



FREQUENTLY ASKED QUESTIONS NON-CANADIAN FUNDS SELLING IN CANADA

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This paper is not a legal opinion and should not be considered to be a legal opinion. The Canadian securities regulators have provided certain limited guidance on what factors they will consider in determining whether an entity is in the business of trading or advising in securities and the role of an investment fund manager and these must be considered light of the actual facts and circumstances of the foreign fund. We emphasize that the foregoing is a summary only and does not purport to be an exhaustive explanation of all applicable legal requirements, rules, regulations or legal options. For the sake of brevity and simplicity, certain issues have been intentionally omitted and others, although included, are discussed in general terms only. Further, statutory and regulatory requirements may change from time to time. It is therefore important that you consult the information contained herein for general guidance purposes only.

INTRODUCTION

The purpose of this paper is to provide a high-level overview of certain regulations applicable to non-Canadian closed-ended investment funds¹ marketing to Canadian investors.



ABOUT DLA PIPER

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We advise a broad range of clients in the area of investment funds and asset management and regularly deal with Canadian provincial securities commissions on regulatory and compliance matters. Our clients include both public and private, and domestic and international, asset managers, investment funds, investment banks, dealers and advisers. We have extensive experience advising on all manner of structuring, (taxation, alternative investment vehicles and derivative products), governance, operations, financing, diligence, registration and regulatory compliance.

¹ For the purposes of this paper, "investment fund" or "fund" refers to an entity whose primary purpose is to pool investor funds and invest such pooled funds in securities and on a passive basis. A "closed ended fund", is a fund whose securities are non-redeemable (as opposed to an entity such as a mutual fund whose securities are redeemable by an investor based on net asset value).

FREQUENTLY ASKED QUESTIONS

Q1: Can a foreign investment fund sell its securities to Canadian investors without being registered in Canada?

Yes, in many cases a foreign investment fund will be able to sell its foreign securities² to Canadian investors without being registered in Canada, provided the fund: (i) sells only to “permitted clients”; (ii) meets all requisite conditions; and (iii) complies with certain filing requirements, as set forth below.

GENERAL

Canadian securities legislation provides that any individual or entity who engages, in Canada, in one or more of the following activities must be registered unless an exemption is available.

Type of Business Activity	Registration Category
Engaging in the business of, or holding itself out as being in the business of, trading in securities ³	Dealer
Engaging in, or holding itself out as being in the business of, advising in securities ⁴	Adviser
Acting as an investment fund manager ⁴	Investment Fund Manager

² “Foreign security” is defined under Canadian securities legislation as a security issued by an issuer incorporated, formed or created under the laws of a foreign jurisdiction or a security issued by a government of a foreign (i.e. non-Canadian) jurisdiction.

³ Whether an entity/individual is in the business of trading or advising in securities is a factual determination and depends on a number of factors such as whether the entity/individual is acting in a similar fashion as a Canadian registrant, whether it is intermediating trades or acting as a market maker, whether it is directly or indirectly carrying on the activity with repetition, regularity or continuity, whether it is being, or expecting to be, remunerated or compensated and whether it is directly or indirectly soliciting securities transaction or offering advice with respect to securities.

⁴ Acting as an “investment fund manager” includes activities such as establishing a distribution channel for the fund; marketing the fund; establishing and overseeing the fund’s compliance and risk management programs; overseeing the day-to-day administration of the fund; retaining and liaising with the portfolio manager, the custodian, the dealers and other service providers of the fund; overseeing advisers’ compliance with investment objectives and overall performance of the fund; preparing offering documents; preparing and delivering security holder reports; identifying, addressing and disclosing conflicts of interest; calculating net asset value of the fund; calculating, confirming and arranging payment of subscriptions and redemptions, and arranging for the payment of dividends or other distributions.

REGISTRATION AS A DEALER

A fund whose business involves investing in the securities of public and/or private entities on a passive basis⁵ will generally be deemed by the Canadian securities regulators to be in the business of trading in securities and, as such, would be required to be registered as a dealer.

However, a foreign investment fund may be able to rely on the “international dealer” exemption in connection with sales of its securities to Canadian resident investors, if it both: (i) sells the foreign security to a “permitted client”; and (ii) meets the additional requirements as set forth in (a) – (f) below. “Permitted clients” include banks, credit unions, trust loan and insurance companies, registrants, an individual who beneficially owns financial assets having an aggregate realizable value of more than \$5 million or a company that has net assets of more than \$25 million. A complete list of categories of “permitted client” is set out in Schedule A.

In addition to all Canadian resident investors being permitted clients, to qualify as an “international dealer”, all the following requirements must be met:

- (a) the head office or principal place of the investment fund must be in a foreign jurisdiction;
- (b) the investment fund must be registered under the securities legislation of the foreign jurisdiction in a category of registration that permits it to sell securities to investors;
- (c) the investment fund engages in the business of a dealer in the foreign jurisdiction;
- (d) one of the following applies:
 - (i) the permitted client is itself a person or company registered under Canadian securities legislation as an adviser or dealer; or

- (ii) the investment fund has notified the permitted client of all of the following: (A) that the investment fund is not registered in the local jurisdiction to make the trade; (B) the foreign jurisdiction in which the head office or principal place of business of the investment fund is located; (C) that all or substantially all of the assets of the investment fund may be situated outside of Canada; (D) that there may be difficulty enforcing legal rights against the investment fund because of the above; (E) the name and address of the agent for service of process of the investment in the local Canadian jurisdiction;
- (e) the investment fund has appointed a Canadian entity to act as its agent for service and submitted to the Canadian securities regulatory authorities in each of the Canadian province(s) where it is selling the security a completed Form 31-103F2 *Submission to Jurisdiction and Appointment of Agent for Service*; and
- (f) if the investment fund has sold securities during any 12-month period preceding December 1 of a year, it must have filed a notice (in the form of an email or letter) with the Canadian securities regulatory authorities in each of the Canadian province(s) where it has sold the securities.⁶

⁵ An investment fund is deemed to be investing on a “passive basis” where it is not actively involved in the management of the issuers of the securities it acquires.

⁶ Sales to permitted clients resident in Ontario, in addition to filing a notice with the Ontario Securities Commission, require remittance of a prescribed fee under Ontario Securities Commission Rule 13-502 - Fees.

REGISTRATION AS AN ADVISER

Canadian securities legislation requires registration as an “adviser” if advice is being provided to investors with respect to a security. Generally, this does not include advice which does not purport to be tailored to the needs of the person or company receiving the advice.

The determination of whether a fund requires registration as an advisor is a highly-fact specific exercise. Should, however, advising be deemed to occur, the fund may be able to rely on the “international adviser” exemption. To rely on this exemption, the fund must (i) provide advice to “permitted clients” (see above and Schedule A) only; (ii) not advise with respect to Canadian securities (unless incidental to advising on foreign securities); and (iii) meet all of the following requirements:

- (a) the head office or principal place of the investment fund must be in a foreign jurisdiction;
- (b) the investment fund must be registered under the securities legislation of the foreign jurisdiction in a category of registration that permits it to provide advice on securities to investors;
- (c) the investment fund engages in the business of an adviser in the foreign jurisdiction;
- (d) as at the end of its most recently completed financial year, not more than 10% of the aggregate consolidated gross revenue of its investments, including those of its affiliates and its affiliated partnerships, can have been derived from portfolio management activities of the fund, its affiliates and its affiliated partnerships, in Canada;
- (e) before advising the Canadian investor, the investment fund must notify the investor of all of the following: (A) that the investment fund is not registered in the local jurisdiction to provide the advice; (B) the foreign jurisdiction in which the head office or principal place of business of the investment fund is located; (C) that all or substantially all of the assets of the investment fund may be situated outside of Canada; (D) that there may be difficulty enforcing legal rights against the investment fund because of the above; (E) the name and address of the agent for service of process of the investment fund in the local Canadian jurisdiction;

- (f) the investment fund has appointed a Canadian entity to act as its agent for service and submitted to the Canadian securities regulatory authorities in each of the Canadian province(s) where it is selling the security a completed Form 31-103F2 *Submission to Jurisdiction and Appointment of Agent for Service*; and
- (g) if the investment fund has advised on securities during any 12-month period preceding December 1 of a year, it must have filed a notice (in the form of an email or letter) with the Canadian securities regulatory authorities in the applicable Canadian province(s).

In the event the foreign fund is not able to rely on the “international adviser” exemption, the fund may be able to utilize the “international sub-adviser” exemption. This exemption permits a foreign fund (including an investment fund) to provide advice to certain Canadian registrants (such as a brokerage) without having to register as an adviser in Canada. In order to utilize the international sub-adviser exemption, the foreign fund must provide advice through a Canadian registrant, which is deemed to receive such advice either for its own benefit or for the benefit of its clients. A condition of this exemption is that the Canadian registrant has entered into an agreement with its clients providing that the Canadian registrant is responsible for client losses arising out of certain failures by the foreign fund.

REGISTRATION AS AN INVESTMENT FUND MANAGER

In most provinces of Canada, an entity or individual that is managing a foreign investment fund in a jurisdiction outside of Canada, does not need to be registered as an investment fund manager, notwithstanding sales of fund securities to Canadian residents.

However, the securities regulators in the Provinces of Ontario, Quebec, and Newfoundland and Labrador require that an investment fund that is “soliciting”⁷ Canadian investors in any of those provinces must be registered unless the following conditions are met:

- (a) the securities of the fund are issued to “permitted clients”⁸ only;
- (b) the investment fund manager does not have its head office or its principal place of business in Canada;
- (c) the investment fund manager is incorporated, formed or created under the laws of a foreign jurisdiction;
- (d) the investment fund itself is not a reporting issuer in any jurisdiction of Canada;
- (e) the investment fund manager has submitted to the applicable provincial securities regulatory authority in the applicable province a completed Form 32-102F1 *Submission to Jurisdiction and Appointment of Agent for Service for International Investment Fund Manager*;
- (f) the investment fund manager has notified the permitted clients in writing of all of the following: (A) that the investment fund manager is not registered in the local jurisdiction to act as an investment fund manager; (B) the

foreign jurisdiction in which the head office or principal place of business of the investment fund manager is located; (C) that all or substantially all of the assets of the investment fund manager may be situated outside of Canada; (D) that there may be difficulty enforcing legal rights against the investment fund manager because of the above; and (E) the name and address of the agent for service of process of the investment fund manager in the local jurisdiction;

- (g) the investment fund manager must notify (via email or letter) the securities regulatory authority in the local jurisdiction by December 1 of any year in which it has relied on the permitted client exemption of: (A) the fact that it relied upon the permitted client exemption; and (B) for all investment funds for which it acts as an investment fund manager, the total assets under management, expressed in Canadian dollars, attributable to securities beneficially owned by residents of the Canadian local jurisdiction as at the most recently completed month; and
- (h) the investment fund manager must file with the securities regulatory authority in the local jurisdiction, a completed Form 32-102F2 *Notice of Regulatory Action* within 10 days of the date on which that person or company began relying on the permitted client exemption and must also notify (via email or letter) the securities regulatory authority in the local jurisdictions of any change to the information previously submitted in that Form within 10 days of the change.

⁷ Solicitation includes contacting someone by any means, including advertising that proposes buying or selling securities or participating in a securities transaction, or that offers services or advice for these purposes.

⁸ It is important to note that to rely on this exemption, the foreign investment fund must ensure that if there are already Canadian investors in those local jurisdictions, those existing Canadian investors fit one of the categories of “permitted clients” at the time the securities were distributed to them.

Q2: Are there restrictions on who the foreign investment fund can market and sell to?

Any sales of securities to Canadian residents (including sales of units of an investment fund) must either (i) be qualified by a prospectus; or (ii) be issued pursuant to a prospectus exemption. The most commonly used exemption allows for sales to “accredited investors”, which include institutional investors, portfolio managers and advisers, investment funds and persons or companies that meet one of several income or asset tests. A complete list of categories of “accredited investor” is set out in Schedule B.

Note that the requirement for an investor to be prospectus exempt is in addition to any registration requirement applicable to the fund itself as described in Q1, above.

Q3: What about venture capital funds? Can they sell securities to Canadian residents without being registered as a dealer, adviser or investment fund manager?

It depends on the facts. If the fund is actively involved in the management of each of the entities in which it invests, it may not be deemed to be in the business of trading or advising in securities, or be acting as an investment fund manager. In such case, no registration of the fund would typically be required, though sales of fund units still would be subject to the prospectus (or prospectus exemption) requirement.

Q4: Can the fund use offering documents?

Yes. However, funds selling in Canada should be aware that the distribution of materials describing the business of the fund may trigger statutory rights of action for damages and/or rescission, as well as trigger certain related disclosure requirements.

In addition, when selling to Canadian residents, a form of Canadian subscription agreement should be utilized to ensure subscribers provide the information required for the fund to rely on the exemptions discussed above

Q5: What reporting, registration or filing requirements will be imposed?

In addition to the filings mentioned above, in each of the provinces where the sale happens, assuming use of the accredited investor or other prospectus exemption, a National Instrument 45-106FI report of exempt trade must be filed with the Canadian regulators, together with the applicable filing fee. The filing of the offering documentation is also required in certain provinces.

SCHEDULE A

CATEGORIES OF “PERMITTED CLIENTS”

“permitted client” means any of the following:

- (a) a Canadian financial institution or a Schedule III bank;
- (b) the Business Development Bank of Canada incorporated under the *Business Development Bank of Canada Act* (Canada);
- (c) a subsidiary of any person or company referred to in paragraph (a) or (b), if the person or company owns all of the voting securities of the subsidiary, except the voting securities required by law to be owned by directors of the subsidiary;
- (d) a person or company registered under the securities legislation of a jurisdiction of Canada as an adviser, investment dealer, mutual fund dealer or exempt market dealer;
- (e) a pension fund that is regulated by either the federal Office of the Superintendent of Financial Institutions or a pension commission or similar regulatory authority of a jurisdiction of Canada or a wholly-owned subsidiary of such a pension fund;
- (f) an entity organized in a foreign jurisdiction that is analogous to any of the entities referred to in paragraphs (a) to (e);
- (g) the Government of Canada or a jurisdiction of Canada, or any Crown corporation, agency or wholly-owned entity of the Government of Canada or a jurisdiction of Canada;
- (h) any national, federal, state, provincial, territorial or municipal government of or in any foreign jurisdiction, or any agency of that government;
- (i) a municipality, public board or commission in Canada and a metropolitan community, school board, the Comité de gestion de la taxe scolaire de l'île de Montréal or an intermunicipal management board in Québec;
- (j) a trust company or trust corporation registered or authorized to carry on business under the *Trust and Loan Companies Act* (Canada) or under comparable legislation in a jurisdiction of Canada or a foreign jurisdiction, acting on behalf of a managed account managed by the trust company or trust corporation, as the case may be;
- (k) a person or company acting on behalf of a managed account managed by the person or company, if the person or company is registered or authorized to carry on business as an adviser or the equivalent under the securities legislation of a jurisdiction of Canada or a foreign jurisdiction;
- (l) an investment fund if one or both of the following apply:
 - (i) the fund is managed by a person or company registered as an investment fund manager under the securities legislation of a jurisdiction of Canada;
 - (ii) the fund is advised by a person or company authorized to act as an adviser under the securities legislation of a jurisdiction of Canada;
- (m) in respect of a dealer, a registered charity under the *Income Tax Act* (Canada) that obtains advice on the securities to be traded from an eligibility adviser⁹ or an adviser registered under the securities legislation of the jurisdiction of the registered charity;

⁹ “eligible adviser” means: (a) a person that is registered as an investment dealer and authorized to give advice with respect to the type of security being distributed, and (b) in Manitoba, also means a lawyer who is a practicing member in good standing with a law society of a jurisdiction of Canada or a public accountant who is a member in good standing of an institute or association of chartered accountants, certified general accountants or certified management accountants in a jurisdiction of Canada provided that the lawyer or public accountant must not (i) have a professional, business or personal relationship with the issuer, or any of its directors, executive officers, founders, or control persons, and (ii) have acted for or been retained personally or otherwise as an employee, executive officer, director, associate or partner of a person that has acted for or been retained by the issuer or any of its directors, executive officers, founders or control persons within the previous 12 months.

- (n) in respect of an adviser, a registered charity under the *Income Tax Act* (Canada) that is advised by an eligibility adviser or an adviser registered under the securities legislation of the jurisdiction of the registered charity;
- (o) an individual who beneficially owns financial assets¹⁰ having an aggregate realizable value that, before taxes but net of any related liabilities, exceeds \$5 million;
- (p) a person or company that is entirely owned by an individual or individuals referred to in paragraph (o), who holds the beneficial ownership interest in the person or company directly or through a trust, the trustee of which is a trust company or trust corporation registered or authorized to carry on business under the *Trust and Loan Companies Act* (Canada) or under comparable legislation in a jurisdiction of Canada or a foreign jurisdiction;
- (q) a person or company, other than an individual or an investment fund, that has net assets of at least \$25 million as shown on its most recently prepared financial statements; and
- (r) a person or company that distributes securities of its own issue in Canada only to persons or companies referred to in paragraphs (a) to (q).

All dollar amounts refer to Canadian dollars.



¹⁰ “financial assets” means cash, securities, or a contract of insurance, a deposit or an evidence of a deposit that is not a security for the purposes of securities legislation.

SCHEDULE B

CATEGORIES OF “ACCREDITED INVESTORS”

“accredited investor” means

- (a) except in Ontario, a Canadian financial institution, or a Schedule III bank;
- (b) except in Ontario, the Business Development Bank of Canada incorporated under the *Business Development Bank of Canada Act* (Canada);
- (c) except in Ontario, a subsidiary of any person referred to in paragraphs (a) or (b), if the person owns all of the voting securities of the subsidiary, except the voting securities required by law to be owned by directors of that subsidiary;
- (d) except in Ontario, a person registered under the securities legislation of a jurisdiction of Canada as an adviser or dealer;
- (e) an individual registered under the securities legislation of a jurisdiction of Canada as a representative of a person referred to in paragraph (d);
- (f) an individual formerly registered under the securities legislation of a jurisdiction of Canada, other than an individual formerly registered solely as a representative of a limited market dealer under one or both of the *Securities Act* (Ontario) or the *Securities Act* (Newfoundland and Labrador);
- (g) except in Ontario, the Government of Canada or a jurisdiction of Canada, or any crown corporation, agency or wholly owned entity of the Government of Canada or a jurisdiction of Canada;
- (h) except in Ontario, a municipality, public board or commission in Canada and a metropolitan community, school board, the Comité de gestion de la taxe scolaire de l'île de Montréal or an intermunicipal management board in Québec;
- (i) except in Ontario, any national, federal, state, provincial, territorial or municipal government of or in any foreign jurisdiction, or any agency of that government;
- (j) except in Ontario, a pension fund that is regulated by the Office of the Superintendent of Financial Institutions (Canada), a pension commission or similar regulatory authority of a jurisdiction of Canada;
- (k) an individual who, either alone or with a spouse, beneficially owns financial assets having an aggregate realizable value that, before taxes but net of any related liabilities, exceeds \$1,000,000;
- (l) an individual who beneficially owns financial assets having an aggregate realizable value that, before taxes but net of any related liabilities, exceeds \$5,000,000;
- (m) an individual whose net income before taxes exceeded \$200,000 in each of the 2 most recent calendar years or whose net income before taxes combined with that of a spouse exceeded \$300,000 in each of the 2 most recent calendar years and who, in either case, reasonably expects to exceed that net income level in the current calendar year;
- (n) an individual who, either alone or with a spouse, has net assets of at least \$5,000,000;
- (o) a person, other than an individual or investment fund, that has net assets of at least \$5,000,000 as shown on its most recently prepared financial statements;
- (p) an investment fund that distributes or has distributed its securities only to:
 - (i) a person that is or was an accredited investor at the time of the distribution;
 - (ii) a person that acquires or acquired securities in the circumstances referred to in sections 2.10 [Minimum amount investment], or 2.19 [Additional investment in investment funds] of National Instrument 45-106; or
 - (iii) (iii) a person described in paragraph (i) or (ii) that acquires or acquired securities under section 2.18 [Investment fund reinvestment] of National Instrument 45-106;
- (q) an investment fund that distributes or has distributed securities under a prospectus in a jurisdiction of Canada for which the regulator or, in Québec, the securities regulatory authority, has issued a receipt

- (r) a trust company or trust corporation registered or authorized to carry on business under the *Trust and Loan Companies Act* (Canada) or under comparable legislation in a jurisdiction of Canada or a foreign jurisdiction, acting on behalf of a fully managed account managed by the trust company or trust corporation, as the case may be;
- (s) a person acting on behalf of a fully managed account managed by that person, if that person is registered or authorized to carry on business as an adviser or the equivalent under the securities legislation of a jurisdiction of Canada or a foreign jurisdiction;
- (t) a registered charity under the *Income Tax Act* (Canada) that, in regard to the trade, has obtained advice from an eligibility adviser or an adviser registered under the securities legislation of the jurisdiction of the registered charity to give advice on the securities being traded;
- (u) an entity organized in a foreign jurisdiction that is analogous to any of the entities referred to in paragraphs (a) to (d) or paragraph (i) in form and function;
- (v) a person in respect of which all of the owners of interests, direct, indirect or beneficial, except the voting securities required by law to be owned by directors, are persons that are accredited investors;
- (w) an investment fund that is advised by a person registered as an adviser or a person that is exempt from registration as an adviser;
- (x) a person that is recognized or designated by the securities regulatory authority or, except in Ontario and Québec, the regulator as an accredited investor; or
- (y) a trust established by an accredited investor for the benefit of the accredited investor's family members of which a majority of the trustees are accredited investors and all of the beneficiaries are the accredited investor's spouse, a former spouse of the accredited investor or a parent, grandparent, brother, sister, child or grandchild of that accredited investor, of that accredited investor's spouse or of that accredited investor's former spouse.

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