MANAGED FUNDS ASSOCIATION
The Voice of the Global Alternative Investment Industry
WASHINGTON, DC | NEW YORK

January 13, 2011

Via Electronic Mail: jstevenson@osc.gov.on.ca
consultation-en-cours@lautorite.qc.ca

British Columbia Securities Commission
Alberta Securities Commission
Saskatchewan Financial Services Commission
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marches financiers
New Brunswick Securities Commission
Register of Securities, Prince Edward Island
Nova Scotia Securities Commission
Superintendent of Securities, Newfoundland and Labrador
Register of Securities, Northwest Territories
Register of Securities, Yukon Territory
Register of Securities, Nunavut

c/o Mr. John Stevenson
Secretary
Ontario Securities Commission
20 Queen Street West
Suite 1903, Box 55
Toronto, Ontario
M5H 3S8
jstevenson@osc.gov.on.ca

Ms. Anne-Marie Beaudoin
Corporate Secretary
Autorité des marchés financiers
800, square Victoria
22 étage, C.P. 246, Tour de la Bourse
Montréal, Québec
H4Z 1G3
consultation-en-cours@lautorite.qc.ca

Dear Sirs/Mesdames:

Re: Comments on Proposed Amendments to National Instrument 31-103 – *Registration Requirements and Exemptions* and Related Companion Policy – Registration of International and Certain Domestic Investment Funds Managers

Managed Funds Association[1] ("MFA") appreciates the opportunity to make this submission of comments in response to the proposed amendments (the "Proposed Amendments") to National Instrument 31-103 – *Registration Requirements and Exemptions* ("NI 31-103") and Companion Policy 31-103CP – *Registration Requirements and Exemptions* (the "Companion Policy") related to the registration of international and certain domestic investment fund managers ("IFMs") which were issued for comment on October 15, 2010. MFA is committed to working in a constructive manner with policy makers and regulators to achieve the shared goal of effective and efficient regulation of fund managers.

INTRODUCTION

MFA members participate in the Canadian capital markets by providing sophisticated Canadian investors with alternative investment opportunities, raising capital from Canadian investors for U.S. or international hedge funds and investing in or trading in the securities of Canadian companies. Therefore, MFA has a strong interest in the Proposed Amendments and their potential impact on the activities of the non-Canadian IFMs of non-Canadian hedge funds and other alternative investment vehicles in the Canadian capital markets.

Before discussing specific issues raised by the Proposed Amendments, we believe it would be beneficial to briefly discuss the nature of the hedge fund industry. Hedge funds and other private investment funds are pooled investment vehicles marketed and sold only to sophisticated investors. They are not sold to retail investors; in fact, hedge funds are precluded by law in the United States from being sold to retail investors. MFA and its members strongly support limiting the sale of hedge funds to sophisticated investors.

Hedge funds and other alternative investment vehicles are a valuable component of the investment portfolio for such sophisticated investors, which include pension plans. The properly managed addition of hedge funds to a portfolio provides diversification, risk management and returns that are not correlated to traditional equity and fixed income markets. These are critical benefits that help investors generate sufficient returns to meet their obligations. As such, we believe that it is critical to sophisticated Canadian investors that the Canadian registration framework not unduly limit their access to non-Canadian IFMs.

---

[1] MFA is the voice of the global alternative investment industry. Its members are professionals in hedge funds, funds of funds and managed futures funds, as well as industry service providers. Established in 1991, MFA is the primary source of information for policy makers and the media and the leading advocate for sound business practices and industry growth. MFA members include the vast majority of the largest hedge fund groups in the world who manage a substantial portion of the approximately $1.7 trillion invested in absolute return strategies. MFA is headquartered in Washington, D.C., with an office in New York.

PROPOSED AMENDMENTS

We provide the following comments on the Proposed Amendments for the Canadian Securities Administrators' (the "CSA") consideration.

1. IFM Registration

MFA recognizes and supports the need for regulators to have appropriate oversight over market participants, including hedge funds and their managers. It is important, however, to ensure that national regulatory regimes are implemented in a way that is consistent with the G-20 commitment to international coordination. In that regard, MFA believes the IFM registration requirement (the "IFM Registration Requirement") should be limited in application with respect to an international IFM if that manager has no place of business in Canada, is registered or otherwise regulated in its home jurisdiction, and all securities of the fund distributed in Canada are distributed to permitted clients.

It is important to underscore the comprehensive and robust nature of the regulatory framework that applies to hedge funds and their managers now that the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") has been enacted in the United States. All hedge fund advisers of meaningful size must register with the Securities and Exchange Commission (the "SEC") under the Investment Advisers Act of 1940 (the "Advisers Act").[2] The responsibilities imposed on hedge fund managers by the Advisers Act entail significant disclosure and compliance requirements, including: publicly available disclosure to the SEC regarding the manager's business; extensive systemic risk reporting to the SEC; detailed disclosure to clients; compliance policies and procedures; designation of a chief compliance officer; maintaining extensive books and records; and periodic inspections and examinations by SEC staff.

In recognition of the global nature of the investment management industry, the U.S. SEC has proposed rules that seek to achieve a balance with respect to the full application of U.S. laws to non-U.S. managers. The SEC's proposed rules regarding the registration of non-U.S. based hedge fund managers would provide an exemption from registration for most managers, unless they have a place of business in the U.S., though such managers will be required to provide certain reports to the SEC and will still be subject to anti-fraud laws and SEC jurisdiction. We believe the SEC's approach is consistent with the G-20 commitment to international coordination in the regulation of investment managers, including hedge fund managers.

To the extent that a hedge fund manager is registered and regulated by its home jurisdiction regulator, we believe that it is unnecessary to require additional registration and regulation in every country in which the manager has investors. Such a result would place enormous burdens on global managers, which could be required to register in numerous jurisdictions. More significantly, global managers could become subject to inconsistent or even

[2] Smaller hedge fund managers, those with less than $100 million in assets under management, generally will be subject to registration and regulation by state securities regulators.

conflicting regulatory requirements in different jurisdictions, which would greatly inhibit the ability of managers to operate globally and impede cross-border flows of capital.

We encourage the CSA to consider an exemption from registration for IFMs that are registered with or regulated by their home jurisdiction regulator. We note that, even if the CSA were to grant such an exemption, the CSA could still maintain oversight over the industry through information sharing and cooperation agreements with other global regulators. We believe this framework would provide an effective and coordinated regulatory framework for fund managers without imposing overly burdensome and potentially duplicative or inconsistent regulatory requirements on global managers.

2. Tailored Application of IFM Regulations

To the extent the CSA believe that registration of international IFMs is necessary, we encourage the CSA to tailor the application of the regulatory framework for registered fund managers with respect to IFMs that are also registered with or regulated by their home jurisdiction regulator. We believe a tailored approach to IMFs registered in their home jurisdiction would be consistent with the G-20 commitment to international coordination while addressing the CSA's public policy concerns. Accordingly, we encourage the CSA to limit the application of IFM regulation with respect to international IFMs registered with or regulated by their home jurisdiction regulator to the following: compliance with the standard of care of IFMs; appointment of an agent for service (as contemplated by section 8.29.1(3)(d) of the Proposed Amendments); non-public reporting requirements to the CSA; and provision of notice to Canadian securityholders of its funds (as contemplated by section 8.29.1(5) of the Proposed Amendments).

As discussed above, U.S.-based IFMs are subject to a comprehensive regulatory framework, which we believe addresses the policy considerations raised by the CSA, including (i) incorrect or untimely calculation of net asset value; (ii) incorrect or untimely preparation of financial statements and reports; and (iii) conflicts of interest between the fund manager and the investor. Given the nature of the private offerings of U.S-based hedge funds and the limits on transferability of the securities, the risks related to record keeping and transfer agency services for such funds are relatively low. Further, hedge fund managers in the United States are already subject to a fiduciary obligation to their clients, and this obligation governs the management and operation of each fund and addresses the calculation of net asset value, supervision of third party service providers, and conflict of interest matters. In addition, U.S. regulatory requirements mandate that U.S. hedge fund managers prepare and deliver annual audited financial statements of the funds to securityholders, designate a chief compliance officer, and maintain appropriate compliance policies, among other requirements.

It is our belief that the full application of the Canadian IFM regulatory framework, as contemplated by the Proposed Amendments, would impose significant costs and compliance burdens without providing added benefits to the sophisticated investors in the affected investment funds. For example, U.S. registered investment advisers are required to have a chief compliance officer who must be knowledgeable about U.S. securities laws and who oversees the

manager's compliance function, but such individuals are unlikely to satisfy the applicable proficiency requirements under NI 31-103. Ultimately, these additional costs and burdens are likely to limit the access of sophisticated Canadian investors to non-Canadian IFMs. In conclusion, to the extent the CSA issues final rules that require IFMs to register under Canadian securities laws, we believe that the CSA should limit the application of the operational requirements set out in NI 31-103 to those requirements set out above.

3. Significant Presence Thresholds

We also encourage the CSA to adjust the significant presence thresholds to better reflect the size and scope of investments in hedge funds. The exemption from the IFM Registration Requirement set out in the Proposed Amendments is not available to an IFM if, as at the financial year end of the manager, any of the following apply:

(a) for any fund for which it acts as investment fund manager, the fair value of the assets of the fund attributable to securities beneficially owned by residents of Canada is more than 10% (the "Securityholder Threshold") of the fair value of all the assets of such fund (the "Securityholder Test"); and

(b) for all investment funds for which it acts as an investment fund manager, the fair value of the assets of the funds attributable to securities beneficially owned by residents of Canada is more than $50 million (the "Total Assets Test").

MFA fully supports exemptions from the IFM Registration Requirement for those international IFMs that do not have a significant number of Canadian investors. As noted above, hedge fund investors are sophisticated investors, frequently institutional investors that invest significant dollar amounts into hedge funds, even though such investments typically are a relatively small portion of the institution's overall portfolio and may be a relatively small percentage of the manager's total assets under management.

As such, we believe that an exemption threshold based on the percentage of an IFM's assets under management is appropriate, though it would be more appropriate to apply the test to the IFM's total assets under management, rather than on a fund-by-fund basis. Many IFMs manage funds in so-called master/feeder structures and may have feeder funds that are sold only to Canadian investors. A fund-by-fund threshold could, therefore, preclude many IFMs from relying on the exemption, even if Canadian investors make up a small percentage of the IFM's overall asset base. In addition, a fund-by-fund test could inadvertently create timing problems in connection with the sale of fund securities as managers would need to monitor the timing of an investment by Canadian investors compared to other investors to avoid inadvertently triggering the registration requirement.

While we believe a modified version of the Securityholder Test provides a workable framework, we are concerned that the Total Assets Test will effectively require all IFMs to register, as it is not uncommon for large institutions to invest significant assets (much larger than $50 million) in a single fund managed by international IFMs. We believe that the Securityholder

Test, even if applied to an IFM's total assets under management, appropriately exempts only those international IFMs which do not generate a significant portion of their business from Canadian investors. As such, we encourage the CSA to delete the Total Assets Test. If not, we are concerned that IFMs could choose to withdraw from the Canadian markets given the regulatory burden associated with registration, which would result in fewer investment options for Canadian investors.

4. Application of Thresholds

International IFMs relying on a threshold exemption will need to ascertain the residency of the beneficial owners of the investment funds under management. IFMs can require representations from new investors regarding their residency in subscription documentation. It is important that the IFM be permitted to rely on the information provided by investors with respect to the identity of the beneficial owners of the fund's securities and with respect to the residency of the beneficial owner(s), unless the manager knows that such information is inaccurate.

As discussed above, the Threshold Tests are based on the residency of the beneficial owners of securities of a fund. We expect that the CSA only intended to include the registered holder of the securities and any person controlling or controlled by that holder. We are concerned that a more expansive interpretation of beneficial ownership that includes, for example, all affiliates of an investor would be extremely difficult for managers to monitor. Furthermore, a more expansive interpretation could potentially include many non-Canadian investors, which we believe is beyond the intended scope of the Proposed Amendments. We request that the CSA limit the scope of beneficial ownership in any final rules to the investor and any person controlling or controlled by the investor.

5. Transition Period

It appears that a fund manager could become subject to an immediate registration requirement if a change happens near or at the year end of the manager (or if the manager learns of one at that time), including in the event of changes that are not caused by the action of an investment fund or its manager (*e.g.,* asset volatility, currency fluctuations, termination of another fund in the group, redemptions by other investors). Further, without an appropriate transition period, managers conducting offerings[3] could be forced to register if there are any potential Canadian investors, particularly with respect to new fund offerings, even if actual beneficial ownership by Canadian investors never crosses the threshold requiring registration. As such, we believe it is important for the CSA to provide international IFMs a reasonable period of time to apply for registration after an event that would require it to register with the CSA.

[3] We note that many hedge funds engage in continuous offerings of their securities making this an ongoing issue for many managers.

6. Grandfathering

We believe that the grandfathering provision in the CSA proposal should not be subject to the Threshold Tests. International IFMs and their investors have structured their businesses and investment portfolios based on the existing regulatory framework. Applying the thresholds to investments already made could force managers to redeem existing Canadian investors in order to meet the new thresholds. A forced redemption of Canadian investors would be detrimental to those investors, which seems inconsistent with the investor protection goals underlying the Proposed Amendments. Accordingly, we believe that the proposed grandfathering provision should not include any thresholds.

CONCLUSION

MFA appreciates the opportunity to provide comments to the CSA in response to the Proposed Amendments. MFA and its members are committed to working in a constructive manner with policy makers and regulators to achieve the shared goal of effective and efficient regulatory oversight over IFMs. Our comments in this letter are provided in that spirit and we hope the CSA finds our proposals useful as it considers how best to finalize its rules.

If you have any questions regarding any of these comments, or if we can provide further information with respect to these or other regulatory issues, please do not hesitate to contact Stuart J. Kaswell or me at (202) 367-1140.

Respectfully submitted,

/s/ Richard H. Baker

Richard H. Baker
President and CEO