

# Registration Reform

IN CANADA

*The Finish Line is Here*

Section A of Stikeman Elliott's Report on Canada's New Registration Regime  
JULY 2009

**Overview of Canada's New Registration Regime**



# Registration Reform IN CANADA

*The Finish Line is Here*

A

## Overview of Canada's New Registration Regime

On July 17, 2009, the Canadian Securities Administrators (CSA) published their final proposal for National Instrument 31-103 *Registration Requirements and Exemptions* (31-103), and revocations of, or amendments to, a number of related instruments and policies. This final proposal results from two comment and review processes that started in 2007, with the first proposal published in February 2007 and the second proposal published in February 2008. Both proposals were the subject of substantial comments. 31-103 is scheduled to come into force on September 28, 2009 (the Implementation Date), subject to government and other local approvals in each province and territory. Transition and grandfathering provisions vary for different aspects of the new regime.

31-103 is intended to harmonize, streamline and modernize registration requirements and exemptions across all Canadian provinces and territories (jurisdictions). It regulates the registration of firms and individuals and consolidates requirements for registration, including proficiency, solvency and insurance requirements, as well as ongoing compliance requirements for registrants. These include requirements with respect to financial reporting, know your client, suitability, client disclosure, safekeeping of assets, recordkeeping, account activity reporting, complaint handling and other compliance procedures. The CSA note that, to create flexible regulation, 31-103 combines principles, supported by guidance in its companion policy, with prescriptive elements where considered appropriate.

31-103 represents a major overhaul of the current registration regime and has significant implications for Canadian and non-Canadian dealers, advisers and investment fund managers currently doing business on a registered or exempt basis in any jurisdiction of Canada.

© STIKEMAN ELLIOTT LLP JULY 2009

This publication provides general commentary only and is not intended as legal advice.

For further information, please contact your Stikeman Elliott representative or any member of our Securities Group at [www.stikeman.com](http://www.stikeman.com)

The new rules will also have significant implications for private placements and other capital market activities.

Significant changes resulting from the new registration regime include:

- the removal of most dealer registration exemptions, including for trades with “accredited investors” (except in a few jurisdictions in very limited circumstances), and the move to a “business trigger” for the dealer registration requirement; this change effectively requires that all persons that are in the business of trading in securities in Canada register as dealers;
- the requirement that persons who are in the business of trading in the so-called “exempt market”, including those now registered in Ontario or Newfoundland and Labrador as limited market dealers, be registered as “exempt market dealers”, and subject to capital, insurance and proficiency requirements and other ongoing compliance requirements;
- the introduction of a new investment fund manager registration requirement;
- the introduction of registration exemptions for international dealers and international advisers;
- the introduction of principles-based rules for managing conflicts of interest;
- the regulation of referral arrangements; and
- the introduction of new client complaint handling and dispute resolution procedures.

### **Not in Perfect Harmony – What Imperfect Harmonization Means for Market Participants**

Each of Canada’s thirteen jurisdictions has its own securities legislation and securities regulator and in some cases its own approach to implementation of the new registration regime. All jurisdictions are not taking a fully harmonious approach with the new registration regime, although on the business trigger for dealer registration, the CSA believe that functional harmonization has been reached since anyone who is in the business of trading in securities must register as a dealer. As to the aspects where there are differences, some jurisdictions, in particular the western provinces and the territories, are providing limited exemptions from the requirement that a person in the business of trading in securities in the exempt market register as an exempt market dealer. Ontario alone will have the sub-adviser exemption from the adviser registration requirement. In Quebec, firms and individuals in the mutual fund and scholarship plan sector are subject to a specific regulatory framework that differs from other jurisdictions. While the differences are generally modest and often of form rather than substance, the result is that market participants will have to continue to consider some local requirements in connection with their activities.

## “Business Trigger” for Registration

Currently, the dealer registration requirement is triggered by the act of trading in a security. With the implementation of 31-103 and related legislative amendments, the dealer registration requirement will be triggered by being in the “business of trading” in securities as principal or agent. The introduction of the “business trigger” for the dealer registration requirement may eliminate the need for certain persons to register as a dealer if they carry out limited trades and are not otherwise in the “business of trading” in securities.

The requirement to register as an adviser is already based on a “business trigger” and no change in this approach is contemplated under the new registration regime.

Companion Policy 31-103CP *Registration Requirements and Exemptions* (31-103CP) provides guidance on how the CSA will interpret the provisions of 31-103 and describes a number of factors to consider in determining whether a person is in the “business of trading” or advising. Under 31-103CP, the business trigger analysis focuses on the type of activity (trading or advising) and whether it is conducted as a business. The mere fact of holding oneself out as being in the business of trading or advising is sufficient to engage the registration requirement. Other factors which alone may not be determinative, but which in one or more combinations may be indicative of a business purpose, include acting in an intermediary capacity between a seller and a buyer of securities or making a market in securities, carrying on the activity with repetition, regularity or continuity, receiving or expecting to receive compensation for carrying on the activity (whether transaction or value based) and direct or indirect solicitation activities.

31-103CP discusses the application of the business trigger factors for various parties and activities, including securities issuers, venture capital and private equity investing and incidental activities such as M&A advisory activities and other professional activities where the trading or advising activity involved may not be considered to be for a business purpose.

In conjunction with the move to a “business trigger” for the dealer registration requirement, the dealer registration exemptions currently set out in National Instrument 45-106 *Prospectus and Registration Exemptions* (45-106) will be repealed, including the “accredited investor” exemption, subject to limited exceptions in certain jurisdictions. The prospectus exemptions in 45-106, including that for distributions to “accredited investors”, will generally remain unchanged.

## Registration Required for Investment Fund Managers

Persons acting as investment fund managers will now be required to register in a new category of investment fund manager. An investment fund manager is a person that directs the business, operations or affairs of an “investment fund”. (For a discussion of the meaning of “investment fund” see the discussion under the topic Impact on Private Equity and Venture Capital Funds). The investment fund manager need not be acting as the portfolio manager of the fund for the

investment fund manager to become subject to the registration requirement. Registrants in this category will be subject to capital, insurance and proficiency requirements for their chief compliance officers and other ongoing compliance obligations.

Managers of all types of investment funds will become subject to registration in this new category, including managers of funds typically characterized as mutual funds, non-redeemable investment funds, labour-sponsored investment funds, scholarship plans, pooled funds or hedge funds. Whether the manager of a fund that is described as a private equity fund or a venture capital fund will be subject to this registration requirement will require careful consideration of the facts specific to the fund. 31-103 does not provide any registration exemption for managers of funds of these types, the question being whether the registration requirement is triggered for them.

If a firm carries on the activities of an investment fund manager it must register as such. The “business trigger” does not apply for this registration requirement. The CSA plan to publish a proposal for comment during the upcoming year describing under what circumstances an investment fund manager that (i) has a head office outside of Canada would be required to register, or (ii) that has a head office in Canada and that is registered in that jurisdiction in Canada would be required to register in another Canadian jurisdiction.

### **Categories of Registration and Permitted Activities**

31-103 introduces new categories of registration, and removes and consolidates several other categories. The categories of registration under 31-103 are the following:

***Investment Dealer*** – permitted to trade in any security with any type of client. An investment dealer is also permitted to act as an underwriter in respect of any security.

***Mutual Fund Dealer*** – permitted to trade only in securities of mutual funds and, except in Quebec, securities of investment funds that are labour sponsored investment corporations or labour sponsored venture capital corporations under provincial legislation.

***Scholarship Plan Dealer*** – permitted to trade only in securities of scholarship plans, educational plans or educational trusts.

***Exempt Market Dealer*** – permitted to trade only in securities distributed under a prospectus exemption, whether or not a prospectus was filed in respect of the distribution, or in securities that, if the trade were a distribution, would be exempt from the prospectus requirement. An exempt market dealer is also permitted to act as an underwriter in a distribution of securities that is made under a prospectus exemption. With the introduction of this new category of registration, the current limited market dealer category in Ontario and Newfoundland and Labrador will be repealed.

**Restricted Dealer** – permitted to carry on business under terms and conditions imposed by the local regulator. This category is intended for specialized dealers that would not necessarily qualify for an unrestricted dealer registration.

**Portfolio Manager** – permitted to advise any type of client with regard to any security. Portfolio managers include advisers with or without discretionary authority.

**Restricted Portfolio Manager** – permitted to advise in specific securities, classes of securities or the securities of a class of issuers, subject to the terms and conditions imposed by the local regulator.

**Investment Fund Manager** – permitted to direct the business, operations or affairs of an investment fund.

Where the firm carries on business in more than one registrable activity, then unless otherwise exempt, the firm must register in all applicable categories and comply with the most stringent registration and ongoing compliance requirements. For example, certain investment fund managers, as a result of their activities, may become subject to a triple registration requirement (namely, as investment fund manager, adviser and dealer).

### **International Dealer and International Adviser Exemptions**

The key changes introduced by 31-103 for non-Canadian dealers are (1) the elimination of the international dealer category of dealer registration in Ontario and Newfoundland and Labrador and (2) the repeal of the accredited investor exemption and other dealer registration exemptions currently available under 45-106 in all Canadian jurisdictions other than in limited cases in Alberta, British Columbia, Manitoba, and the territories.

Significantly, 31-103 introduces a new “international dealer exemption” in all Canadian jurisdictions. Provided the applicable conditions are met, the exemption permits non-Canadian dealers to trade in “foreign securities” and certain debt instruments with “permitted clients”, a subset of “accredited investors” under 45-106. “Permitted Clients” include institutional investors, persons or companies, other than individuals or investment funds, with net assets exceeding \$25,000,000 and individuals with net financial assets exceeding \$5,000,000. The practical effect of the international dealer exemption is to narrow the list of persons with which a non-Canadian dealer is permitted to trade on an exempt basis outside Ontario and Newfoundland and Labrador and to eliminate the requirement to register as a dealer in Ontario and Newfoundland and Labrador to trade on this limited basis. A non-Canadian dealer would be required to register as an exempt market dealer in order to trade with the full range of accredited investors in all types of securities, in which case it would be subject to the registration conditions and ongoing compliance obligations for that category of registration. (For a discussion of the international dealer exemption and its requirements, see the topic Impact on International Dealers and Non-Canadian Dealers Trading in the Exempt Market.)

The key changes introduced by 31-103 for non-Canadian advisers are the elimination of the international adviser and portfolio manager & investment

counsel (foreign) registration categories in Ontario and Alberta, respectively. 31-103 introduces an “international adviser exemption” in all Canadian jurisdictions which, provided the applicable conditions are met, permits a non-Canadian adviser to advise “permitted clients” in Canada on “foreign securities”. Where the “international adviser exemption” cannot be relied upon, the non-Canadian adviser will be required to register as a “portfolio manager” and will be subject to the registration conditions and ongoing compliance obligations for that category of registration. (For a discussion of the international adviser exemption and its requirements, see the topic Impact on International Advisers.)

### **Sub-Adviser and Other Adviser Registration Exemptions**

31-103 does not extend the sub-adviser exemption to the adviser registration requirement to jurisdictions beyond Ontario at this time. For now, the adviser registration exemption for sub-advisers in OSC Rule 35-502 – *Non Resident Advisers* (35-502) will be retained in Ontario and exemptive relief where necessary will be considered on a case by case basis in other jurisdictions, as is the current situation.

With the elimination in Ontario of the “look-through” analysis on the adviser registration requirement, which has been confirmed by the CSA in 31-103, related adviser registration exemptions that are currently available under 35-502, such as that for non-Canadian advisers in connection with the private placement of the securities of non-Canadian investment funds, are considered unnecessary and not being carried forward in 31-103 or 35-502.

### **Registration and Ongoing Compliance Requirements**

31-103 sets out registration requirements, including proficiency (for individual registrants) and capital and insurance requirements, as well ongoing compliance requirements applicable to registrants. These include, by way of example, rules governing policy and procedure requirements for control systems and supervision, recordkeeping, know your client and suitability obligations, relationship disclosure, complaint handling, conflicts of interest, and referral arrangements.

31-103 provides certain exemptions from these requirements for a registrant that is an investment fund manager or for a registrant that is a member of a self-regulatory organization (SRO) (e.g., an investment dealer or mutual fund dealer) and is subject to SRO rules that deal with the same subject matter.

31-103 extends the application of a number of existing requirements that currently apply to current categories of registrants to other types of registrants. 31-103 also provides a number of new or expanded requirements, including:

- moving to exam-based individual proficiency requirements;
- a requirement that all registrants appoint an ultimate designated person and a chief compliance officer;
- increased capital requirements for most non-SRO registrants;

- moving from pre-set insurance amounts to a formula-based method for determining insurance requirements;
- a requirement for registrants to file financial statements with regulators more frequently and on an unconsolidated basis;
- a requirement for investment fund managers to file with the regulators, together with their financial statements, a description of any net asset value adjustment made during the period;
- a requirement for registrants (other than investment fund managers and SRO members) to provide to a client “relationship disclosure information”, which is to be all information that a reasonable investor would consider important about the client’s relationship with the registrant and is to include various items such as disclosure of the compensation paid to the registered firm in relation to the different types of products that a client may purchase through it, a description of risks that should be considered, a description of applicable client reporting and a description of certain conflicts of interest;
- a requirement for registrants (other than investment fund managers) to document and respond to client complaints and to ensure that an independent dispute resolution or mediation services are made available, at the firm’s expense; and
- requirements for entering into referral arrangements, including prescribed disclosure to clients and the requirement for the referring party and recipient of the referral to enter into a written agreement.

Firms registered in more than one category must comply with the highest capital and insurance requirements and with conduct requirements that apply to the registrable activity being conducted.

### **Continuous Registration**

Registration will no longer have to be renewed annually, and will remain in effect until suspended or terminated by certain triggering events, including non-payment of annual fees.

### **Transition**

Firms and individuals currently registered will be automatically moved by the securities regulators in each jurisdiction to equivalent categories of registration under 31-103. The equivalent categories are set out in Appendices C and D to 31-103.

31-103 sets out various transition periods to allow firms and individuals to comply with the new requirements.

#### *Firms*

Generally for firms registered in a jurisdiction before 31-103 comes into force, the transition timelines from the Implementation Date are as follow:

- 3 months for firms to designate and apply for registration for the ultimate designated person (UDP) and chief compliance officer (CCO);

- 12 months for firms to satisfy capital requirements and notify the regulator of a subordination agreement;
- 6 months for firms to satisfy bonding or insurance requirements;
- 6 months for firms to comply with referral arrangement requirements;
- 12 months for firms to deliver relationship disclosure information to clients; and
- 24 months for firms to ensure that an independent dispute resolution or mediation service is available to resolve client complaints.

Capital and insurance in accordance with current requirements must be maintained during the transition.

A firm which fails to meet the prescribed timelines will be prohibited from carrying on business in the relevant jurisdictions until all the requirements of 31-103 are met.

#### MUTUAL FUND DEALER

- 24 months for firms to comply with the requirement to deliver client statements.

#### INTERNATIONAL DEALER

- A firm's registration as an international dealer in Ontario and Newfoundland and Labrador will be automatically revoked on the date 31-103 comes into force and, as of such date, the firm can continue to do business in these provinces pursuant to the international dealer exemption under 31-103. The firm will have one month to submit the required Form 31-103F2 *Submission to Jurisdiction and Appointment of Agent for Service* (Form 31-103F2), which is a condition of the exemption.

#### INTERNATIONAL ADVISER

- 12 months for firms currently registered as an international adviser in Ontario or as a portfolio manager & investment counsel (foreign) in Alberta, to submit Form 31-103F2, which is a condition of the international adviser exemption.

During the 12 month transition period, registrants in the category of international adviser in Ontario, or portfolio manager & investment counsel (foreign) in Alberta will be automatically converted to the category of portfolio manager and permitted to operate under their current conditions of registration. At the end of the transition period, the firm's registration as portfolio manager will be revoked. During the transition period, the firm will need to register as a portfolio manager under 31-103 or determine that it is able to operate under the international adviser exemption under 31-103.

#### *Individuals*

For **individuals registered before 31-103 comes into force**, individuals currently registered, and in each case who will continue to be registered, as a dealing representative of a mutual fund dealer, advising representative of a portfolio manager, associate advising representative of a portfolio manager, or

advising representative subject to terms and conditions of registration equivalent to the scope of authority of an associate advising representative under 31-103, will not be required to satisfy formal proficiency requirements. Individuals designated on the National Registration Database as CCOs upon implementation of 31-103 will not be required to satisfy formal proficiency requirements.

An individual currently registered as a dealing representative of either a scholarship plan dealer or a limited market dealer (which is transitioning to exempt market dealer registration) will have 12 months to satisfy formal proficiency requirements. Similarly, a CCO of a limited market dealer who applies for registration within three months of implementation will have 12 months to meet formal proficiency requirements.

*Individuals and Firms not Required to be Registered before 31-103 comes into force, but Requiring Registration once in force*

Generally, a firm or individual that is **not registered before the date 31-103 comes into force** must meet all requirements of 31-103 at the time of the firm's or individual's application for registration is filed. However, there are two main exemptions to this general rule for individuals or firms who intend to register as exempt market dealers or investment fund managers. These are:

EXEMPT MARKET DEALERS

- Other than in Ontario and Newfoundland, firms **active** in the exempt market in a jurisdiction prior to the date 31-103 comes into force will have 12 months from the Implementation Date to apply for registration in that jurisdiction and comply with the requirements. New entrants, not previously active in the jurisdiction, will have no transitional relief;
- in Ontario and Newfoundland and Labrador, limited market dealer registrants will be moved automatically to the exempt market dealer registration on the Implementation Date, and will be subject to the transition periods set out above.

INVESTMENT FUND MANAGERS

- Investment fund manager firms with their head office in Canada and **active** prior to the Implementation Date will have 12 months from the Implementation Date to apply for registration in the jurisdiction in which their head office is located and 24 months to apply for registration in other applicable Canadian jurisdictions;
- firms with their head office outside Canada that are either **active or inactive** prior to the Implementation Date will have 24 months to apply for registration.

*Continuation of Exemptive Relief*

Discretionary relief granted by regulators prior to 31-103 coming into force will extend to equivalent requirements under 31-103 on the same terms and conditions.

### *Operational Transition by the CSA and IIROC*

CSA Staff Notice 31-311 – *Proposed National Instrument 31-103 Registration Requirements and Exemptions - Transition into the New Regime (31-311)* discusses a number of operational matters for transitioning into the new regime. Key features include:

- a “freeze period” for the National Registration Database (NRD) from 5:00 pm (ET) on September 25, 2009 to 11:59 pm (ET) on October 12, 2009;
- during the freeze period the following information will need to be filed by paper (and after the freeze period, on NRD by November 10, 2009)
  - reinstatements,
  - termination notices for individuals who resign or are dismissed for cause,
  - notices of changes to civil, criminal and financial information,
- all other notices which should have been submitted during the freeze period, must be submitted on NRD by November 24, 2009; and
- applications made by paper during the freeze period must be resubmitted on NRD, and if approved during the freeze period, they must be resubmitted by November 24, 2009.

### **Matters Being Considered Further by the CSA**

While 31-103 is a very comprehensive overhaul of registration requirements and exemptions in Canada, the CSA have noted a number of matters which they expect to revisit. These matters include:

- the circumstances under which an investment fund manager that does not have a Canadian head office would need to register;
- the circumstances under which an investment fund manager with a head office in one Canadian jurisdiction would need to register in other Canadian jurisdictions;
- amendments to 31-103 are expected in respect of requirements or guidance for cost disclosure and performance reporting. The CSA have stated that the goal is to make 31-103 consistent with the Client Relationship Models (CRMs) of the SROs, once finalized, and to potentially exempt members of the SROs from some of these requirements if they are satisfied with the CRMs;
- the CSA have stated that they are working with the SROs to harmonize complaint-handling requirements and anticipate amending 31-103 accordingly;
- the CSA have stated that they are considering proposing expanded custodial requirements;
- the forms related to registration will be subject to further review and changes may be proposed to the registration process; and
- the CSA have stated that they will continue to assess new examinations for recognition as sufficient for proficiency requirements.

# Registration Reform in Canada:

## *The Finish Line is Here*

Canada's new registration rule was published by the Canadian securities administrators in final form on July 17, 2009.

The new regime is expected to be in force September 28, 2009 with transition periods for implementation of aspects varying. The new regime, which has been several years in the making, is intended to harmonize, streamline and modernize registration requirements and exemptions across all Canadian jurisdictions. It regulates dealers and advisers, effectively eliminating the dealer registration exemption for trading in the exempt market in Canada, and imposes a new registration requirement for investment fund managers.

The new regime has significant implications for Canadian and non-Canadian market participants, particularly those now doing business on an unregistered or exempt basis.

This document is one part in a series that details the regime and its impact on particular types of market participants and their business activities. The complete document includes the following sections:

- A** Overview of Canada's New Registration Regime
- B** Impact on Limited Market Dealers and Unregistered Dealers Trading in the Exempt Market
- C** Impact on Investment Fund Managers
- D** Impact on Portfolio Managers and Investment Counsel
- E** Impact on International Dealers and Non-Canadian Dealers Trading in the Exempt Market
- F** Impact on International Advisers
- G** Impact on Investment Dealers and Mutual Fund Dealers
- H** Impact on Issuers Generally
- I** Impact on Investment Funds
- J** Impact on Private Equity and Venture Capital Funds
- K** Impact on Non-Canadian Investment Funds Privately Placing Securities in Canada
- L** New Compliance Requirements for Registrants
- M** Registering in Multiple Jurisdictions
- N** Quebec's *Derivatives Act*
- O** Trading or Advising in Commodity Futures
- P** Useful Links

**If you would like a copy of any of the other sections, in electronic or print format, please contact your Stikeman Elliott representative, email us at [info@stikeman.com](mailto:info@stikeman.com) or visit our website at [www.stikeman.com](http://www.stikeman.com)**

# Canadian Business Law – Worldwide

---

**Stikeman Elliott is recognized nationally and internationally** for the sophistication of its business law practice. The firm is a Canadian leader in each of its core practice areas – corporate finance, M&A, securities, banking, corporate-commercial, real estate, tax, insolvency, structured finance, competition, intellectual property, employment and business litigation – and has developed in-depth knowledge of a wide range of industries.



London-based *World Finance* magazine named Stikeman Elliott as the *2008 Best Corporate & Commercial Team in Canada*. Additionally, the *International Financial Law Review* honoured Stikeman Elliott as *2007 National Law Firm of the Year (Canada)*, while Chambers Global identifies it as one of Canada's two top-tier Corporate/M&A practices. The firm is frequently ranked among Canada's leaders in domestic and cross-border M&A and corporate finance league tables. The National Litigation Group, whose specializations include class actions, securities litigation and restructurings, has been ranked among the top three business litigation practices in Canada by Lexpert. Among Stikeman Elliott's other highly regarded practices are competition/antitrust (named as a leader by the *Global Competition Review*), taxation (highly ranked by Lexpert) and structured finance (widely considered to be Canada's foremost practice in that field).

The firm's clients can expect a consistently high level of service from each of its eight offices who work together on major transactions and litigation files, and regularly collaborate with prominent U.S. and international law firms on cross-border transactions of global significance. The firm has invested heavily in leading-edge knowledge management systems in order to assure our clients of advice of the highest quality, grounded in the accumulated expertise of Stikeman Elliott's national and international practice.

**STIKEMAN ELLIOTT**

---

MONTRÉAL TORONTO OTTAWA CALGARY VANCOUVER NEW YORK LONDON SYDNEY

[www.stikeman.com](http://www.stikeman.com)