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Financial and Consumers Services Commission, New Brunswick
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
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The Secretary Ontario Securities Commission
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Me Philippe Lebel Corporate Secretary and Executive Director, Legal Affairs Autorité des marchés financiers
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Dear Sirs/Mesdames:

RE: CSA Notice and Request for Comment Reducing Regulatory Burden for Investment Fund Issuers – Phase 2, Stage 1

About Alternative Investment Management Association (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 alternative investment funds, futures funds and currency fund management – whether managing money or providing a service such as prime brokerage, administration, legal or accounting.

AIMA's global membership comprises approximately 2,000 corporate members in more than 60 countries, including many leading investment managers, professional advisers and institutional investors and representing over $2 trillion in assets under management. AIMA Canada, established in 2003, has approximately 140 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 alternative investment 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 investment exemptions. Manager members also have multiple registrations with the Canadian securities regulatory authorities: as Portfolio Managers, Investment Fund Managers, Commodity Trading Advisers 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.

Comments

We are writing in response to **CSA Notice and Request for Comment Reducing Regulatory Burden for Investment Fund Issuers – Phase 2, Stage 1**. This response is organized based on the areas of focus outlined in the CSA Notice and Request for Comment.

Overall, AIMA Canada supports the objective of reducing regulatory burden and commends the Canadian Securities Administrators (CSA) and the Ontario Securities Commission (**OSC**) for their initiatives and ongoing projects to date.

We note that AIMA has previously submitted comments in response to ongoing CSA initiatives, such as the recent **OSC Regulatory Burden Reduction consultation**, **proposed CSA Derivatives legislation** and **proposed CSA Mutual Fund Sales Practices**, along with the recently amendments to the **CSA Client Focused Reforms**.[1] We do not intend to repeat those comments here and understand that AIMA's prior submissions will be considered as part of the CSA's review of regulatory burden, even where initial action by the OSC and CSA might have already been announced and underway.

A. Response to Workstream 2 – Investment Fund Designated Website

Workstream 2 proposes that reporting investment funds be required under NI 81-106 to designate a qualifying website with the purpose of the investment fund posting regulatory disclosures. It also notes that these websites would be required to be public.

Many reporting investment fund managers already have these types of websites for this exact purpose to increase accessibility for investors to applicable and meaningful information, and we applaud the CSA commitment to increased use of Internet-based technologies. We encourage the regulator to move towards more opportunities to explicitly allow electronic delivery and electronic access to

1 OSC Staff Notice 11-784, Proposed National Instrument 93-101 & Proposed Companion Policy 93-101CP; Proposed National Instrument 93-102 & Proposed Companion Policy 93-102CP; Proposed amendments to National Instrument 31-103 & Companion Policy 31-103CP; & Proposed amendments to National Instrument 81-105, Companion Policy 81-105CP and Related Consequential Amendments.

investors. The new designated website guidance should be consistent with previous guidance in the NI 81-106CP and apply on a go forward basis. Any new regulatory documents added to the website should stay on the website for reasonable length of time (1-2 years), and this should not turn towards being a longer-term archiving project for previously filed documents.

B. Response to Workstream 5

In response to:

a) Fund-on-Fund Investments by Investment Funds that are not Reporting Issuers

d) Inter-Fund Trades of Portfolio Securities between Related Reporting Investment Funds, Investment Funds that are not Reporting Issuers and Managed Accounts at Last Sale Price

Workstream 5 proposes to codify frequently granted exemptive relief in respect of the "investment fund conflict of interest restrictions" defined in NI 81-102 and the "inter-fund self-dealing investment prohibitions" defined in NI 81-107; these include proposals to accommodate changes to investment funds that are not reporting issuers ("private funds").

NI 81-102 sets out the requirements under which mutual funds and non-redeemable investment funds, both offered by way of prospectus, may be offered to the public in Canada.

NI 81-107 requires every public investment fund to have a fully independent body, called an Independent Review Committee, whose role is to oversee all decisions involving an actual or perceived conflict of interest faced by the fund manager in the operation of the fund. NI 81-107 sets out an independent oversight regime for all publicly offered investment funds that is intended to improve investment fund governance in Canada.

The requirements set out in NI 81-102 and the governance framework required under NI 81-107 seek to, among other things, ensure that that the regulatory mandate for investor protection is being met. This includes ensuring that conflicts of interests are addressed in the interests of funds/fund investors and not in the interests of fund managers or insiders.

Private funds are offered in Canada pursuant to to prospectus exemptions primarily under NI 45-106 and are not targeted to the public at large, but rather generally to accredited and permitted clients (together, "sophisticated investors").

Investors in private funds are intentionally considering and seeking out these types of products for a variety of purposes (i.e. they want non-correlated returns, they want investments in issuers that will outperform comparable passive public investments over the long-term, differentiated volatility and different concentration of securities) and have different liquidity needs than a traditional retail investor. Additionally, and often, these types of investors have advisers to support their investment decisions (i.e. ultra-high net worth individual investors or family offices) or entire investment teams to assist in investment decision making (i.e. pension and endowment funds).

There should not be an equalization of private funds and public funds – they are fundamentally different with different needs.

Fundamentally, investors in private funds, by virtue of being sophisticated investors, do not have the same need for investor protection as retail investors, either because they can withstand losses in these investments and/or have advisers to support their investment decisions.

Many alternative investment funds have fund-on-fund structures for the purposes of, among other things, tax efficiency. Investors subscribe to these top "feeder" funds which in turn make investments in an underlying "master" fund. The master fund then makes investments in securities and the interests in these securities by the feeder fund is determined by the proportionate investment in the master fund. Fees and expenses for the top feeder funds are generally adjusted given that the master fund also charges a management fee and performance fee.

The conflicts of interests in these master-feeder situations are inherently different than the conflicts that may arise from investments in retail fund-on-fund structures.

There is currently an exemption from the inter-fund self-dealing investment prohibitions in subsection 6.1(2) of NI 81-107 for public investment funds. The proposals recommend extending this exemption so that it will apply to inter-fund trades involving related investment funds that are not reporting issuers and amending section 6.1 of NI 81-107 so that all inter-fund trades of exchange-traded securities may occur at last sale price.

The imposition of requirements under NI 81-102 and NI 81-107 would not, in fact, alleviate the regulatory burden placed on private funds and managers of these funds, but rather add to the burden and cost to registrants and investors. An IRC would have to be established for the private funds as well as an infrastructure developed to support the IRC. Under NI 81-107, the costs associated with the IRC would then be charged to the private fund.

For those private fund managers that do not currently engage in the public fund arena and have no understanding of or exposure to IRC's, there would be increased cost and time for these managers to learn about and develop an infrastructure for the requirements set out in NI 81-102 and NI 81-107.

Private fund advisers already have a fiduciary obligation, and investment fund managers have a standard of care, to do what is in the best interest of the fund/its investors – therefore, there is no need to layer on more requirements/restrictions that in substance require the adviser/investment fund manager to continue to do what is in the best interests of the fund and its investors.

Under the October 2019 amendments to NI 31-103, a registered firm must disclose in writing all material conflicts of interest identified to a client whose interests are affected by the conflicts of interest if a reasonable client would expect to be informed of those conflicts of interest. Therefore, we believe the issues/concerns can be addressed by way of disclosure.

Suggestions:

- Manage the conflicts issues in this workstream, in NI 31-103 (including inter-fund trades for private funds) rather than making these funds and their managers subject to NI 81-102 and NI 81-107 which will add to the regulatory burden and add costs to investors and the manager. This allows them to meet the regulatory/legal standard for a registrant while allowing them flexibility to meet that standard in the context of their specific services.

- Registered firms should establish an internal committee made up of various senior individuals with objective oversight, to review and assess conflicts (similar to the way private fund managers establish internal valuation committees)

- Rather than having an IRC assess conflicts and the registered firm report to the IRC, have the CCO report to the board of directors as to compliance with the requirements of NI 31-103 (including inter-fund trades at last sale price).

- Consider the approach taken in other jurisdictions – such as the anti-fraud provisions in the US under the Advisors Act where conflicts management is not prescribed but rather a requirement of the registrant along with initial and ongoing disclosures regarding conflicts.

It is our view that establishing an IRC in and of itself is not a solution to managing conflicts as it adds cost and it is not necessarily appropriate for private funds. If the regulations state how a conflict matter should be addressed (i.e. interfund trades in securities on the exchange must be done at last sale price), then the requirement can be addressed via policies and procedures and controls without an IRC.

C. Workstream 5, Part (a)

While the proposed amendment to section 2.5.1 of NI 81-102 to permit private funds to invest in other related investment funds purports to be an effort to reduce regulatory burdens, the proposed changes actually increase the regulatory requirements applicable to non-reporting issuer investment funds.

First, under Section 13.5(2)(a) of NI 31-103, an adviser is permitted to cause an investment fund managed by it to invest in a related investment fund as long as notice is provided to the investors and their consent is obtained. There is no distinction between private and public funds with respect to the applicability of this section. The provisions of section 13.5(2)(a) should be maintained and amendments that would reduce regulatory burdens related to investments in related investment funds include:

- codifying the situation where a manager did not provide notice and obtain consent as required under section 13.5(2)(a); and

- for a mutual fund that is not a reporting issuer to invest in a related issuer, which is prohibited in certain circumstances as described in section 111 of the Securities Act (Ontario).

As described in the [Request for Comments] in Workstream 5, Part (a), the new exemption would permit private funds to invest in other related private funds and in related reporting issuer investment funds, "[S]ubject to several conditions being met." Given that section 13.5(2)(a) permits a related party investment in certain circumstances, imposing any further conditions under the proposed amendment in such circumstances would increase regulatory burdens.

Second, we believe that amendments to NI 31-103 should not be made through amendments to NI 81-102. Private funds are not subject to NI 81-102. It would only take additional time, and cause inconvenience and added expense for such investment funds to suddenly be required to look to NI 81-102 for any reason, and investor protection concerns for private funds are different than for public funds. NI 81-102 is a lengthy and complex rule intended to address rules for funds offered to the public. It would be a step backward from a regulatory reduction perspective to make NI 81-102 apply to private funds. Further, it would be more rational and easier to interpret the rules applicable to funds when they are contained in one place – section 13.5 imposes the restrictions so any exceptions should also be contained in the same provision in NI 31-103. This would also cause confusion in interpreting existing references to "NI 81-102 funds", "funds to which NI 81-102 applies", etc. in existing exemptive relief orders and elsewhere.

We also note that many of the conditions imposed in the context of relief applications are appropriate for a top fund that is a mutual fund but are not appropriate for a non-redeemable investment fund. For example, the latter type of funds is not subject to the same liquidity constraints as mutual funds and should not be subject to the same conditions for relief.

Similarly, under Workstream 5, Part (c), the CSA is proposing amendments to NI 81-102 to provide relief for in-specie redemptions and subscriptions for private mutual funds that are not subject to NI 81-102. This is problematic and confusing for the reasons identified above where legislation that was not applicable to a type of entity becomes applicable only for the purposes of an exemption. Second, rather than codifying an exemption to section 13.5(2)(b) that likely does not impose any restriction on in-specie subscriptions and redemptions for mutual funds and other investment funds that are not reporting issuers, the CSA should clarify the interpretation of those provisions.

Under Workstream 5, Part (d), the CSA is proposing to permit interfund trades in certain circumstances that would be welcome relief for private funds that are not subject to NI 81-107. Again, for the reasons set out above, relief from the restrictions on inter-fund and account trades under NI 31-103, should be provided under NI 31-103. There will be an increased regulatory burden if portfolio managers, including their counsel and compliance staff, would not be required to have to review NI 81-102 or NI 81-107, instruments that do not currently apply to them or their funds, in order to have relief from restrictions imposed under NI 31-103.

The foregoing proposed amendments also pose a technical problem. As drafted, it appears that the funds themselves will be able to effect the transactions that were previously prohibited. However, nothing in the amendments provides relief to registrants that are prohibited from causing the funds they manage to carry out those same transactions. Relief from restrictions in NI 31-103 that apply to private funds should be added to NI 31-103.

To be clear, AIMA would be supportive of amendments to section 13.5 of NI 31-103 to codify exemptive relief for inter-fund trades by non-reporting funds and managed accounts on similar terms as those established for publicly offered investment funds. The *prohibition in section 13.5(2) should include exemptions if such trade (i) is executed at the last sale price; (ii) is completed following procedures approved by the Board of the fund or IFM/PM; and (iii) such trades are reported at least annually to the Board.*

D. Approaching Cost/Benefit Analysis of Burden Reduction

The Securities Act (Ontario) requires that any proposed rule published must include “a description of the anticipated costs and benefits of the proposed rule.” (s. 143.2(2)). There are two SEC proposals, the SEC Derivatives Rule Proposal & SEC Best Interest Proposal, outlining how they approach cost/benefit analyses. These may be considered as a type of benchmark analysis that should be aimed for, both for when new proposals are issued and for estimating the impact of the burden reduction effort. For example, full calculation details and underlying assumptions should be provided to the industry, similar to the SEC (using FOIA if necessary), so that they can be reviewed for reasonableness, especially with respect to wage costs. For further examples, please see:

- SEC Derivatives Rule Proposal (November 2019): Economic Analysis pages 249-327, Paperwork Reduction Analysis pages 329-379. Benefits and costs analysis begin on page 260. A full discussion of possible impacts is given. Quantification is not as great given the nature of the proposals, but some is given (see pages 267-268, 280, 290)

- SEC Best Interest Proposal (April 2018): Economic Analysis pages 214-333, Paperwork Reduction Analysis pages 338-375. The discussion of costs starts on page 272 and includes a full discussion of possible impacts. For example, see page 283 where they specifically state (with assumptions outlined) that the Disclosure Obligation might impose an initial burden of 5.8 million hours at a cost of $40.79 million. Quantification is not as great given the nature of the proposals, but some is given.

E. Additional suggestions in regard to Regulatory Burden Reduction

Earlier this year, the OSC issued **OSC Staff Notice 11-784 Burden Reduction** for comments and consequently published on November 19, 2019 a report titled, Reducing Regulatory Burden in Ontario's Capital Markets. AIMA commends the OSC for their active consultation with the market participants on this issue and action taken to date to reduce regulatory burden. We urge the CSA to review this letter for further consideration as the burden reduction project continues both in Ontario and across Canada.

We appreciate the opportunity to provide the CSA with our views on this initiative. Please do not hesitate to contact the members of AIMA set out below with any comments or questions that you might have. We would be pleased to meet with you to discuss our comments and concerns further.

Yours truly,

ALTERNATIVE INVESTMENT MANAGEMENT ASSOCIATION CANADA

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