

International Comparative Legal Guide – Alternative Investment Funds 2023: Canada

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1 Regulatory Framework

1.1 What legislation governs the establishment and operation of Alternative Investment Funds?

In Canada, the term “alternative investment fund” or AIF is not a term of art. Canadian securities laws distinguish between collective investment vehicles that are “investment funds” and those that are not investment funds. Consequently, certain AIFs in Canada are regulated as investment funds. Additional regulations apply to an investment fund that files a prospectus and is a “reporting issuer”. Certain prospectus-qualified mutual funds, designated as “alternative mutual funds”, are marketed to retail investors as liquid AIFs or “liquids alts”. Also available to the retail market in Canada are listed issuers that are “investment entities” under International Financial Reporting Standards (IFRS). These are “hybrid” issuers that have portfolios, or portions thereof, managed by a registered portfolio manager and are marketed as public private equity funds.

In Canada, securities regulation is a matter of provincial and territorial jurisdiction. Each of Canada’s 10 provinces and three territories has its own securities laws, administered by a local securities regulatory authority. However, in a growing number of areas, including investment fund regulation, the distribution of securities and the registration of market participants in the asset management industry, the rules have been largely harmonised across the 13 jurisdictions. National instruments (NIs) are securities rules that have been adopted by all 13 provincial regulators and apply nationally.

The principal securities legislation applicable to the private placement of AIF securities in Canada is NI 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* (NI 31-103) and NI 45-106 *Prospectus Exemptions* (NI 45-106).

Canadian tax laws applicable to AIFs apply at both the federal and provincial levels. It is also typical that corporation law, limited partnership law, anti-money laundering law, terrorist financing law and privacy law will apply.

1.2 Are managers or advisers to Alternative Investment Funds required to be licensed, authorised or regulated by a regulatory body?

Foreign managers that manage or advise AIFs that are not investment funds do not have to be registered in Canada.

Under Canadian securities laws, unless an exemption is available, or a discretionary exemption is granted, firms must register in each jurisdiction where they are:

- In the business of trading or advising.

- Holding themselves out as being in the business of trading or advising.
- Acting as an investment fund manager (IFM).

Portfolio managers that advise AIFs investing in commodity futures contracts or options may need to register as advisers under applicable commodity futures legislation, unless their activity can be characterised as incidental.

Managers and advisers located outside of Canada may be able to rely on certain “international” exemptions from the requirement to register for certain activities in Canada. Dealing only with permitted clients is a condition common to reliance on each of the international adviser, dealer and IFM exemptions. See *question 1.8*. A similar exemption is available under commodity futures legislation in Ontario.

1.3 Are Alternative Investment Funds themselves required to be licensed, authorised or regulated by a regulatory body?

An AIF is not required to be licensed or authorised by any regulatory body. In Canada, the sale of AIF securities to the public is subject to a prospectus requirement, meaning that an AIF must either file a prospectus or rely on an exemption from such requirement in order to distribute securities. The “accredited investor” exemption is the most common exemption relied on to distribute both domestic and non-resident AIF securities. Non-resident AIF securities can be distributed on a private placement basis to accredited investors and other exempt purchasers by registered dealers, and to “permitted clients” by foreign dealers under the “international dealer exemption”.

1.4 Does the regulatory regime distinguish between open-ended and closed-ended Alternative Investment Funds (or otherwise differentiate between different types of funds or strategies (e.g. private equity vs hedge)) and, if so, how?

There is no such distinction in Canada, but as noted above, Canadian securities laws distinguish between “investment funds” and non-investment funds.

Under Canadian securities laws, the two main types of “investment funds” are “mutual funds” and “non-redeemable investment funds”. A “mutual fund” is an issuer whose securities are redeemable on demand with reference to the fund’s net assets. A “non-redeemable investment fund” is an issuer that is not a mutual fund and that does not invest for the purpose of exercising or seeking to exercise control of an issuer or for the purpose of being actively involved in the management of any issuer in which it invests.

In Canada, “investment funds” are intended to be diversified, passive investors and are distinguished from other funds that may carry on active business or exercise control over, or be involved in the management of, an investee company or hold securities representing more than 10% of an investee company’s securities. AIFs that typically are not considered to be investment funds include private equity and venture capital funds, direct lending and factoring funds and real estate funds. Also excluded from the definition of investment fund are investment entities under IFRS, business income trusts, real estate investment trusts (REITs) and royalty trusts.

1.5 What does the authorisation process involve for managers and, if applicable, Alternative Investment Funds, and how long does the process typically take?

A manager of an AIF that is not a “investment fund” is not subject to authorisation. See *question 1.8*. Similarly, there is no authorisation process for AIFs that do not file a prospectus. By accessing the capital markets, AIFs and investment funds will become “market participants” subject to the oversight of the applicable securities regulators and examination of the books, records and documents that are required to be kept by a market participant.

As noted above under *question 1.2*, a manager of an “investment fund” for Canadian securities purposes must register as an IFM. An adviser managing an investment fund’s portfolio must be registered as a portfolio manager. Securities of an investment fund must be distributed through registered dealers.

Registration is a harmonised process in Canada and entails the filing of an application for registration of a sponsor firm and each individual seeking to be registered with a sponsor firm. In Ontario, the registration process exceeds the six-month target service standard established by the Ontario Securities Commission (OSC) and can take considerably longer.

1.6 Are there local residence or other local qualification or substance requirements for managers and/or Alternative Investment Funds?

Generally, no. Non-resident managers can obtain registration as an IFM or a portfolio manager in Canada without a physical presence in Canada.

Non-resident managers without a physical presence in Canada seeking to obtain registration or filing to rely on the international adviser exemption must file a submission to the jurisdiction and appoint an agent for service for each jurisdiction where the firm is seeking registration. There are also requirements under the corporate legislation of certain Canadian jurisdictions that require firms that are “carrying on business” in such jurisdictions to register as extra-provincial corporations.

AIFs structured as limited partnerships may need to be extra-provincially registered as a result of carrying on, or being deemed to carry on, business in certain provinces or territories. Such registration may be necessary or desirable to ensure limited liability treatment for limited partners.

Subject to certain exceptions, portfolio assets of prospectus-qualified mutual funds held in Canada must be held by a Canadian custodian. The Canadian custodian requirement effectively restricts non-resident mutual funds from filing a prospectus in Canada.

1.7 What service providers are required?

AIFs that are investment funds must appoint a registered IFM and a registered portfolio manager.

Prospectus-qualified mutual funds must appoint a prescribed Canadian custodian and a public accounting firm that participates in the Canadian Public Accountability Board (CPAB) oversight programme.

Registered firms including managers that hold or have access to the cash or securities of a client including an AIF must, subject to certain exceptions, appoint a Canadian custodian.

Registered firms are also required to use the Ombudsman for Banking Services and Investments (OBSI) as their provider of dispute resolution services for disputes with clients outside of Quebec.

1.8 What rules apply to foreign managers or advisers wishing to manage, advise, or otherwise operate funds domiciled in your jurisdiction?

Foreign managers that manage or advise AIFs that are not investment funds do not have to be registered in Canada. A distribution of securities of such an AIF is subject to the prospectus requirement and the dealer registration requirement.

The distribution of securities of non-resident investment funds in Canada requires IFM registration in the Provinces of Ontario, Quebec and Newfoundland and Labrador if the investment fund has a security holder from such province, unless an exemption from such registration is available.

A foreign portfolio manager can act as portfolio manager for a Canadian investment fund by:

- registering as a portfolio manager;
- acting as a sub-adviser to a Canadian registered adviser or registered dealer; or
- relying on an exemption, such as the international adviser exemption, to advise “permitted clients” (other than registered dealers or advisers), provided that advising on securities of Canadian issuers is incidental to its advice on a foreign security and subject to satisfying all the conditions.

1.9 What relevant co-operation or information sharing agreements have been entered into with other governments or regulators?

Securities regulators in the Provinces of Alberta, British Columbia, Ontario and Quebec have entered into Memoranda of Understanding (MOUs) specific to AIFs concerning consultation, cooperation and the exchange of information related to the supervision of cross-border AIF managers with each of the EU and EEA Members under the EU Alternative Investment Fund Managers Directive (AIFMD), the UK Financial Conduct Authority, the Croatian Financial Services Supervisory Agency and the Gibraltar Financial Services Commission. The purpose of these supervisory MOUs is to facilitate consultation, cooperation and the exchange of information related to the supervision of AIF managers that operate on a cross-border basis in the jurisdictions of both the relevant offshore and Canadian authorities.

Canadian securities regulators have also entered into a number of international MOUs with international partners to foster cooperation and information sharing on various matters, including enforcement.

2 Fund Structures

2.1 What are the principal legal structures used for Alternative Investment Funds (including reference where relevant to local asset holding companies)?

AIFs are typically structured as limited partnerships and trusts. Trusts are often structured to meet the conditions necessary

to qualify as a “mutual fund trust” for Canadian income tax purposes. The choice of structure is generally driven by the particular investment strategy of the fund, its target investor base and related tax considerations.

For example, securities of mutual fund trusts are qualified investments for registered plans under the *Income Tax Act* (Canada) (Tax Act), a feature that can expand the universe of prospective investors since many Canadians hold retirement and other savings in registered plans such as registered retirement savings plans, tax-free savings accounts, first home savings accounts and other similar plans.

2.2 Do any of the legal structures operate as an umbrella structure with several sub-funds, and if yes, is segregation of assets between the sub-funds a legally recognised feature of the structure?

Umbrella structures have not been introduced in Canada.

2.3 Please describe the limited liability of investors in respect of different legal structures and fund types (e.g. PE funds and LPACs).

As a general rule, Canadian law holds that the shareholders of a corporation are not liable for the debts of the corporation.

The liability of limited partners for the debts and other liabilities of a limited partnership is limited to the value of money and other property contributed or agreed to be contributed, except where the limited partner takes part in the control of the business of the partnership. Representation on a limited partner advisory committee (LPAC) and the exercise of customary LPAC powers typically would not result in an investor being found to be taking part in the control of the business of the partnership, subject to review on a case-by-case basis.

Investors in a trust are likely to have limited liability but there is a risk, generally considered to be remote, that an investor could have liable personal liability in the event of a lawsuit against the trust. This risk can be addressed by providing in contracts of the trust, where possible, that no recourse may be had to the personal assets of investors. To address this risk in the public markets, some provinces have adopted legislation that provides for statutory limited liability for unitholders of trusts that are reporting issuers.

2.4 What are the principal legal structures used for managers and advisers of Alternative Investment Funds?

Managers and advisers are typically organised as corporations, including unlimited liability companies (ULCs), but are also structured as general partnerships and limited partnerships.

2.5 Are there any limits on the manager's ability to restrict redemptions in open-ended funds or transfers in open-ended or closed-ended funds?

There are no such restrictions on AIFs that are not offered by prospectus. A transfer of securities of an AIF that is not a reporting issuer is subject to resale restrictions, and an investor must rely on a private placement exemption to effect a transfer in addition to complying with fund documentation.

AIFs that are investment funds offered by prospectus are subject to redemption requirements under NI 81-102 *Investment Funds* (NI 81-102). Securities of listed closed-ended funds and

exchange-traded funds (ETFs) are freely transferable on a stock exchange. Securities of public AIFs that are not listed are typically redeemed rather than being transferred.

Certain AIFs may restrict ownership by non-resident investors in order to preserve their Canadian tax status. See *question 3.9*.

In certain circumstances, limitations on redemptions may cause a trust not to qualify as a mutual fund trust for purposes of the Tax Act.

2.6 Are there any legislative restrictions on transfers of investors' interests in Alternative Investment Funds?

AIF securities acquired pursuant to a prospectus exemption from an AIF that is not a reporting issuer are subject to resale restrictions. Any resale of such securities is subject to the prospectus requirement unless made under an exemption from the prospectus requirement, such as the accredited investor exemption.

2.7 Are there any other limitations on a manager's ability to manage its funds (e.g. diversification requirements, asset stripping rules)?

Prospectus-qualified investment funds are subject to certain restrictions and requirements under NI 81-102 that are designed in part to ensure that the investments of the mutual fund are diversified and relatively liquid and to ensure the proper administration of the mutual fund. These include investment restrictions relating to investments for control, investments in real property and loan syndications, investments in other investment funds (fund-on-fund structures) as well as illiquid securities and the use of leverage and derivatives, short-selling and securities lending.

2.8 Does the fund remunerate investment managers through management/performance fees or by a combination of management fee and carried interest? In the case of carried interest, how is this typically structured?

Canadian AIFs typically remunerate investment managers by a combination of management fee and carried interest.

Carried interest can be structured as a fee (which attracts sales tax) or, in the case of AIFs structured as limited partnerships, as an allocation of income that may receive capital gains treatment.

Managers of publicly offered investment funds are generally remunerated through management fees. Public funds with incentive fees are less common and such fees must comply with requirements under NI 81-102.

3 Marketing

3.1 What legislation governs the production and use of marketing materials?

Under Canada securities laws, a “trade” is broadly defined to include not only the sale of a security, but also any act, solicitation or conduct that is directly or indirectly in furtherance of the sale of a security. Consequently, sending or transmitting of marketing materials to an investor will generally be characterised as an activity in furtherance of a “trade” under the securities laws, subject to the prospectus and dealer registration requirements.

In addition, Canada’s Anti-Spam Law (CASL) imposes significant limitations on the electronic marketing practices and processes of businesses that send commercial electronic

messages (CEMs) to recipients in Canada. For the purposes of CASL, a CEM is an electronic message that, having regard to the content of the message, the hyperlinks in the message to content on a website or other database, or the contact information contained within the message, has as its purpose, or one of its purposes, to encourage participation in a commercial activity. An electronic message includes, but is not limited to, an email or other electronic messaging or social media communication, including a text, sound, voice or image message. As a result, the law governs not only direct solicitations, but also a broad range of advertising, marketing and general promotional activity.

3.2 What are the key content requirements for marketing materials, whether due to legal requirements or customary practice?

Best practices for marketing are set out in regulatory notices of the Canadian Securities Administrators (CSA) and the OSC, including CSA Staff Notice 31-325 *Marketing Practices of Portfolio Managers* and OSC Staff Notice 33-729 *Marketing Practices of Investment Counsel/Portfolio Managers Prospectus*. Prospectus-qualified mutual funds are subject to NI 81-105 *Mutual Fund Sales Practices*.

For private placements generally, there is no required disclosure document or prescribed content for marketing materials. However, an offering memorandum (OM) delivered to prospective investors in certain provinces must include prescribed disclosure relating to purchaser statutory rights of action for damages or rescission where the OM contains a misrepresentation, and disclosure relating to certain conflicts of interest.

Securities of non-resident AIFs can be issuers of eligible foreign securities and may avail themselves of exemptions from the requirement to disclose some of this information provided that certain conditions are met, including the requirement to restrict any distribution to investors that are qualified “permitted clients”.

3.3 Do the marketing or legal documents need to be registered with or approved by the local regulator?

As a general rule, marketing and legal documents of AIFs offered by way of a private placement do not have to be registered with or approved by Canadian securities regulators.

In some provinces, when an OM is provided to a prospective purchaser, a copy of the OM must be delivered to, or filed with, the applicable provincial securities regulator within 10 days of the distribution made under the OM. This requirement also applies to any standalone Canadian “wrapper” that is delivered to prospective Canadian investors along with the foreign prospectus or private placement memorandum.

3.4 What restrictions (and, if applicable, ongoing regulatory requirements) are there on marketing Alternative Investment Funds?

Marketing of AIF securities is considered an act in furtherance of a trade of securities and, as such, subject to the prospectus and registration requirements as outlined above unless an exemption is available.

3.5 Is the concept of “pre-marketing” (or equivalent) recognised in your jurisdiction? If so, how has it been defined (by law and/or practice)?

In Canada, the concept of pre-marketing applies in the context of a prospectus offering; it does not apply to the private placement

of AIF securities. In general, any advertising or marketing activities undertaken in connection with a prospectus prior to the issuance of a receipt for the preliminary prospectus are prohibited under securities legislation by virtue of the prospectus requirement. Any marketing activity directed to potential Canadian investors would be an act in furtherance of a trade and, as such, subject to the prospectus and registration requirements as outlined above unless an exemption is available.

3.6 Can Alternative Investment Funds be marketed to retail investors (including any specific treatment for high-net-worth individuals or semi-professional or similar categories)?

As a general rule, AIFs cannot be marketed to retail investors unless the distribution is qualified by a prospectus.

Securities of resident and non-resident AIFs are commonly distributed on a private placement basis to “accredited investors” (as such term is described under *question 3.7*).

The “offering memorandum exemption” may allow an AIF to solicit investments from a wider range of investors than under other prospectus exemptions subject to preparing a prescribed form of OM (including audited financial statements) and subject to limits that apply on how much can be invested by individuals. In some jurisdictions (e.g. Ontario), this exemption is not available to AIFs that are investment funds.

Prospectus offerings can be distributed only by registered investment dealers or mutual fund dealers. Exempt market dealers can market and sell investment funds to retail investors who qualify as “accredited investors” in reliance on the accredited investor exemption or another prospectus exemption under NI 45-106.

Some non-resident AIFs, such as private equity funds, opt to distribute their securities without engaging a registered dealer on the basis that the AIF has non-securities-related business and that their capital raising activities are occasional and uncompensated, such that the business trigger for dealer registration is not met. If the business trigger for dealer registration is met, securities of non-resident AIFs can be distributed to “permitted clients” in reliance on the international dealer exemption or by a local registered dealer, such as an exempt market dealer.

Some non-resident AIFs, such as private equity funds, opt to distribute their securities without engaging a registered dealer on the basis that the AIF has non-securities-related business and that their capital raising activities are occasional and uncompensated, such that the business trigger for dealer registration is not met. If the business trigger for dealer registration is met, securities of non-resident AIFs can be distributed to “permitted clients” in reliance on the international dealer exemption or to “accredited investors” by a local registered dealer, such as an exempt market dealer.

3.7 What qualification requirements must be met in relation to prospective investors?

AIF securities distributed by way of a private placement in Canada are generally marketed and sold to two categories of qualified investors: “accredited investors”; and “permitted clients”.

In general terms, the term “accredited investor” includes various institutions such as banks, trust companies, pension funds, municipalities, certain investment funds, entities (other than investment funds) that have net assets of at least C\$5 million (as shown on their most recent financial statements) and individuals meeting the following criteria:

- Net income before taxes was more than C\$200,000 in each of the two most recent calendar years and is expected to be more than C\$200,000 in the current calendar year.
- Net income before taxes combined with a spouse was more than C\$300,000 in each of the two most recent calendar years and their combined net income is expected to be more than C\$300,000 in the current calendar year.
- Financial assets, alone or with a spouse, of more than C\$1 million before taxes but net of related liabilities.
- Net assets, alone or with a spouse, worth more than C\$5 million.

The term “permitted client” includes a similar list of institutional investors, but the financial tests for individuals and entities are much higher. A permitted client includes individuals who beneficially own net financial assets in excess of C\$5 million and persons or companies, other than individuals or investment funds, that have net assets of at least C\$25 million (as shown on their most recently prepared financial statements).

3.8 Are there additional restrictions on marketing to public bodies such as government pension funds?

Subject to compliance with dealer registration requirements and CASL, there are no restrictions on marketing to public bodies such as government pension funds.

3.9 Are there any restrictions on the participation in Alternative Investment Funds by particular types of investors (whether as sponsors or investors)?

There are no such restrictions. In order to preserve their Canadian tax status, Canadian AIFs formed as limited partnerships may form a parallel partnership for non-resident investors, and some mutual fund trusts may cap ownership by non-residents.

3.10 Are there any restrictions on the use of intermediaries to assist in the fundraising process?

In Canada, fundraising intermediaries must be registered as a dealer unless an exemption is available. AIF managers and sponsors that engage a registered dealer in Canada can rely on an exemption from the dealer registration requirement for trades to or through a registered dealer. This is also referred to as the “wholesaling exemption”. The exemption is not available if a manager or sponsor solicits or contacts directly any purchaser or prospective purchaser in relation to the trade.

4 Investments

4.1 Are there any restrictions on the types of investment activities that can be performed by Alternative Investment Funds?

AIFs generally are not subject to any such restrictions. AIFs that are investment funds and offered by way of prospectus are subject to investment restrictions under NI 81-102, designed in part to ensure that the investments of the fund are diversified and relatively liquid. See *question 2.7*.

Depending on the structure of the AIF, the Tax Act may impose certain restrictions on its investment activities.

4.2 Are there any limitations on the types of investments that can be included in an Alternative Investment Fund's portfolio, whether for diversification reasons or otherwise?

See *question 4.1*.

4.3 Are there any local regulatory requirements that apply to investing in particular investments (e.g. derivatives or loans)?

Portfolio managers that advise AIFs resident in the Province of Quebec with respect to investing in derivatives may have to register under the *Derivatives Act* (Quebec). Portfolio managers that advise AIFs resident in the Provinces of Ontario or Manitoba with respect to commodity futures contracts or options may have to register under applicable commodity futures legislation or file to rely on an exemption (in Ontario).

Some regulated sectors in Canada have sector-specific legislation regulating investments (including foreign investments) into undertakings in these sectors, including for telecommunications companies (*Telecommunications Act*), broadcasting companies (*Broadcasting Act*), financial institutions (*Bank Act*) and transportation undertakings (*Canada Transportation Act*), but these restrictions are not unique to AIFs.

4.4 Are there any restrictions on borrowing by the Alternative Investment Fund?

AIFs generally are not subject to any such restrictions. AIFs that are investment funds and offered by way of prospectus are subject to NI 81-102 restrictions on cash borrowing, short sales and leverage through the combined use of borrowing, short-selling and specified derivatives.

4.5 Are there any restrictions on who holds the Alternative Investment Fund's assets?

Assets of Canadian AIFs that are managed by registered firms or that are investment funds must be held by a qualified custodian. Under NI 31-103, cash and assets of clients of registered firms must be held by a Canadian custodian unless it is more beneficial to use a “foreign custodian”. The assets of a prospectus-qualified investment fund must be held by one Canadian custodian that satisfies the requirements of NI 81-102.

There are additional custodian requirements with respect to AIFs that invest in or hold cryptoassets. In addition to being licensed as a trust company pursuant to the requirements of section 1.1 of NI 31-103 and satisfying minimum capital requirements, the custodians of cryptoassets must also have completed a Service Organization Controls (SOC) report under the SOC 1 Type 1 and SOC 2 standards from a leading global audit firm with respect to cryptoassets held in hot and cold wallets.

5 Disclosure of Information

5.1 What disclosure must the Alternative Investment Fund or its manager make to prospective investors, investors, regulators or other parties, including on environmental, social and/or governance factors?

See *question 3.2* for prescribed OM disclosure.

An AIF that is a mutual fund formed in Canada may have to comply with the financial statement requirements of NI 81-106. An exemption from the requirement to file these financial

statements with the securities regulators may be available if such financial statements can be prepared and delivered to investors as prescribed by the rules. If the AIF is not formed in Canada, there are no ongoing public disclosure requirements.

Investment funds that are reporting issuers are required to file and deliver, in addition to the annual audited financial statements and semi-annual unaudited financial statements, annual and interim management reports of financial performance (MRFPs), quarterly portfolio disclosure, proxy voting disclosure, and NAV weekly (if the fund does not use specified derivatives or make short sales), otherwise daily.

Best practice guidance for investment fund disclosure with respect to environmental, social and governance (ESG) consideration is set out in CSA Staff Notice 81-334 *ESG Related Investment Fund Disclosure*. The guidance is especially relevant to investment funds whose investment objectives reference ESG factors and investment funds that use ESG strategies, in the following areas: (i) investment objectives and fund names; (ii) fund types; (iii) investment strategies disclosure; (iv) proxy voting and shareholder engagement policies and procedures; (v) risk disclosure; (vi) suitability; (vii) continuous disclosure; (viii) sales communications; (ix) ESG-related changes to existing funds; and (x) ESG-related terminology.

5.2 Are there any requirements to provide details of participants (whether owners, controllers or investors) in Alternative Investment Funds or managers established in your jurisdiction (including details of investors) to any local regulator or record-keeping agency, for example, for the purposes of a public (or non-public) register of beneficial owners?

If securities of an AIF are sold by way of a private placement, a report of exempt distribution on Form 45-106F1 generally must be filed with the securities regulator of the province where the Canadian investor purchasing securities is resident. Among other information on the fund and any compensation paid to a dealer, the form requires that the amount of investment and details of the investor be provided. The investor information provided to the securities regulator is not publicly available. Freedom of information legislation may require the securities regulator to make this information available if requested, although securities regulators have indicated that any such freedom of information requests for investor information contained in a Form 45-106F1 would be opposed by securities regulators.

In the Province of Ontario, a limited partnership must maintain, at the limited partnership's place of business, a record of limited partners setting out each partner's name and address and Ontario corporation number, if any, and the amount of money and the value of other property contributed or to be contributed by the partner to the limited partnership. The record is open to inspection by any person.

Investment funds that are structured as corporations must maintain registers of beneficial owners, which are publicly available in certain provinces.

5.3 What are the reporting requirements to investors or regulators in relation to Alternative Investment Funds or their managers, including on environmental, social and/or governance factors?

See *question 5.1*.

5.4 Is the use of side letters restricted?

No, the use of side letters is not restricted.

6 Taxation

6.1 What is the tax treatment of the principal forms of Alternative Investment Funds and local asset holding companies identified in question 2.1?

An AIF that is structured as a trust is subject to tax in Canada on its net income, but in computing its net income the trust is generally able to deduct distributions paid to unitholders. Generally, a trust will make sufficient distributions each year so that the trust itself is not liable for Canadian income tax.

A partnership is generally not subject to Canadian income tax; rather, income of the partnership is allocated to the partners in accordance with the partnership agreement. See *question 6.4*.

6.2 What is the tax treatment of the principal forms of investment manager/adviser identified in question 2.4?

Fees paid to the manager will generally be treated as ordinary income to the manager.

If the manager is a Canadian resident corporation, it will be subject to Canadian income tax on its worldwide income.

If the manager is a partnership, the partners will be subject to tax on income allocated to them from the partnership regardless of whether the partnership has made distributions. See *question 6.4*.

Note that if the AIF itself is a partnership, the partnership will generally be structured so that any carried interest is paid to a special limited partner (usually an affiliate of the manager/general partner) as a partnership distribution rather than a fee, and income will be allocated to the special limited partner by the AIF in accordance with the partnership agreement (and should retain its character as ordinary income or capital gains).

6.3 Are there any establishment or transfer taxes levied in connection with an investor's participation in an Alternative Investment Fund or the transfer of the investor's interest?

Transfers and redemptions are taxable events for income tax purposes. There are generally no establishment or sales taxes imposed on investors who acquire or transfer their interests; however, in some circumstances, land transfer tax may apply on the transfer of an interest in an AIF that holds certain Canadian real property.

6.4 What is the local tax treatment of (a) resident, (b) non-resident, and (c) pension fund investors (or any other common investor type) in Alternative Investment Funds?

A trust unitholder that is resident in Canada is generally required to include in income for a particular taxation year the portion of the net income of the trust for a taxation year, including the taxable portion of net realised capital gains, that is paid or payable to the unitholder in the year. Capital gains, taxable dividends, and foreign source income earned by the trust will generally retain their character in the hands of the unitholder provided appropriate designations are made by the trust.

Distributions of income by a trust (other than capital gains in most cases) that are made to non-residents of Canada from the trust are generally subject to Canadian withholding tax.

Holders of partnership interests are subject to tax on income allocated to them from the partnership, regardless of whether a distribution is received from the partnership. In general, a

partner's share of any income or loss of the partnership from a particular source (including the partner's share of capital gains and losses of the partnership) will retain its character as such in the hands of the partner. Distributions received by a partner from the partnership are generally not in and of themselves taxable but will reduce the cost base of the partner's partnership interest. If the cost base becomes a negative amount, the partner will generally realise a capital gain.

Partnerships are generally not required to withhold tax on distributions paid to non-residents of Canada (however, dividends and certain other amounts paid to the partnership by Canadian issuers may be subject to Canadian withholding tax if the partnership has any non-resident members). Subject to certain exceptions, if the partnership carries on business in Canada, non-resident partners could become subject to income tax in Canada unless an exemption is available under an applicable income tax treaty.

Canadian pension funds are generally tax exempt.

6.5 Is it necessary or advisable to obtain a tax ruling from the tax or regulatory authorities prior to establishing an Alternative Investment Fund or local asset holding company?

It is not necessary to obtain a tax ruling and is not advisable in most circumstances.

6.6 What steps have been or are being taken to implement the US Foreign Account Tax Compliance Act 2010 (FATCA) and other similar information reporting regimes such as the OECD's Common Reporting Standard?

The Tax Act has been amended to incorporate the due diligence and reporting requirements under FATCA and the Common Reporting Standard.

6.7 What steps have been or are being taken to implement the OECD's Action Plan on Base Erosion and Profit Shifting (BEPS), in particular Actions 2 (hybrids/reverse hybrids/shell entities) (for example, ATAD I, II and III), 6 (prevention of treaty abuse) (for example, the MLI), and 7 (permanent establishments), insofar as they affect Alternative Investment Funds' and local asset holding companies' operations?

Canada has joined the two-pillar plan for international tax reform. Amendments to the Tax Act have been proposed to, among other things, address hybrid mismatch arrangements as well as excessive interest and financing expenses. The MLI is currently in force in Canada.

Canada is a signatory to the MLI, which entered into force in Canada at the end of 2019.

6.8 Are there any tax-advantaged asset classes or structures available? How widely are they deployed?

Generally, no. Only 50% of capital gains are subject to income tax in Canada, so investors may prefer capital gains to ordinary income. Mutual fund trusts can elect to have all gains (and losses) realised on the disposition of securities that are "Canadian securities" (for purposes of the Tax Act) deemed to be capital gains (or losses) to the trust.

6.9 Are there any other material tax issues for investors, managers, advisers or AIFs?

The Tax Act contains rules relating to the taxation of publicly traded trusts, partnerships and their investors (the SIFT Rules). Trusts and partnerships to which the SIFT Rules apply will be subject to entity-level taxation. The SIFT Rules generally do not apply if (i) investments in the fund are not listed or traded on a stock exchange or other public market, or (ii) the fund does not hold any "non-portfolio property" for purposes of the Tax Act. Most funds conduct their affairs so that they are not subject to these rules.

6.10 Are there any meaningful tax changes anticipated in the coming 12 months other than as set out at question 6.6 above?

No, other than amendments related to BEPS. See *question 6.7*.

7 Trends and Reforms

7.1 What have been the main trends in the Alternative Investment Funds space in the last 12 months?

The continued "retailisation" of AIF strategies is a current trend in Canada. Accredited investors have gained access to AIFs and strategies normally restricted to institutional investors by way of sponsor formed and managed feeder funds as well as third-party formed and managed "access funds". The underlying AIF strategies include private equity, debt funds (including U.S. business development corporations (BDCs) and real estate (including U.S. REITs)).

7.2 What reforms (if any) in the Alternative Investment Funds space are proposed?

Although no reforms are currently proposed, the AIF space may be affected by ongoing initiatives of the OSC with respect to investment funds. For example, the OSC has announced its intention to continue to strengthen the regulatory framework to better assess liquidity risk and leverage associated with investment funds. To assess liquidity, leverage, and other risks in funds, the OSC continues to expand its data collection efforts, including an annual investment fund survey.



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