



# Alternative Investment Management Association (AIMA)

The Forum for Hedge Funds, Managed Futures and Managed Currencies

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January 14, 2010

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Financial Services Regulation Division, Department of Government Services,  
Newfoundland and Labrador  
Superintendent of Securities, Northwest Territories  
Superintendent of Securities, Yukon Territory  
Superintendent of Securities, Nunavut

John Stevenson, Secretary  
Ontario Securities Commission  
20 Queen Street West  
19<sup>th</sup> Floor, Box 55  
Toronto, Ontario  
M5H 3S8

Dear Mr. Stevenson:

**Re: AIMA Canada's Comments on Proposed Amendments to National Instrument 81-106 Investment Fund Continuous Disclosure, National Instrument 31-103 Registration Requirements and Exemptions, and National Instrument 45-106, Prospectus and Registration Exemptions, and associated Companion Policies**

This letter is being written on behalf of the Canadian chapter (“**AIMA Canada**”) of the Alternative Investment Management Association (“**AIMA**”) and its members to provide our comments to you on the proposed amendments to National Instrument 81-106 *Investment Fund Continuous Disclosure* (“**NI 81-106**”), National Instrument 31-103 *Registration Requirements and Exemptions* (“**NI 31-103**”) and National Instrument 45-106 *Prospectus and Registration Exemptions* (“**NI 45-106**”) and their Companion Policies and supporting schedules (collectively the “**Rules**”).

AIMA was established in 1990 as a direct result of the growing importance of alternative investments in global investment management. AIMA is a not-for-profit international educational and research body that represents practitioners in hedge

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fund, futures fund and currency fund management – whether managing money or providing a service such as prime brokerage, administration, legal or accounting. AIMA's global membership comprises over 1,280 corporate members, throughout 49 countries, including many leading investment managers, professional advisers and institutional investors. AIMA's Canadian chapter, established in 2003, now has over 70 corporate members.

The objectives of AIMA are to provide an interactive and professional forum for our membership and act as a catalyst for the industry's future development, to be the pre-eminent voice of the industry to the wider financial community, institutional investors, the media, regulators, governments and other policy makers, to offer a centralized source of information on the industry's activities and influence, and to secure its place in the investment management community.

For more information about AIMA Canada and AIMA, please visit our web sites at [www.aima-canada.org](http://www.aima-canada.org) and [www.aima.org](http://www.aima.org).

This comment letter has been prepared by the IFRS working group of the members of AIMA Canada, comprised of managers of hedge funds, fund-of-funds, third party service providers and accountancy and law firms with practices focused on the alternative investments sector.

## ***General***

Thank you for the opportunity to provide our comments on the proposed amendments to the Rules. Generally, we support the direction of the proposed amendments. However, AIMA does not support the proposals related to consolidation and we have included our comments below with respect to this issue. We have also included our comments on the proposed amendments related to the classification of investment fund securities and certain other items in the proposed changes to the Rules.

## ***Consolidation***

The proposed amendments require that investment funds subject to NI 81-106 prepare consolidated financial statements, if required by IFRS. The proposed amendments further require that financial statements of an investment fund include a non-consolidated statement of investment portfolio and that financial highlights included in the MRFP be prepared on a non-consolidated basis.

We do not believe that consolidation by investment funds provides meaningful financial information to investors. In fact, we believe consolidation by investment funds is misleading to investors, creates issues of comparability and imposes

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additional costs and operational burden on investment funds, their managers, service providers and other industry participants.

Historically, investment funds were required to consolidate when reporting under Canadian GAAP. This resulted in operational issues for industry participants and confusion by investors. However, with the subsequent amendments to AcG-18 and AcG-15, investments held by investment companies were accounted for at fair value. We believe that fair value is the appropriate basis of measurement and presentation of investments held by an investment fund. The proposed amendments reverse this historical progression of accounting for investments.

We expect consolidation issues to impact a significant number of alternative investment funds in Canada. The Investment Funds Institute of Canada estimates that 21% of investment funds in Canada (excluding pooled and hedge funds) will have to consider consolidation of investments (an estimated 992 funds with \$133 billion in assets). Generally, the impact will be greater to alternative investment funds due to greater use of master-feeder funds, access funds, fund-of-funds and structured products, as well as generally greater holdings in private investments.

More specifically, we anticipate the following issues with consolidation by investment funds:

Comparability Issues: Investors will find it difficult to compare financial statements of investment funds that have consolidated certain investments versus those that have not, even if both funds have the same or similar investments.

Operational Issues: An investment fund's percentage ownership in another fund will change as frequently as daily and the ability of an investment fund to track these changes, and potentially the daily calculation of income and expenses, is onerous. The consideration of qualitative factors in determining control further complicates this process and adds considerable subjectivity. Where a fund's investment fund manager is unrelated to an underlying fund in a fund-of-fund structure, it may be difficult or impossible to access the financial records of the underlying fund in sufficient detail to support consolidation. Further, underlying funds may have different year-ends than the reporting fund which could make consolidation impractical and, at a minimum, more costly. Finally, the additional time required to obtain and process information to make consolidation determinations will likely result in many funds being unable to meet the current interim and annual filing deadlines. Overall, the investment industry is not structured to deal with consolidation and any requirement to do so would represent a significant and fundamental operational shift.

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Cost vs. Benefit: AIMA believes that the costs associated with tracking a fund's ownership position in underlying investments on an ongoing basis outweigh the benefits. The costs include potential changes to a fund manager's information technology systems, changes to operational processes and procedures, and the likely addition of finance department resources. Many investment funds outsource certain operational functions, such as fund accounting, to third party service providers. The costs charged to investment funds by these service providers would likely increase as a result of the systems and operational changes required to track the consolidation issue. It is also likely that audit costs would rise as a result of the additional procedures involved in auditing the consolidation, or potential consolidation, of investments.

Measurement Basis: In some situations, the consolidation of certain operating entities would result in a change in the measurement basis from fair value to historical cost or other measurement bases. Consolidation at the fund level could bring items such as property, plant and equipment, leases, goodwill, etc. onto the balance sheet, which would not be measured at fair value. We believe such measurement and presentation would be misleading and would add significant additional accounting and audit cost.

## Statement of Investment Portfolio

AIMA Canada believes that inclusion of a non-consolidated statement of investment portfolio in a set of consolidated financial statements will not be acceptable under IFRS, and an unqualified audit opinion under International Standards on Auditing could not be issued on such a statement. In AIMA's opinion, providing a reconciliation between the consolidated statement of financial position and the non-consolidated statement of investment portfolio, explanatory or numerically, would not provide meaningful information to investors due to the issues with the principle of consolidation enunciated above.

## Recommendation

AIMA does not believe that investment funds should prepare consolidated financial statements. There is precedent for the CSA accepting non-consolidated financial statements of registrants (such as that provided in NI 31-103, further supported by NI 52-107) which could be applied to investment funds. Also, the CSA could make the determination that investment funds are not considered to be 'publicly accountable enterprises' and apply private company Canadian GAAP, including the fair value provisions of AcG-18. While the IASB will be considering consolidation by investment funds at a future meeting, potential changes, if any, are unlikely to

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be applicable prior to the adoption of IFRS by investment funds in Canada. As such, a regulatory solution is desired.

To the extent that consolidation is required for investment funds, we recommend that any statement of investment portfolio be moved to a schedule or to the notes to the financial statements in order to facilitate an unqualified audit opinion. We believe a requirement for a supplementary audited schedule would add unnecessary audit costs and create potential auditing issues such as those related to the determination of materiality thresholds and an auditors' association with offering documents. Ultimately, we encourage the CSA to ensure that the accounting firms, who will be providing the audit opinions, are in agreement with the final format.

## *Classification of Investment Fund Securities (Puttable Instruments)*

The proposed amendments provide two presentation formats, one for funds determined to issue equity instruments and one for funds determined to issue liability instruments. These presentation formats do not accommodate fund structures with both equity and liability financial instruments (ie either 'total equity' or 'net assets attributable to securityholders', but not both). Further, many alternative investment funds are formed as partnerships. Limited partners in a fund are not issued securities and a presentation of 'net assets attributable to securityholders' would not be accurate. We would recommend a format that applies to all possible fund structures and any combination of equity and liability in order to achieve greater comparability across investment funds. We would be happy to work with the CSA in developing such a format.

The requirement in Section 3.2 (17.1) to show distribution expense should be renumbered so that it is after subsection 18. This is to ensure consistency with the description of subsection 18 and the NI 81-106 Companion Policy s. 2.1.1(2) requirement that the increase or decrease in net assets attributable to securityholders from operations exclude distributions.

It is important to note that the requirement in Section 3.2 (19) to report in the statement of comprehensive income the increase or decrease in total equity/net assets attributable to securityholders from operations per security appears to be a non-GAAP earnings measure. As such it should not be presented in the financial statements.

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## *Other comments*

### First interim and annual filings

The proposed filing extensions for financial statements in NI 31-103 and NI 45-106 are inconsistent. While AIMA appreciates the recognition of the issues involved in preparing the first filings it is our opinion that there should be consistency of the extension periods.

NI 45-106 grants a 30 day extension to the deadline for including the first IFRS interim financial report for reporting issuers. NI 31-103 grants a 15 day extension for the delivery of the first interim financial information for exempt market dealers and investment fund managers.

In AIMA's opinion the amendments to both NI 45-106 and NI 31-103 should be consistent and include a one-time 30-day extension for first interim and annual filings, including non reporting issuers (e.g. pooled funds sold under private placement exemptions). The wholesale changes to the measurement, presentation and disclosure in the financial statements, including opening balance sheet disclosures, first time presentation of statement of cash flows in many instances, terminology changes and reclassifications will prove a considerable exercise for all investment funds (both reporting and non-reporting issuers) and registrants. It is important to note that a registrant's financial results are dependent on the results of the investment funds, and therefore may not be determinable in advance of the fund financial results being finalized. Consistency of timeframes is required.

### Comparability across the Canadian Investment Fund Industry

We recommend that the CSA re-engage with the Accounting Standards Board to support the position that investment funds not be considered publicly accountable enterprises. We would be happy to assist the CSA in this re-engagement. In some jurisdictions where NI 81-106 applies, such as Ontario, some funds are subject to NI 81-106 and will report under IFRS and some funds are not subject to NI 81-106 and could potentially follow private company Canadian GAAP. Further, funds in provinces such as Alberta, British Columbia, Manitoba and Newfoundland, are not subject to NI 81-106 and could potentially report under private Company Canadian GAAP. The investment fund industry will continue to lack comparability across, and even within, jurisdictions in Canada. We also ask that the CSA re-consider whether private investment funds should be included in the scope of NI 81-106.

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### *Conclusion*

We appreciate the opportunity to provide the CSA with our views on the proposed amendments. Please do not hesitate to contact the members of the AIMA Canada set out below with any comments or questions you might have. We would appreciate the opportunity to meet with you in order to discuss our comments.

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Yours truly,

**ALTERNATIVE INVESTMENT MANAGEMENT ASSOCIATION**

By: 

Ian Pember  
On behalf of AIMA Canada and the Legal & Finance Committee

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