it have to re-apply for an exemption from section 6.2? Given the length of time that section 118 has been in effect (several decades), it is critical that the CSA provide blanket relief from this section to any registrant who has relief from the equivalent provisions of securities legislation.

(iii) Paragraph (c) could, in our view, be more concisely drafted (as drafted it is confusing and mixes concepts that fall within the same definition). We believe this paragraph should read:

"purchase or sell a security from or to another investment portfolio managed by the adviser *[we recommend this term stay in for clarity, although its redundant given the definition of responsible person]* or a responsible person."

30. **Prohibition on Certain Managed Account transactions (section 6.2) – Cross-Trading/Inter-fund Trading**

As noted in the 1995 OSC staff paper on Conflicts of Interest, it has always been unclear the extent to which 118(2)(b) and the equivalent provisions in other securities legislation captures "inter-fund" trading (internal trading of securities between two or more investment funds) and "cross-trades" (trades made by a portfolio manager of securities between two of its managed portfolios, including two or more investment funds where those trades are placed with a registered dealer who carries out those trades on an exchange or other marketplace). This is a very significant issue for the investment fund and portfolio management industry.

We believe that it appears that section 6.2(c) is intended to cover inter-fund trading. What about trading between two portfolios that are not investment funds? This is not today prohibited under any regulation to our knowledge. We are concerned that the language is so broad in section 6.2 that it will capture transferring securities from one client portfolio to another, which we understand is a common practice for portfolio managers, since it is efficient and cost-effective for the client, particularly in the case of smaller holdings.

What about cross-trades? If cross-trades are caught, why? And if so, how?

The inter-relationship of section 6.2 with NI 81-107 is of critical importance here. We do not see where the CSA addressed this comment in the Summary of Comments (other than to describe it in comment 471).

We strongly recommend that the CSA conduct additional consultation with the investment management industry on inter-fund trading and cross-trading before formulating a final rule in this area. We would be pleased to provide the CSA with further feedback, including our clients' experience with NI 81-107 and the inter-fund

trading rules contained in that instrument. In our experience, there is much confusion amongst the industry and also within the CSA on the appropriate interpretation of section 118 and its relationship with section 6.1 of NI 81-107. We recommend that the CSA specifically indicate that section 6.2 of the Proposed Rule is not intended to restrict cross trades or inter-fund trades at this time – and that the CSA conduct further consultation with the industry on the appropriate regulation (if any) of this practice.

31. **Issuer Disclosure Statement – (section 6.4)**

We appreciate that the CSA dealt with many of our comments on the previous version of section 6.4 and responded to our comments in comment response 479. The response of the CSA is to the effect that section 6.4 was redrafted to accommodate our comments. We do not believe that the CSA has addressed all fundamental issues we (and other commenters) raised.

In our earlier comment letter, we strongly recommend that section 6.4 be redrafted to provide the following:

(i) Account opening documents must clearly disclose the possibility of a portfolio manager causing a client to invest in a "related issuer" and outlining the general reasons why an issuer may become a related issuer to the portfolio manager. In our view, section 6.4(1) does not address this proposal.

(ii) Clients will consent to the portfolio manager causing them to invest in related issuers as part of their general discretion given to portfolio managers at account opening. In our view, section 6.4(1) does not address this proposal.

(iii) Clients will receive a list of related issuers when they enter into an account, and a revised, updated list of related issuers on an annual basis. The concept of an annual revised updated list has not been brought forward into section 6.4. Instead the CSA have retained the very difficult and simply impractical and costly approach of requiring portfolio managers to contact clients describing a new related issuer every time this relationship threshold is tripped or materially changed, before being able to invest client's assets in that related issuer. In any event, we expect that clients will not appreciate, or know what to do with, the regular paper flow of information proposed to be mandated in section 6.4.

We do not understand the rationale behind subsection (7) and feel we, and the industry would benefit from a more complete discussion about what this exemption will mean for a portfolio manager.

32. International dealer (section 8.15)

We have two comments on section 8.15 as it relates to international dealers:

(a) The definition of "international dealer" should recognize the fact that the dealer may be "exempt" from registration as a dealer in its home jurisdiction. This is the case for "international advisers" and this reality should be reflected in the definition of international dealers.

(b) The permitted activities of an international dealer should be at least consistent with the current international dealer activities permitted under section 208 of the Regulation made under the Ontario Securities Act. An international dealer should be permitted to engage in <u>any trading</u> in Canada with a registered investment dealer.

33. **International adviser (section 8.16)**

We support the introduction of the concept of "permitted clients" and the exemption provided for in section 8.16 for international advisers who act as "advisers" in a Canadian jurisdiction to "permitted clients". However, as a critical matter, this exemption must be expanded to exempt these entities from having to be registered as "investment fund managers" if they happen to manage an investment fund that is established in Canada (generally for tax or marketing reasons) and they only distribute those securities to permitted clients. Currently many of our international adviser clients that advise primarily institutional clients based in Canada have set up investment funds in Canada (pooled funds). The only purpose for establishing these pooled funds was to package their advice to institutional clients into an efficient and more diversified model. Without an expansion to the exemption, there would be an odd result in that these international advisers dealing with only permitted clients would be permitted to give up their current adviser registrations only to have to assume an investment fund manager registration. Also, as they have no head office (or really any office) in Canada it is unclear as to which province they would be required to registered as an investment fund manager. This would seem to be an inadvertent and unforeseen result and we urge the CSA to provide an exemption from having to hold this registration on similar grounds as contained in section 8.16.

34. Exemptions for Sub-Advisers (section 8.17)

We recognize that section 8.17 of the Proposed Rule codifies exemptive relief that has been regularly provided by the CSA in recent times, although this relief has not been required in Ontario or Quebec. We continue to strongly object to the continued "opt-out" from the Manitoba Securities Commission provided for in subsection 8.17(f). We see absolutely no regulatory rationale for the MSC continuing to insist on this condition, which is particularly burdensome, embarrassing (to all Canadians) and surprising given the CSA's (including the Chair of the MSC) efforts to inform the Canadian marketplace about the benefits of the Passport System. We do not view the MSC's response to this comment made in our comment letter on the first version of the Proposals (at comment 558) to be meaningful.

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35. **Mobility Exemptions for Dealers and Advisers (Division 2 – Mobility Exemptions of the Proposed Rule)**

In our view, the proposed mobility exemptions for dealers and advisers do not reflect the realities of a more mobile Canadian population or the efforts of the CSA to implement a Passport System and will not significantly reduce the regulatory burdens of having to become registered in multiple provinces where clients reside.

In our view the restrictions on the availability of this exemption, particularly for mid-to-large registrants are patently too onerous and without reasonable practicality. For a dealer registrant with over a hundred sales representatives to consider that the exemption would only apply if 10 or fewer clients move to a particular province is not meaningful. And a successful sales representative to be capped at five clients moving to a particular province, is also not realistic or meaningful.

We also urge the CSA to review the complexities proposed that are associated with using this exemption. Are all of the filings, forms, and notices really necessary in light of (i) the Passport System and (ii) a more mobile Canadian population?

In our view, the same rationale should apply to U.S. registered investment advisers who happen to be advising a U.S. client who moves to Canada. The same conditions can be said to apply to this U.S. registered investment adviser, which will permit the former U.S. resident to enjoy continuity of service while living in Canada, and at the same time, reduce the regulatory burden on that investment adviser. Investor protection will not be compromised. We fully understand that this point raises issues of reciprocity for Canadian registrants into the United States.

We made these comments in our 2007 comment letter, but were unable to locate where the CSA responded to these comments.

36. **Definition of "permitted client" – (section 1.1)**

We recommend two clarifications to the definition of "permitted client" – both of which are critical.

(a) Paragraph (k) of the definition refers to an investment fund that is advised by a registered portfolio manager (Canadian registrant). In our view, this is too restrictive. Many Canadian mutual funds currently engage directly non-Canadian investment advisers to provide investment advice in respect of certain portfolios (or the entire portfolio). If this paragraph is not amended, such mutual funds would have to also engage a Canadian registrant or the non Canadian adviser would have to incur the disproportionate administrative burden of registering as a full portfolio manager as they would not be able to avail themselves of the international adviser exemption. Accordingly this paragraph should be revised to include an investment fund that is managed by a registered investment fund manager in one of the provinces or territories of Canada.

(b) Paragraph (o) should be expanded to include any entity that is equivalent to a corporation and that has the equivalent to shareholders equity in the stated amount.

(c) The definition should be expanded to also include as a permitted client an investment fund that distributes its securities only to other permitted clients. This amendment would be consistent with the current definition of an international adviser under OSC Rule 35-502.

37. **Comment on Asset Allocation**

The CSA have removed references from the Proposed Policy that were in the 2007 version of the Proposed Policy that gave the CSA's views on when "asset allocation" would cross the line into being "in the business of advising" in securities, requiring an entity that purported to provide asset allocation advice to a client to be registered as an adviser. In our view, the CSA's views should be provided so that industry participants can fully understand when they will be subject to securities regulation. We strongly recommend that the CSA continue to consult with industry participants about this issue. We would be pleased to meet with the CSA to discuss this issue.

38. **Transition – Generally**

There is considerable confusion about the transition requirements and what the CSA will expect of current registrants and new registrants when the Proposed Rule comes into effect. We outline some specific comments in the comments that follow, but we urge the CSA to clarify:

(a) What they mean by their statements in comment response 665? These statements are, to our knowledge, not incorporated into the transition rules or in the other amended rules. We strongly recommend that this approach (which we don't disagree with) be written clearly into the applicable rules and explained clearly by the CSA. If this is indeed the approach to be taken, then our comments set out below may not apply.

(b) What will happen to international advisers who are registered either as international advisers (in provinces that have this category) or as full advisers? We have not found any discussion of this issue in the February 2008 publications. We urge the CSA not to assume that all such registrants will drop such registration in order to rely on the exemption for international advisers. We know that some of our international clients (particularly those currently registered in the category of "non-Canadian adviser in Ontario) may intend to retain their full advising status in order to manage assets of clients who are not permitted clients or to advise on Canadian securities. We would be pleased to discuss this issue more completely with the CSA in order to develop a practical and

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efficient process for ensuring these registrants don't suddenly lose their registration necessary to carry on their business in Canada.

39. Part 10 – Transition – Investment Fund Managers

(a) We are not clear (notwithstanding section 10.3 of the Proposed Rule) when the capital and insurance requirements will apply to a **new** applicant for registration as an investment fund manager. There will be circumstances where an entity will apply for registration that has never been registered before and is not registered in any other capacity at the time of application. Subsection 10.3(2) speaks of "registered" dealers or "registered" advisers and gives these entities six months from the coming in force of the Proposals to come up with the increased capital and insurance coverage. We believe it would be consistent with this concept to allow a previously unregistered entity to *apply* for registration without the requisite capital or insurance. The firm would have to have the additional capital and insurance at the time the principal regulator is ready to grant the registration or on a date that is one year after that application, whichever is later. We note that section 4.18 and 4.23 only applies to "registered" investment fund managers in any event, which we believe is consistent with our interpretation.

(b) We also note that the fit and proper requirements, as well as the conduct rules also only apply once the firm is "registered". This is consistent with current regulatory practice, which means that none of the "investment fund manager" rules will apply to an unregistered fund manager until such time as it becomes registered. This is appropriate, given the fact that today all fund managers are operating properly without registration without cause for undue regulatory concern (given that the CSA have powers to do compliance reviews on these entities).

(c) We strongly encourage the CSA to consider a much more streamlined registration process for companies that are " in the business" of acting as an investment fund manager at the time the Proposals come into force. The proposed requirements for an application for registration have been substantially increased which will put additional regulatory burdens on capital markets participants at a time when they will be overburdened with the compliance issues associated with ensuring compliance with the new regime embodied in the Proposals. This has particularly resonance to investment fund managers that now must become registered. Some of these entities have been operating successfully and without regulatory cause for concern for decades. To pull together the new application filing package required of completely new, start-up entrants into the industry appears to us to be unduly burdensome to long-time compliant participants in Canada's capital markets.

40. **Part 10 – Transition – Applications for Registration as an EMD**

In light of subsection 10.1(2) it is not clear whether the OSC and the Newfoundland regulator expect a registered limited market dealer to apply (under section 10.4) for registration as an EMD. We urge the OSC and the Newfoundland regulator to clarify that no additional filing is necessary in those provinces if a mutual fund dealer is also registered as a limited market dealer at the time the Proposals come into force. We do not understand that there is any regulatory need for these already registered entities to be forced to apply for registration (when they are deemed to be so registered under subsection 10.1(2)).

We also strongly encourage the CSA to consider a much more streamlined registration process for companies that are "in the business" of dealing in exempt securities at the time the Proposals come into force, particularly for a registrant that is also registered in Ontario and Newfoundland as an LMD. The proposed requirements for an application for registration have been substantially increased which will put additional regulatory burdens on registrants wishing to continue their ability to trade in exempt products at a time when they will be overburdened with the compliance issues associated with ensuring compliance with the new regime embodied in the Proposals.

41. **Transition – Filing Deadlines (section 10.5 and 10.6)**

We urge the CSA to adopt uniform timing throughout this transition period. The one-month deadline for UDPs and CCOs to apply for registration in those capacities (and be grandfathered from the new proficiency requirements for CCOs) is unrealistic and unduly punitive for compliant registrants. Capital market participants will be fully engaged in continuing to understand the Proposals when they come into force, as well as considering what business changes they must implement in order to be compliant. Having to remember to file two applications for registration within one month of the Proposed Rule coming into force is not realistic or reasonable.

42. Comment on Proposed Form 33-109F6

We note that the CSA now propose to have new applicants submit a large amount of back-up documentation with their application for registration, including a five-year business plan, marketing materials, policies and procedures manual, account opening documentation, written policy on fairness allocation, employment/agency agreements, "client-related documentation" etc. We feel that this is a regressive step for the CSA to take. Unless the CSA staff are able to review this information on a timely and substantive (informed) manner, we feel it would be best to retain the existing requirements for registrants (and applicants for registration) to maintain this information, and have it available for review by compliance audit staff.

In addition, despite the CSA's response to comments made in connection with the first publication of the Proposals (at comment response 664), we are very concerned about the need for our clients to file full business plans and full compliance manuals with the regulators. As you can appreciate, these plans and manuals generally represent significant outlays of resources to develop and are considered proprietary and non-public documents. We recommend if the CSA continue to require these to be filed (which as

above we do not agree with), that the CSA permit applicants to file summaries of these documents for registration purposes.

43. **Comments on Proposed Form 33-109FI and Proposed Form 33-109F4**

In our 2007 comment letter on the first version of the Proposals, we provided comments on Proposed Forms 33-109F1 and 33-109F4 with a view to ensuring that they are consistent with reasonable practice and the other aspects of the Proposed Rule (as we have commented on it). We note that the CSA responded favourably to many of our comments, but we still have the following comments, which we submit again for the CSA's consideration as we believe our earlier comment was not addressed adequately.

We note that the term "national registration database" used in both Forms should be capitalized to "National Registration Database".

Our comments on Proposed Form 33-109F1 are:

(a) *Part E – Further Details (Form 33-109F1):* In our view, completion of the "Further Details" section should not be required unless an individual was dismissed or resigned for cause. Where an individual has resigned or was dismissed without cause (i.e. – simply moved on to another job or was downsized), the litany of checkboxes that are required to be filled out by the sponsoring firm are intrusive and unnecessary. We also believe many of the questions are vague and subjective and hence will be very difficult to answer. We note that there are consequences for providing incomplete or erroneous information in regulatory forms and therefore, in our view, the questions must be completely clear and understandable and capable of a definitive answer.

(b) *Part E – Section 8:* Again, in addition to the more general comment above, we believe the concept of "demonstrating a pattern of failing to follow compliance policies and procedures" is particularly vague and confusing and, in our view, will be very difficult to answer.

Our comments on Proposed Form 33-109F4 are:

(c) *Item 1, #3 – Business Names*: We recommend that this section would be better found in the Current and/or Former Employment sections. It is confusing to have questions regarding carrying business under any other business names on a form that is for the registration of individuals.

(d) *Item 13 – Regulatory Disclosure:* We recommend amending the definition of "derivatives" now found at the top of the Form to mean "financial instruments such as commodity futures contracts, exchange contracts and swaps whose market price…". We recommend removing the word "options" from this definition, as an "option" is already included in the definition of "security" in the *Securities Act* (Ontario). It would therefore be redundant in Item 13(1)(a) to ask whether an individual has been

registered or licensed to trade in or advise on securities (including options) or derivatives (including options).

(e) *Item 16 – Financial Disclosure:* In question #2 – Debt Obligations, we recommend clarifying the threshold level for disclosing the failure of a firm ("of which you were an officer, partner or director") to meet a financial obligation. That is, does the question ask whether you have, or any firm of which you were an officer, partner or director has, ever failed to meet a financial obligation of $5,000 or more; or does the question ask whether you have ever failed to meet a financial obligation of $5,000 or more, or has any firm of which you were an officer, partner or director ever failed to meet *any* financial obligation (i.e. – even an obligation for, say, $10)?

(f) *Schedule "A":* With respect to the "business names" that are required to be provided, please see our comment #2, above.

44. Revocation of OSC Rule 35-502 *Non-Resident Advisers*

We recognize that OSC Rule 35-502 *Non Resident Advisers* will be revoked since some of the provisions will be built into the Proposed Rule and other provisions will no longer be necessary since the flow-through analysis will no longer be applied in Ontario. However, certain of the provisions in OSC Rule 35-502, such as section 7.2 (Commodity Pool Programs) and section 7.6 (Advising Pension Funds of Affiliates) are still necessary yet have not been built into the Proposed Rule.

We urge the CSA to retain these exemptions and build them into Part 8 of the Proposed Rule. In our view, these exemptions are being relied on by market participants and are still necessary.

45. OSC Fee Rule – OSC Rule 13-502

(a) In our 2007 comment letter, we asked the OSC to amend its Fees Rule where they purport to charge regulatory participation fees to unregistered international fund managers. Given the amendments made to the Proposed Rule that would not require international fund managers, who distribute securities of their non-Canadian funds in Canada pursuant to prospectus exemptions to be registered and the clear rejection by the CSA of the OSC's "look through" principle, we urge the OSC to make these amendments now. Please see our earlier comment letter on OSC Rule 13-502 *Fees* that we attached to our 2007 letter. Given our views contained in that letter and as outlined in this comment letter, we again strongly recommend that the OSC amend the Fees Rule to remove the requirements for payment of participation fees by international fund managers. We do not see where the OSC responded to this comment made in our 2007 comment letter.

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(b) In addition and for the same reasons as set out above, we strongly recommend that the OSC not move forward with proposed amendments to the Fee Rule which would purport to require those international advisers and dealers who are availing themselves of the registration exemptions provided for in the Proposed Rule, to also pay participation fees to the OSC. Among other things, in our experience, this kind of rule (for unregistered non-Canadian market participants) will be extremely difficult to enforce and virtually impossible to monitor.

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We thank you for allowing us the opportunity to comment on the Proposals. Please contact the following lawyers in our Toronto, Vancouver and Montreal offices if the CSA members would like further elaboration of our comments. We, together with other BLG lawyers who contributed to this letter, would be pleased to meet with you at your convenience.

- Prema K.R. Thiele (Toronto office) at 416-367-6082 and pthiele@blgcanada.com
- Rebecca A. Cowdery (Toronto office) at 416-367-6340 and rcowdery@blgcanada.com
- Jason J. Brooks (Vancouver office) at 604-640-4102 and jbrooks@blgcanada.com
- Francois Brais (Montreal office) at 514-954-3143 and fbrais@blgcanada.com

Again, we commend the CSA on the work done to date and urge the CSA to complete the registration reform initiative in ways that achieve complete national uniformity of applicable rules and that recognize the national scope of most Canadian capital markets industry participants.

Yours truly,

"SECURITIES AND CAPITAL MARKETS PRACTICE GROUP"

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COPY OF ORIGINAL EMAILED TO ONTARIO MINISTRY OF FINANCE

May 29, 2008

Via Email

Ministry of Finance
95 Grosvenor Street, 4th Floor
Toronto, Ontario
M7A 1Z1

Attention: Colin Nickerson
Senior Manager
Industrial and Financial Policy Branch

Dear Sirs/Mesdames:

Re: Proposed Amendments to the Securities Act – Consultation Draft and Invitation for Comments dated April 25, 2008

We are pleased to provide the Ministry of Finance with comments on the above-noted proposed amendments to the Securities Act (the Proposed Legislation), which are designed to come into force at the same time as the proposed new rule of the Canadian Securities Administrators – National Instrument 31-103 *Registration Requirements*. Our comments incorporate comments that we have made to the CSA on proposed National Instrument 31-103 and we attach, for your information, the letter that we have now sent to the CSA on proposed National Instrument 31-103.

Our comments are those of lawyers in BLG's Securities and Capital Markets practice group and do not necessarily represent the views of individual lawyers, the firm or our clients, although we have incorporated feedback received to date from certain of our clients into this letter. Please note that this letter is in addition to the letter that we signed as members on the OSC's Securities Advisory Committee and elaborates on the same and additional matters.

We fully support the goal of the Ontario Securities Commission, and the other members of the CSA, with the overall Registration Reform Project: to harmonize, streamline and modernize the registration regime across Canada and to create a flexible and administratively efficient regime with reduced regulatory burden.

To the extent that National Instrument 31-103 will create a nationally uniform set of rules that would govern the "fit and proper" requirements and conduct rules for registrants, as

well as any applicable exemptions for specified industry participants, we believe that National Instrument 31-103 is a very positive regulatory development. Today, in order to properly advise our clients, we must keep track of not only differing rules in the various provinces that apply to the same activity or registrant, but even more troubling, different interpretations and methods of administering regulations, rules and legislation that may be substantively the same in each province. Today's regulatory regime creates inefficiencies, regulatory burdens and increased costs for our clients that are unjustified in the context of the Canadian capital markets.

Legislative Approach

2. We are troubled by the approach taken by the Ontario government in building into legislation matters that the other provincial governments appear content to leave up to the securities regulatory authorities. As far as we are aware, the Ontario government has not explained the reason it believes it needs to do this. However, we assume that the approach is based on a view that certain provisions are so important that they should be in the Act and not the regulations or rules. While we understand this approach in theory, we suggest that most of the provisions that the Proposed Legislation would duplicate (in proposed National Instrument 31-103) are not of this nature or importance. In our view, all that really must be provided for in the Act is the requirement to register (and the related definitions) and the ability of the OSC to make the necessary rules to implement these requirements.

   We believe that the approach taken by the Ontario government is a regressive step and will significantly detract from the above-noted goals of a nationally uniform regime.

   The Ontario government's approach has necessitated the OSC to publish a revised version of National Instrument 31-103 indicating where the words "other than in Ontario" will appear in the final draft. We believe that the potential for a shift, over time, away from a uniform or even harmonized approach is considerable, given the ease with which other provincial regulators will be able to amend the rules and the comparative difficulties that the OSC will experience in requesting the Ontario legislature to amend the legislation to ensure that Ontario stays in step with the other members of the CSA. We point out below several areas where this approach may lead to potential difficulties and we urge the Ontario government to ensure that the legislation adopted is consistent in approach with the other provincial legislatures. In our view, there is no justification for the Ontario legislation to duplicate securities rules or to rephrase the securities rules using different language – we note several places where the Ontario government has chosen to entrench into legislation matters otherwise written into National Instrument 31-103, but using different terminology. We do not view this as a positive step forward.

   We note that this approach has been taken with respect to the take-over bid rules and certain aspects of the prospectus rules. We urge the Ontario government to reconsider this approach with respect to those provisions and amend the Act accordingly. Beyond the reasons given above, the inference that this approach

gives is that Ontario has to do things in its own way, which in turn leads other provinces to believe that Ontario would seek to dictate the terms of any national securities commission and any national securities laws. Therefore, in our view, this approach undermines the stated goal of the Ontario government to work towards a single national securities regulator.

We strongly urge the Ontario government to limit the legislative amendments to those set out under "Proposed Legislative Amendments" in the CSA request for comments on National Instrument 31-103 (except as may otherwise be helpful to clean up the Act) and in a manner consistent with the amendments to the legislation of the other provinces.

Definition of "representative"

3. We fully support the proposed change from the current definition of "salesperson" to the proposed definition of "representative". The proposed change clarifies that a representative of a registered dealer can be in a principal-agent (independent contractor) relationship with the dealer, in addition to a more traditional employment relationship.

In our comment letter on proposed National Instrument 31-103, we encourage the OSC and the other members of the CSA to continue to consider how best to allow for "incorporated salespersons", given the importance of this issue for dealers in their recruitment and retention of qualified advisors. Given that legislative solutions may be necessary, we urge the Ministry of Finance to work closely with the OSC to ensure that this matter is dealt with on an expedited time frame. This issue has become increasingly important to many registered dealers and individual representatives and we believe that an appropriate legal structure can be developed that will ensure appropriate investor protection, while also allowing increased flexibility and tax efficiencies for advisors.

In the interim until a definitive position is taken, we have also suggested that the CSA clearly permit, via National Instrument 31-103 or by some other mechanism, representatives of all registered dealers to direct commissions to be paid to their personal holding corporations. We know that the approach taken to this matter is not uniform across Canada, but given the importance of this issue, we have recommended that the CSA work to permit the most permissive scheme through amendments to National Instrument 31-103 (or by some other instrument). We believe that the approach recently adopted by the Manitoba Securities Commission is one that will work in practice, at least in the interim.

Engaged in a Business – subsection 25(6)

4. We have three comments on this subsection.

(a) Consistent with our first comment we believe it is completely inappropriate for subsection (6) to entrench into legislation the various factors that must be considered in an analysis of whether an entity is "in the business" of acting as an adviser or a dealer. In all of the other

provinces, we understand that the discussion on the meaning of "being in the business" is provided for in a regulatory statement of policy (i.e. in the Companion Policy). It is much easier to amend a companion policy than to amend legislation. We do not understand the rationale for entrenching these factors in legislation, even if the registration reform initiative were an Ontario-only project, and given the desirability for Ontario to stay in step with the other provinces, we recommend that this subsection be deleted and the OSC retain the jurisdiction to expand on the meaning of this term in conformity with the other provinces.

(b) We do not understand the intention of the Ontario government in listing various factors to be considered. If an entity met one factor, but none of the others, is that entity likely to be considered to be "in the business"? If the intention is that it is more likely that the entity is in the business of trading or advising if it hit an accumulation of factors, then we believe the drafting should reflect this. We believe that if an entity is trading or advising without any remuneration or expectation of profit (factor 2), that even if the entity hit the other tests, that entity should not be considered to be "in the business of trading or advising".

(c) Perhaps equally important, we believe that the narrative explanation of the factors that industry participants are to consider when making the critical determination of whether or not they are "in the business" of a regulated securities business contained in the proposed Companion Policy are far more complete and comprehensible than the list of factors proposed in the Proposed Legislation.

Dealer Registration Categories – section 26

5. In the interests of allowing future flexibility, we recommend that the Proposed Legislation not contain the table presently part of section 26(2) of the Proposed Legislation. We believe that it is not useful to have entrenched in legislation, the different categories of dealers and the permitted activities of these dealers. We believe that the future for the distribution of securities is fluid and that something so subject to potential change should not be entrenched in the Act.

   Again, our comment should be read with our first comment – it has not historically been the approach to include such detailed tables or even the list of categories in the Act.

6. In our comment letter on National Instrument 31-103, we urge the CSA to allow firms and their representatives that are registered as mutual fund dealers to be authorized to also distribute other forms of securities, including scholarship plans, exchange traded funds, exempt mutual funds and financial products that are not securities, such as GICs, principal protected notes and deposit accounts, without necessarily having to become also registered as scholarship plan dealers and/or exempt market dealers. In our view, the mutual fund dealer registration category should permit registered firms to distribute securities, whether on a public or exempt basis, where those products either do not fall within the purview of

securities regulators (GICs and PPNs) or have many of the same characteristics of mutual funds and are regulated as "investment funds", in ways similar to mutual funds. We believe that the regulatory oversight of mutual fund dealers, when coupled with the proficiency required of mutual fund dealer representatives, is sufficient to cover such securities and no additional registration or proficiency is necessary. This comment is relevant to the Ministry of Finance given the restrictions on the ability of mutual fund dealers embodied in the table contained in subsection 26(2). Even if the table is deleted from the final amendments to the Securities Act (which we recommend), we want to bring this issue to the attention of the Ministry of Finance, given its importance to Ontario investors and capital markets.

Duty to deal fairly, honestly and in good faith – section 32(3)

7. We are concerned about the proposal to impose a statutory duty of care on the Ultimate Designated Person and the CCO under Ontario laws. We are not aware of any other provincial government proposing similar legislation, nor do we understand that the securities regulators are taking this stance. This concept is not part of National Instrument 31-103. It is one thing for a securities regulator to explain that they believe that a CCO or UDP should consider that their firm has a fiduciary responsibility to clients (as well as the duty of care set out in National Instrument 31-103) in performing their duties, but it is quite another to say that these individuals must act in accordance with a statutory duty of care contained in legislation. In our view, if a statutory duty of care were imposed personally on UDPs and CCOs, there is a danger that qualified individuals would not wish to take on these responsibilities without significant reassurances as to their liability, which will impact on compensation and insurance costs for registrants, among other things.

   We are also not aware of any regulatory or governmental policy behind this particular proposal. What problem is this proposed legislation intended to solve? Why is this considered necessary for Ontario registered firms?

Trades by Mutual Fund Insiders – section 119

8. We recognize that the government proposes to replace existing section 119 with a new section 119 that is essentially the same, but for the new defined term "adviser", rather than "portfolio manager". We strongly recommend that the government consider updating this section to:

   (a) Delete the specific focus on "mutual funds" and leave the section to apply to all "investment portfolios managed for a client by an adviser". This term encompasses "mutual funds", as well as other investment funds and separately managed accounts managed by an adviser. We note that the term "portfolio securities" as used in (new) subparagraph (a) is defined to include current and future securities of a mutual fund which we believe is appropriate. We do not understand why this concept should not also apply to investment portfolios more generally managed for clients by advisers,

including non-redeemable investment funds and therefore a revised section should include this concept.

(b) Define more specifically what is meant by the phrase "access to information concerning the investment program". We believe this is an ill-defined phrase that can have an overbroad meaning, depending on how it is interpreted. We believe a better formulation of the concept would be to align it with various industry tests for who would be an "access person" for the purposes of personal trading policies. For example, in the Investment Funds Institute of Canada's Model Code of Ethics for Personal Investing (May 1998) the following definition is used: "a [person] who has, or is able to obtain access to, non-public information concerning the portfolio holdings, the trading activities or the ongoing investment programs of [funds]". We would substitute a concept of "participating in or being privy to the investment decision-making process" for the somewhat nebulous phrase "investment program".

(c) Define more specifically what is meant by the phrase "his, her or its direct benefit or advantage", which is another over-broad phrase that has led to confusion in the past. The above-noted IFIC code refers to "front running" as using knowledge of a fund's portfolio transaction to profit by the market effect of such transactions. We recommend that the over-broad words be replaced with a concept of benefits or advantage that are a direct result of the individuals' insider knowledge and that result in a detriment to the client.

Further, we also believe that this section would be better placed in proposed National Instrument 31-103, as then it would be a national rule with application across the country, which we believe is desirable. We recommend that section 119 be deleted from the Ontario legislation.

Exemptions from Registration Requirements

9. OSC Rule 45-501 removes the exemptions contained in sections 34 and 35 of the Act, as National Instrument 45-106 and OSC Rule 45-501 are designed to provide for a complete set of exemptions. It is unclear then why these sections should be amended to replace the exemptions stated therein and to what effect they would have (for example, would they supersede OSC Rule 45-501?). We recommend that sections 34 and 35 be replaced with what, in effect, you are proposing in sections 34(1)3 and 35(6). Section 35.1 is unnecessary because of the exemptions in section 3.7(a) of NI 45-106 and sections 4.1 and 4.5 of OSC Rule 45-501.

Other Recommended Changes

10. While the Act is being amended, we urge the Ontario government to take the same approach as we suggest for section 34 and 35 with section 72(1) to (7) and section 73, that is, simply to provide exemptions as prescribed in the regulations.

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Similarly, sections 75 and 77 to 86 can be deleted as they have been effectively superseded by National Instrument 51-102 and National Instrument 81-106.

Section 44

11. We fully support the proposed replacement of section 44, which is long overdue.

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We thank you for allowing us the opportunity to comment on the Proposals. Please contact the following lawyers in our Toronto office if Ministry staff would like further elaboration of our comments. We would be pleased to meet with you at your convenience.

- Paul G. Findlay at 416-367-6191 and pfindlay@blgcanada.com
- Prema K.R. Thiele at 416-367-6082 and pthiele@blgcanada.com
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Yours truly,

ORIGINAL SIGNED

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