Alternative Investment Management Association (AIMA)

The Forum for Hedge Funds, Managed Futures and Managed Currencies

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September 28, 2016

The Secretary
Ontario Securities Commission
20 Queen Street West,
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Fax: 416-593-2318
Comments@osc.gov.on.ca

Dear Sirs/Mesdames:

Re: Ontario Securities Commission ("OSC") Notice and Request for Comment - Proposed OSC Rule 72-503 Distributions Outside of Canada (the "Rule") and Companion Policy 72-503CP to OSC Rule 72-503 Distributions Outside of Canada (the "Companion Policy", and collectively with the Rule, the "Proposal")

This comment letter is submitted on behalf of the Canadian section ("AIMA Canada") of the Alternative Investment Management Association ("AIMA") and its members to provide our comments to you on the legislation referred to above.

About AIMA

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 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 1,600 corporate members in more than 50 countries, including many leading investment managers, professional advisers and institutional investors. AIMA Canada, established in 2003, now has more than 130 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 provide leadership to the industry and be its pre-eminent voice; and to develop sound practices, enhance industry transparency and education, and to liaise with the wider financial community, institutional investors, the media, regulators, governments and other policy makers.

The majority of AIMA Canada members are managers of hedge funds and fund of

funds. Most are small businesses with fewer than 20 employees and $50 million or less in assets under management. The majority of assets under management are from high net worth investors and are typically invested in pooled funds managed by the member. Investments in these pooled funds are sold under exemptions from the prospectus requirements, mainly the accredited investor and minimum amount exemptions. Manager members also have multiple registrations with the securities regulatory authorities: as Portfolio Managers, Investment Fund Managers and in many cases as Exempt Market Dealers. AIMA Canada's membership also includes accountancy and law firms with practices focused on the alternative investments sector.

For more information about AIMA Canada and AIMA, please visit our web sites at canada.aima.org and www.aima.org.

Summary and Overview

We support and agree with the Proposal and appreciate the OSC's recognition of the desirability of providing certainty to market participants regarding the effect of prospectus and registration requirements in cross-border transactions where securities are distributed to investors outside of Canada. In particular, we appreciate the OSC's acknowledgment of the encroaching concept of the "real and substantial connection" test (or "sufficient connecting factors") which appears to have found itself into a number of judicial rulings. The Proposal creates certainty by creating a clear statement of the application of Ontario law to the distribution of securities to investors outside of Canada.

We believe that creating explicit exemptions from the prospectus and registration requirements in certain circumstances is very useful for market participants and we fully support the objectives behind the Proposal. Having said that, we have identified a small number of issues that may hinder the effectiveness of the Proposal:

1. In the event of a distribution outside of Canada section 4.1 requires the filing of Form 72-503F within 10 days, unless certain exemptions are met. The majority of our members will not meet the exemptions as they are typically registered as an Exempt Market Dealer ("**EMD**"). As a result there are duplicative filing requirements vs. NI 45-106 *Prospectus Exemptions* ("NI 45-106").

2. When relying on an exemption to the prospectus requirements through section 2.1, 2.2, or 2.3 of the Rule, it is not clear what constitutes taking "reasonable steps" to ensure that the securities come to rest outside of Canada.

3. The Companion Policy notes that purchasers of Ontario prospectus-qualified

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securities may be entitled to certain rights and investor protections under the Ontario *Securities Act* (the "**Act**") even if the investor is outside of Canada.

These issues are expanded upon below along with suggestions for potential clarifications to the Proposal.

1. Filing Requirements

The Proposal requires the filing of Form 72-503F within 10 days of a distribution to a non-resident, unless certain exemptions are met. As noted, the majority of our members are also registered as EMD's in order facilitate direct investment pursuant to an available prospectus exemption into funds that they manage. As such, these members would not qualify for the filing exemption in the Proposal since they are registered as a dealer in Canada.

Our members manage alternative investment funds that are generally in continuous distribution throughout the year. Partially in recognition of this fact NI 45-106 allows for an annual filing of a distribution report within 30 days of year end. Under the Proposal our members would be required to file the Form 72-503F every time there is a distribution to an investor outside of Canada. They would also be required to file the annual report of exempt distribution under NI 45-106 covering all distributions (domestic and foreign) made during the year. We respectfully request that the Proposal be amended to provide the same reporting exemption for investment fund issuers as section 6.2(2) of NI 45-106 to avoid duplication and reduce the complexity of the filing regime.

2. Guidance on taking reasonable steps

The Companion Policy provides that although nothing in the Rule prohibits or restricts the resale of the securities distributed under an exemption from the prospectus requirement in section 2.1, 2.2, or 2.3 of the Rule, the OSC expects that the issuer, underwriter and other participants in the offering will have taken reasonable steps to ensure that the securities come to rest outside of Canada and are not redistributed back into Canada in a manner that constitutes an indirect distribution in Ontario.

The Proposal notes that OSC Staff regularly encounter various challenges that issuers and intermediaries face in determining whether sufficient steps have been taken to reasonably conclude that securities have "come to rest" outside of Canada. One of the main objectives of the Proposal is to address these challenges.

We note that Interpretation Note 1 provides guidance on what would constitute

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taking reasonable steps. Interpretation Note 1 includes specific examples of positive steps, including placing a restriction in the underwriting agreement (or banking/selling group agreement) against the securities being offered to any Ontario residents and obtaining underwriter certificates or providing confirmation slips to purchasers affirming the residency of the purchasers. In addition to these examples, Interpretation Note 1 also contains contributing factors that should be considered in determining what steps may be reasonable in the circumstances, which include the class and nature of the securities, the attractiveness to Ontario investors of such securities, whether a market for such securities exists in Ontario or is likely to develop, and whether the underwriters are investment dealers that conduct substantial activities in Ontario or are affiliated with such investment dealers.

While it is not clear whether the examples and factors set forth in Interpretation Note 1 would be applicable or appropriate today, the draft Companion Policy is missing any guidance on taking reasonable steps. In the absence of any such guidance, it is possible that the Proposal may lead to some ambiguity and uncertainty for market participants trying to interpret the requirements.

We respectfully recommend that a modern set of guiding examples or principles should be included in the Companion Policy that can be applied by market participants in determining whether reasonable steps have been taken to ensure that the securities come to rest outside of Canada.

3. Investor protection under the Act for foreign purchasers

The Companion Policy states that, if an issuer or selling securityholder files a prospectus to qualify a concurrent distribution to a person or company in Ontario, the issuer may choose to file a prospectus in Ontario to qualify the distribution of securities to an investor outside of Canada and that any prospectus filed in such circumstances should therefore clearly state whether or not it also qualifies the distribution of securities to an investor outside of Canada. The Companion Policy goes on to say that "purchasers of Ontario prospectus-qualified securities may be entitled to certain rights and investor protections under the Act even if the investor is outside of Canada." In this regard, we would draw Staff's attention to the case of *Pearson v Boliden Ltd.*, 2002 BCCA 624 (*Pearson*), which appears to be settled law in Canada and which may be contrary to the statement in the Companion Policy.

Pearson involved a class action proceeding against Boliden Ltd. ("Boliden") for misrepresentation under the *Securities Act* (British Columbia). In 1997, Boliden completed a share offering and prepared a prospectus in compliance with the securities legislation of each Canadian province, the prospectus being duly accepted for filing by their respective securities authorities. The shares were

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also offered outside Canada on a private placement in the United States.

The British Columbia court considered whether purchasers from Alberta, New Brunswick, and the United States were entitled to be part of the class action by virtue of relying on the prospectus misrepresentation provisions of the *Securities Act* (British Columbia). After excluding New Brunswick purchasers from the class, the British Columbia Court of Appeal held that purchasers of securities outside of Canada were also not entitled to the protections of the provincial securities Acts:

> "*Outside Purchasers*: Similar reasoning applies to exclude those (the "outside purchasers") who bought their shares pursuant to distributions occurring in the Territories of Canada or outside of Canada, where no provincial *Securities Act* has application and where no prospectus (as defined in any of the *Acts*) was or could be required to be circulated. Instead, the laws of those jurisdictions must be looked to establish disclosure and filing requirements and the consequences of non-compliance. As submitted by counsel for Nesbitt Burns, the Acts of the provinces do not attach civil consequences to offering documents prepared in and pursuant to the laws of a foreign state."

The *Pearson* case appears to stand for the proposition that investors outside of Canada who purchased shares under the umbrella of a foreign legislative regime could not avail themselves of the statutory cause of action in Canadian provincial statutes because the provinces do not have the legislative jurisdiction to regulate foreign transactions. The Supreme Court of Canada refused leave to appeal from the judgment in the *Pearson* case ([2003] SCCA No. 29).

As a result of the holding in the *Pearson* case, we respectfully suggest that Staff reconsider the statement in the Companion Policy that "purchasers of Ontario prospectus-qualified securities may be entitled to certain rights and investor protections under the Act even if the investor is outside of Canada" as it may result in confusion among market participants.

Conclusion

In summary, we agree with the OSC's objective of reducing uncertainty for market participants regarding their obligations during the distribution of securities outside of Canada. However, we note the following points and recommendations for improving the Proposal:

- We recommend that investment funds be allowed to report distributions outside of Canada annually, consistent with the approach of NI 45-106.
- We recommend that OSC Staff consider creating a modern set of guiding examples or principles to be placed in the Companion Policy that can be

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applied by market participants in determining whether reasonable steps have been taken to ensure that the securities come to rest outside of Canada

- We recommend that OSC Staff reconsider whether the statement "purchasers of Ontario prospectus-qualified securities may be entitled to certain rights and investor protections under the Act even if the investor is outside of Canada" is an accurate statement of the law in Canada.

We appreciate the opportunity to provide the OSC with our views on the Proposal. Please do not hesitate to contact the members of AIMA set out below with any comments or questions that you might have.

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Yours truly,

ALTERNATIVE INVESTMENT MANAGEMENT ASSOCIATION

By:

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On behalf of AIMA Canada and the Legal & Finance Committee