



Starting a Hedge Fund in Canada

March 8, 2021

AIMA

THE ALTERNATIVE INVESTMENT
MANAGEMENT ASSOCIATION

Panelists



Speakers:

- **Sarah Gardiner**, Partner, Securities & Capital Markets, **Borden Ladner Gervais LLP**
- **Peter Hayes**, Partner, National Director, Canadian Alternative Investments Practice, **KPMG Canada**
- **Supriya Kapoor**, Principal/Founder, **Aurelius G.R.P. (Canada)**
- **Ron Landry**, Head of Product and Canadian ETF Services, **CIBC Mellon**
- **Rob Lemon**, Executive Director, Prime Services, **CIBC Capital Markets**
- **Raj Vijh**, Chief Operating Officer and Chief Financial Officer, **Lysander Funds**

Moderator:

- **Claire Van Wyk-Allan**, Director, Head of Canada, **AIMA**

Legal Issues

- What you need to build a small business
- Creating/registering a management company
- Creating a fund – legal structures and fund documents
- Determining offering terms

What You Need to Build the Business

- Resources
 - Personal resources
 - Seed money – for the manager and for the fund
- Infrastructure
 - Team skillset and regulatory proficiency
 - Physical infrastructure
- Budget
 - Start-up costs
 - Minimum regulatory capital

Manager Formation

- Typically a corporation, but consult with tax and legal advisers to consider other structures such as a limited partnership

- Consider nature and share of ownership
 - shareholder or partnership agreement
 - employment agreements
 - other profit sharing arrangement

Manager Registration



- Will need to register in one or more of the following categories:
 - Investment Fund Manager
 - Adviser (Portfolio Manager and/or Commodity Trading Manager)
 - Dealer (typically, Exempt Market Dealer)
- Consider securities commissions where registration required
- Minimum proficiency, capital, insurance and infrastructure requirements
- Timing and cost (4-6 months)

Fund Formation – Most Common Legal Structures

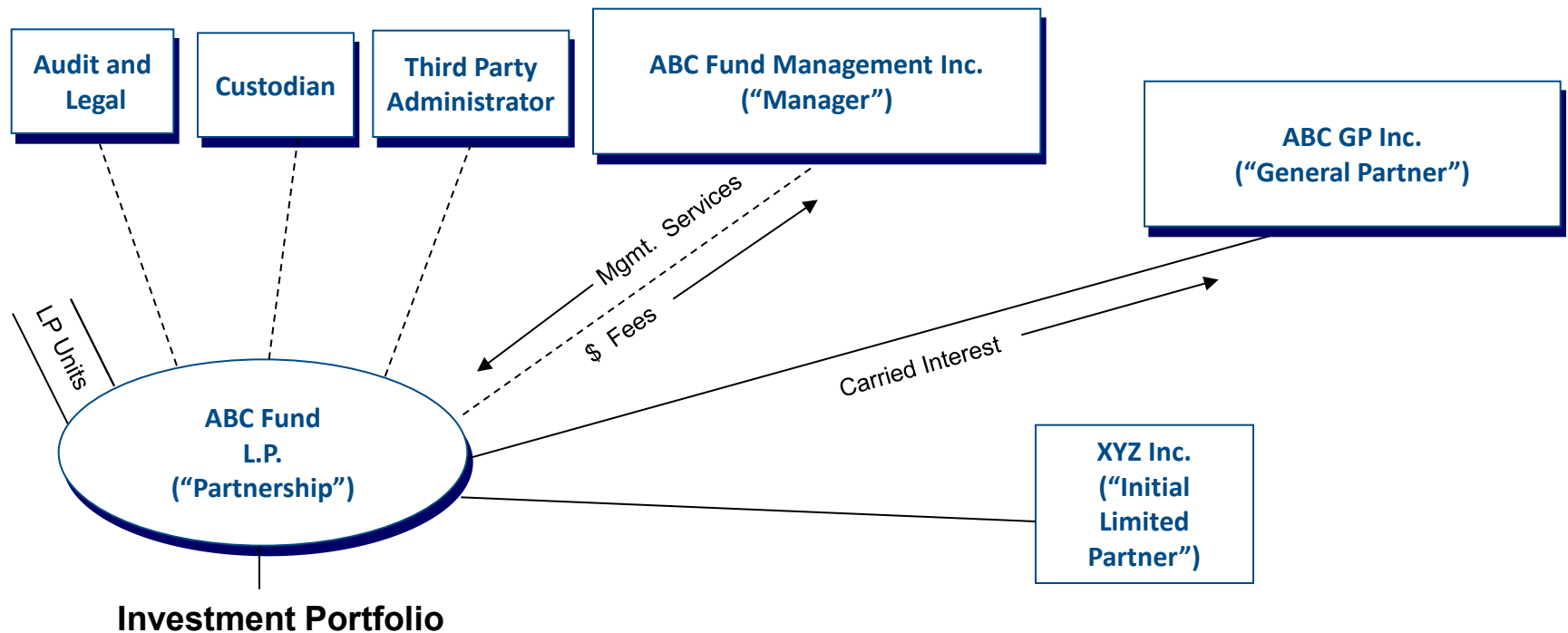
■ Limited Partnership

- certainty of limited liability for passive investors
- profit/loss flow through to investors in the nature earned by the partnership
- greater flexibility in structuring how profits are shared
- may require extra-provincial registration in certain provinces where units are offered
- typically not RRSP-eligible
- requires creation of a general partner
- governing document: limited partnership agreement between general partner and limited partners

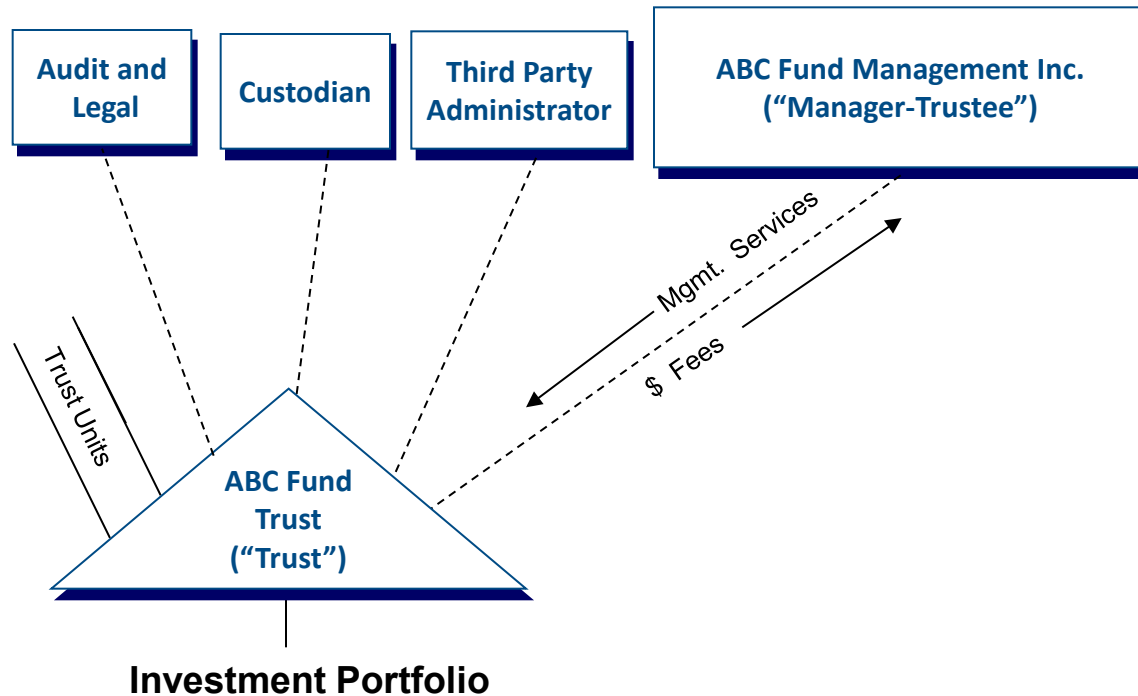
■ Trust

- RRSP eligibility can be achieved by registration as a “registered investment” (but subject to investment restrictions that might preclude certain investment strategies) or by qualification as a mutual fund trust (requiring 150 unitholders, each holding a block of units having a certain NAV, among other things, including that units are redeemable)
- taxable profit is distributed to investors so that the Trust does not pay income tax, however losses can only be carried forward
- Requires a trustee (which can be the investment fund manager)
- governing document: declaration of trust or trust agreement

LP Structure



Trust Structure



Fund Documentation

- Creating the fund (constitutional documents)
 - Declaration of Limited Partnership and LP Agreement, or
 - Declaration of Trust or Trust Agreement, or
 - Articles of Incorporation
- Material Contracts
 - Management, portfolio management and distribution agreement(s) (typically one agreement)
 - Custodian/prime broker agreement
 - Administrative services agreement
 - ISDA agreements and other derivative contracts
- Offering Documents
 - Offering memorandum
 - Subscription agreement
 - Marketing documents

Terms of Offering

- Investment objectives, strategies and restrictions
- To whom and where will the fund be sold?
- Series accounting
- Offering price per Unit
- Redemption terms
 - Frequency of redemptions
 - Lock-up period or early redemption deduction or fee?
 - Redemption deduction to recover costs?
 - Hold-back pending audit?
 - Suspension/deferral of redemptions
 - ✓ Broad discretion if illiquidity?
 - ✓ Gates?
 - ✓ Redemptions in kind?

Terms of Offering

- Management Fees
 - Typical “2+20” fee model
 - Management fee based on net asset value
 - Weekly, monthly or quarterly?
 - Performance fee based on increases in NAV?
 - Calculate at the unit, series, class or fund level?
 - Quarterly or annual?
 - Class-specific
- GP Profit-Share
 - In lieu of paying performance fee to Manager
 - Consider tax implications and potential risk
- Fund versus manager expenses

Terms of Offering

- Terms of performance fee / GP profit-share
 - High water mark (loss carry-forward)
 - Permanent, rolling or reset?
 - Hurdle rate
 - Fee/participation only on portion in excess of hurdle rate, or on whole amount if threshold met?
 - Catch-up fee/return?
 - Clawback?
- Net Asset Value (NAV) valuation methodology

Raising Capital

- Prospectus Exemptions (Private Placements)
 - Accredited Investor Exemption
 - \$150,000 Minimum Amount Exemption (not for individuals)
 - Offering Memorandum Exemption (largely unavailable)
 - Family, Friends and Business Associates Exemption (largely unavailable)
 - Employee Exemption for Manager's employees?

- Distribution Networks
 - Seed Investors
 - IIROC members and Fundserv
 - EMDs
 - Cap Intro

- Foreign Investors? (be careful)

Upcoming AIMA events



- March 9-11: AIMA Next Generation Manager Forum 2021
- March 11: 12th Annual Vancouver Alternative Investment Outlook Forum (with CAIA Vancouver and CFA Society Vancouver)
- March 15: Becoming a Responsible Investment Signatory
- March 18: AIMA/Albourne Diversity & Inclusion DDQ: A Walk-through
- March 23: Trends and Opportunities in Commodity Investing
- April 7: Digital Asset Industry in Canada
- April 20-21: Alternative Credit Council Global Virtual Summit 2021

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