September 7, 2020

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TO: Capital Markets Modernization Taskforce

Delivered by email: CMM.Taskforce@ontario.ca

Dear Sirs/Mesdames:

RE: Consultation — Modernizing Ontario's Capital Markets

About Alternative Investment Management Association (AIMA)

AIMA was established in 1990 as a direct result of the growing importance of alternative investments in global investment management. AIMA is a not-for-profit international educational and research body that represents practitioners in alternative investment funds, futures funds and currency fund management – whether managing money or providing a service such as prime brokerage, administration, legal or accounting.

AIMA's global membership comprises approximately 2,000 corporate members in more than 60 countries, including many leading investment managers, professional advisers and institutional investors and representing over $2 trillion in assets under management. AIMA Canada, established in 2003, has approximately 140 corporate members.

The objectives of AIMA are to provide an interactive and professional forum for our membership and act as a catalyst for the industry's future development; to provide leadership to the industry and be its pre-eminent voice; and to develop sound practices, enhance industry transparency and education, and to liaise with the wider financial community, institutional investors, the media, regulators, governments and other policy makers.

The majority of AIMA Canada members are managers of alternative investment funds and fund of funds. Most are small businesses with fewer than 20 employees and $50 million or less in assets under management. The majority of assets under management are from high net worth investors and are typically invested in pooled funds managed by the member.

Investments in these pooled funds are sold under exemptions from the prospectus requirements, mainly the accredited investor and minimum amount investment exemptions. Manager members also have multiple registrations with the Canadian securities regulatory authorities: as Portfolio Managers, Investment Fund Managers, Commodity Trading Advisers and in many cases as Exempt Market Dealers. AIMA Canada's membership also includes accountancy and law firms with practices focused on the alternative investments sector.

For more information about AIMA Canada and AIMA, please visit our websites at canada.aima.org and www.aima.org.

Comments

We are writing in response to the published **Consultation — Modernizing Ontario's Capital Markets**. This response is organized based on order of priority as it relates to key items pertaining to AIMA's members, and then with further items organized based on the numbered proposals and discussion questions outlined in the Consultation.

Overall, AIMA Canada supports the objective of modernizing Ontario's Capital Markets. There are a number of issues where we are supportive and we commend the taskforce for conceptualizing a first iteration of this modernization initiative. In general, we are commenting only where we have issues or substantive feedback for review and consideration.

The Consultation notes that: "Ontario needs to attract and grow businesses that support and sustain an innovation economy that can compete for investment and talent worldwide. The purpose of securities regulation is to protect investors in a manner that inspires confidence in the capital markets and limits systemic risk, while creating an environment where enterprising companies choose Ontario as the optimal place to raise capital and establish an active presence." We believe that from a regulatory perspective, the modernization of Ontario's capital markets will depend on a variety of factors such as: reasonable and technology friendly regulation that addresses particular risks and that can be fairly and readily operationalized for firms of all sizes; regulatory reformation at a national level, to the extent possible; and the consistent application of regulation considering international requirements, so that market participants in Ontario specifically (and Canada more broadly), are not at a competitive disadvantage. Regulation should serve to ensure that issues and market participants are held to a high standard of integrity and conduct, but not be so burdensome that it stifles growth of the capital markets and not give investors a false sense of security that somehow more regulation is correlated to "better" or "stronger" markets.

We note that AIMA has previously submitted comments in response to ongoing regulatory burden initiatives, such as the recent OSC Regulatory Burden Reduction consultation and the CSA Regulatory Burden Reduction Consultation.[1] We do not intend to repeat those comments here and kindly ask that AIMA's prior comments will be considered where relevant and look forward to discussing further at your convenience.

Given the backdrop of a global pandemic and the active implementation of the CSA Client-Focused Reforms and regulatory burden reduction initiative, it is our position that any projects posing additional burden on registrants should not occur until the completion of those projects.

Key Items

Item #13: Prohibit short selling in connection with prospectus offerings and private placements

We are highly concerned about this proposal. It presumes that people are trading on inside information or are engaging in manipulative market activities to affect a securities' price. We believe short selling is a fundamental, necessary part of investment strategies. In early 2020, even SEC Commissioner Clayton publicly indicated that the practice of short selling is needed to "facilitate ordinary market trading" and should not be banned.[2]

1 OSC Staff Notice 11-784, Proposed National Instrument 93-101 & Proposed Companion Policy 93-101CP; Proposed National Instrument 93-102 & Proposed Companion Policy 93-102CP; Proposed amendments to National Instrument 31-103 & Companion Policy 31-103CP; & Proposed amendments to National Instrument 81-105, Companion Policy 81-105CP and Related Consequential Amendments.

2 https://www.cnbc.com/2020/03/30/sec-chairman-jay-clayton-short-selling-should-not-be-banned.html

While not explicitly stated, it appears that this initiative may be premised on an unstated and perhaps unintended more fundamental assault on short selling as a negative capital market influence. We strongly disagree with this; there is an extensive body of research to invalidate this premise. As such, it is inappropriate to differentiate between selling a security or short selling a security unless either are based on access to insider information or market manipulation. Currently, there are adequate rules and regulations in place to address these factors. Hence, this is a matter of enforcement of existing regulations not implementing prejudicial additional regulations.

For most asset managers, short selling is an essential risk management tool, one that is widely used to protect investors' money and limit the risk of losses. It gives investment managers flexibility, diversifies their income streams and enable them to express downside sentiment. Indeed, there is increasing interest in the use of short selling as a means to further responsible investment and ESG.

Short selling also has important benefits for the market as whole, as most clearly demonstrated in situations where authorities have restricted the practice[3]. It provides liquidity in a falling market and has the broader potential to help uncover corporate malfeasance, as previously exemplified in the context of Enron or more recently Wirecard.

US Rule 105 of Regulation M is intended to protect an issuer in an offering, and its participants, from attempts at price manipulation, versus the insider trading concerns. Although application of a Rule 105-like construct could yield some benefit against short selling motivated by insider trading, it would do nothing to prevent bad actors from accumulating shares during the same period with the benefit of inside information.

Note that, unlike rules designed to deter insider trading, the mechanical aspects of US Rule 105 of Regulation M and its prophylactic application operate as strict liability and consequently are blind to intent – intent being a core element of US insider trading prosecution. More often than not, Rule 105's mechanical approach has led to technical violations and foot-faults, such as miscounting of a five-day period or errors due to confusion with issuer filing types, pricing dates, and times, as supported by the technical detail included in the volume of SEC enforcement actions since the Rule was adjusted. These actions in turn have served to dissuade participation in public offerings where a clear, quick distinction cannot be made in enough time to participate, for fear of an unintended technical violation. This is particularly true for managers who oversee multiple and more complex strategies, trade multiple products that may be correlated (e.g., ADRs and ORDs, options, convertible debt), and trade in multiple jurisdictions.

US rules require managers who cannot meet two other very narrow technical exemptions to conduct a bona fide purchase of all shorting activity during the preceding five-day restriction period, often forcing them to choose between over-purchasing securities in a manner that may disadvantage some investors solely due to coincidental trading, or exclude all of its eligible investors from rightful participation in an offering – a choice that challenges fiduciary duty, the balancing of best interests of all investors, and fairness.

Furthermore, Rule 105 does not apply to offerings exempt from registration, which often carry their own specific trading prohibitions that are unique to each particular offering. The US regulatory application is understanding of the fundamentally different market structure, transparency, and

[3] https://www.aima.org/uploads/assets/58c1345a-72dd-4a31-a488570249876267/Short-Selling-Guide-May-2020-final.pdf

liquidity between public offerings and private placements. In the case of Rule 105 applying to public offerings, the transparency of the market can give rise to price manipulation to the detriment of other participants; in the case of private placements, no such transparency exists and consequently, nor does the same risk. The ability to manipulate deal pricing and harm the capital raising process of public offerings has not been demonstrated in unregistered private offerings, to such a degree that related conduct generally is excluded from consideration under Rule 105.

The Canadian markets are principles-based and have ample regulation to protect and deter from market manipulation and fraud. Absent clear demonstration of abusive or violative conduct, and how this proposal would enhance existing market protections without also posing harm to normal, healthy market practices, Item 13 likely would have a chilling effect on capital markets deal participation and can only be viewed as appearing to further cast short selling in a negative light.

We note the CSA comments published on this topic, and look forward to participating in this consultation as it is published and discussing further in due course.

Item #17: Increase access to the shelf system for independent products

We note the industry is still working on the implementation of the CSA Client-Focused Reforms under 31-103, which at the core, aim to focus on the client's best interests and remove any conflicts of interest. We believe that Canadian retail investors deserve fair access to investment products, including independent and alternative products, across Canada. AIMA continues to advocate, for example, for fair access to alternative mutual funds under NI 81-102 to investors within the MFDA channel. There may also be opportunities for the CSA and/or a single SRO to lessen commonly cited distribution issues by considering more proactive guidance on suggested dealer risk ratings on alternative product or removing risk acknowledgement form for alternative funds where appropriate KYC/KYP has been met, amongst others.

Item #4: Move to a single SRO that covers all advisory firms, including investment dealers, mutual fund dealers, portfolio managers, exempt market dealers and scholarship plan dealers

As indicated in our comments to Item #3, we are supportive of the creation of a single SRO (Newco) responsible for the regulation of investment dealers and mutual fund dealers. We support the position recommended by McMillan LLP and have briefly summarized key aspects of the McMillan LLP comment letter on this item below. For the reasons set out below, we believe that the Newco should be primarily a prudential regulatory authority and do not support the extension of the scope of the Newco's regulatory authority to include portfolio managers, exempt market dealers or scholarship plan dealers.

As noted by McMillan LLP, as a result of the manner in which market participants have traditionally been regulated, significant knowledge and expertise has developed within: (i) IIROC and the MDFA in relation to the oversight and regulation of investment dealers and mutual fund dealers (respectively); and (ii) the OSC and individual members of the CSA in relation to the registration, oversight and regulation of portfolio managers, exempt market dealers and scholarship plan dealers. Consolidation of the regulatory oversight for all of these categories of registrants in a single SRO entity would require a significant transfer of personnel with such knowledge and experience from CSA members to Newco and would likely result in jurisdictional disputes where registrant activities relate to a specific province or territory or multiple provinces or territories.

Many portfolio managers are also registered as investment fund managers in order to manage the investment funds that they advise and offer to investors in either a publicly offered investment fund or on a private placement basis (in which case they are also typically registered as an exempt market dealer in order to facilitate direct investments in the fund).

The consultation does not appear to contemplate that investment fund managers will be regulated by Newco. This would result in many portfolio managers being subject to regulation by both Newco and the applicable CSA member (or members) resulting in an additional, unneeded regulatory burden and increased costs for these registrants.

We agree with McMillan LLP's recommendation that: (i) Newco be responsible for the prudential regulation of investment dealers, mutual fund dealers and national market surveillance matters; and (ii) CSA members be responsible for the statutory registration function and regulatory oversight of all categories of registration (investment dealers, mutual fund dealers, portfolio managers, investment fund managers, exempt market dealers and scholarship plan dealers). The prudential regulation authority of Newco would relate to matters including: (i) minimum capital requirements, (ii) liquidity requirements and (iii) identification and control of risks (at both a macro and micro level). A single SRO would remain subject to the oversight of the CSA in the manner we have proposed above in our comments in response to Item #3.

<u>Item #11</u>: Allow exempt market dealers to participate as selling group members in prospectus offerings and be sponsors of reverse-takeover transactions

We agree that EMDs should be permitted to expand the scope of their business activities to include participation as selling group members in prospectus offerings of securities and CPC offerings in connection with qualifying transactions and acting as sponsors for reverse takeover transactions.

<u>Item #20</u>: Introduce a regulatory framework for proxy advisory firms (PAFs) to: (a) provide issuers with a right to "rebut" PAF reports, and (b) restrict PAFs from providing consulting services to issuers in respect of which PAFs also provide clients with voting recommendations

We are highly supportive of these proposals including restricting proxy advisory firms from providing consulting services to issuers. There is no level of a Chinese wall that can effectively mitigate this most basic conflict. In addition, these process reviews can be viewed as black boxes and it should be mandated that submissions from non-clients be accepted, reviewed and addressed. It is important to have a level playing field to accept submissions and to have a process to require dialogue and communication. To the question, does the proposal restrict PAFs to either providing consulting services or making voting recommendations in respect of an issuer appropriately address conflicts of interest, we answer no. It should simply not be permitted.

<u>Item #21</u>: Decrease the ownership threshold for early warning reporting disclosure from 10 to 5 per cent

In comparison to the US, Canada's public capital markets are materially different and much smaller We do not support the change in the early warning threshold from 10% to 5%. This change in threshold was previously considered by the CSA and the determination made in 2016 that a reduction in threshold would not be appropriate given, among other things, the intended benefits of the enhanced transparency of a lower threshold were outweighed by the potential negative impacts and increased regulatory burden of implementing the lower reporting threshold. This would be a significant detriment to the competitiveness of the Canadian capital markets environment. The current early warning regime was recently updated in 2016 to enhance the integrity and quality of the early warning system. At this time, we believe no further amendments to the system are required, consistent with the CSA comments here.

Item #2: Separate regulatory and adjudicative functions at the OSC

We believe that for fair and efficient operation of the capital markets system there should be an independence and separation of adjudicative functions from regulatory functions and support efforts to achieve this objective. Of the two options, the creation of a new separate adjudicative entity or a bifurcated model with separation of the adjudicative and regulatory functions within a current regulator (OSC, CSA or CCMA) comprised of its own adjudicators and staff, we prefer the latter option as the creation of a new separate entity could have the potential to increase regulatory burdens on market participants by having yet another entity or body to deal with and by removing efficiencies in dealing with a single entity. Further, the OSC, CSA or even a future CCMA has or will have the expertise, knowledge and operational infrastructure to address issues and concerns. We further support strengthening of independence and governance and reducing conflicts of interest through separation and independence of the Chair and CEO positions for the regulatory and adjudicative functions.

Item #14: Introduce additional Accredited Investor (AI) categories

We recommend that AI and "permitted client" (under NI 31-103) criteria should be expanded to be less Canadian-centric in nature and take into consideration potential foreign investors that don't neatly fit either definition in form, but do so in substance. By limiting such definitions investors and registered firms are subject to increased but mostly unnecessary regulatory requirements such as certain client reporting, we agree with expanding qualifications such as the CFA CAIA, CAIA Fundamentals or another relevant course offered by local course providers. The CFA is considered a key proficiency requirement for registration as a discretionary manager to advise on and manage various securities, as are the CAIA courses for recommending alternative assets; therefore, these proficiencies should be appropriate for an individual to make a self-determination to invest in prospectus exempt securities.

Item #39: Greater rights for persons or companies directly affected by an OSC investigation or examination

We support measures to ensure transparency throughout the investigation process and initiatives to streamline the production of documents during the investigation process. We suggest the creation of a disclosure framework that provides greater fairness to subjects of investigations with appropriate disclosure and opportunity to respond to allegations prior to matters being made public, as once in the public domain there is a risk of serious harm to reputation. A proper process will serve to better protect investors while safeguarding the interests of market participants. We look forward to providing further input regarding details of a disclosure framework and measures to enhance rights of persons or companies affected by OSC investigations or examinations.

Item #22: Adopt quarterly filing requirements for institutional investors of Canadian companies

Institutional investors have reporting under NI 81-106, and we do not believe mandatory quarterly filing requirements should be adopted.

Disclosure requirements are currently in place for investment funds. Under NI 81-106, investment funds that are reporting issuers or mutual funds in a jurisdiction, including private funds, are subject to continuous disclosure requirements. These disclosures include, but are not limited to, the provision of financial statements, quarterly portfolio disclosures, and proxy voting disclosures. We believe the investor protection mandate is fulfilled with the existing requirements, that increasing the requirements may not provide further meaningful information to the marketplace, and additional requirements would be inconsistent with the regulatory burden reduction mandate.

The proposal attempts to mimic SEC 13F regulation, which currently is undergoing consultation for proposed amendments. The 13F framework has not provided intended market transparency. Instead, it has created a cumbersome, flawed reporting process for often-outdated information that largely benefits the shareholder tracking firms retained by issuers. The current proposed amendments are unlikely to do more than discourage shareholder engagement, magnifying visibility into the holdings of large fund managers while obscuring the holdings of the majority of participants entirely, as noted by SEC Commissioner Lee in her response[4].

Further Items

Item # 1: Expand the mandate of the OSC to include fostering capital formation and competition in the markets

In incorporating capital formation and fostering competitive capital markets into the OSC's mandate, the OSC would formalize this goal of helping spur economic growth in Ontario, as it does with its other mandates to ensure investor protection and ensure the integrity of the capital markets. It would not adversely impact the remaining mandates but rather provide a holistic approach in dealing with the capital markets and investors. However, modernizing the capital markets in Ontario cannot be done in a silo and incorporating the modernization directive with the other mandates ensures that changes can be made while considering investors, the markets and other capital market concerns.

Item #3: Strengthen the SRO accountability framework through increased OSC oversight

We are generally supportive of the Taskforce's recommendations designed to strengthen the governance and oversight of Canada's SROs. However, we are concerned with the proposed process to implement these changes (via amendments by the OSC to the SRO Recognition Orders) and have additional specific recommendations, as outlined below. We support the position recommended by McMillan LLP and have briefly summarized key aspects of the McMillan LLP comment letter on this item below.

We are concerned that if the amendments to the Recognition Orders are implemented, further fragmentation of our nascent national regulatory framework will be the inevitable result. Should Ontario unilaterally alter material aspects of the governance and oversight of the SROs by amending the Recognition Orders, it is reasonable to expect that other Canadian jurisdictions would respond with similar measures designed to reflect their own interests relating to the governance and operation of the SROs. We find the proposed inclusion of an OSC "veto" for key SRO publications and appointments to be particularly provocative.

The governance and oversight of Canada's SROs are national issues and require a coordinated national solution. The CSA has demonstrated its capacity to operate as an effective quasi-national regulator over the last several years making significant strides in harmonizing securities legislation across all

[4] https://www.securities-administrators.ca/uploadedFiles/RELEModernizationTaskforceReport.pdf

Canadian jurisdictions. Until such time as a viable national securities regulatory agency is in place, the CSA remains the best option to effect meaningful change in our capital markets. Ontario's capital markets are an integral element of Canada's economy and the OSC continues to play a central leadership role within the CSA. A unilateral amendment of the Recognition Orders could damage this leadership position.

We recommend that the OSC be directed to work with other CSA members to reform the governance and oversight of Canada's SROs, and work to towards a single SRO. The end result of a single SRO should bring lower costs, increased efficiencies, increased transparency and increased access to Canadian investors. This single SRO should have the appropriate technology, systems and infrastructure to handle all types of products, advisors and clients across Canada, in both small communities and large cities.

We support McMillan LLP's suggested SRO governance reforms to be implemented by the CSA including:

(i) consolidation of the operation and governance of the SROs within a single entity ("**Newco**") (discussed in further detail in our comments on Proposal 4 below);

(ii) determination of the optimal size of the Board of Newco;

(iii) a mechanism for the appointment of directors by CSA members and a resolution mechanism for the resolution of any disagreements concerning such appointments amongst CSA members;

(iv) a requirement that <u>all</u> directors of Newco be approved by the CSA;

(v) further development of the required criteria for a director of an SRO to be considered to be "independent", including a required "cooling off" period if a candidate has been previously employed by an SRO member.

(vi) a requirement that at least two-thirds of the Board of Newco be comprised of independent directors (including representatives of investor protection advocates);

(vii) a requirement that the Chair of the Board of Newco be independent;

(viii) the introduction of maximum term limits for directors; and a requirement that the Board approve the compensation of principal SRO executives in accordance with annual public interest and policy objectives developed and published by the CSA.

The CSA might consider establishing a standing committee responsible for the governance and oversight of SRO activities in Canada. We support McMillan LLP's suggestion that the SRO oversight committee should be comprised of permanent members from Ontario, Québec, Alberta and British Columbia, complemented by three rotating members (with three-year terms) from the remaining CSA jurisdictions. The SRO oversight committee would be empowered to establish sub-committees or working groups to address specific issues, as required, including ad hoc sub-committees or working groups headed by specific CSA members for matters having a specific local connection or importance.

The SRO oversight committee's responsibilities should include:

(i) development and publication of a three-year statement of policy and public interest objectives for Newco including long term recommendations of areas for the reduction of the regulatory burden and compliance costs of registrants;

(ii) development and publication of an annual statement of priorities for Newco in connection with the implementation of the three-year plan, including annual performance objectives for SRO executives upon which their compensation will be based;

(iii) approval of any significant new regulations or guidance developed by Newco or any material amendments to such regulations or guidance;

(iv) regular, as well as risk-based, oversight powers regarding the operations of Newco; and

powers to review and resolve any complaints received from SRO members relating to the operation of Newco.

We do not support the creation of a separate ombudsperson for the review and resolution of SRO member complaints as we are of the view that this would only create an additional layer of regulatory oversight and costs. We believe that this role might be performed more effectively by an SRO Oversight Committee.

<u>Item #6:</u> Streamlining the timing of disclosure (e.g., semi-annual reporting)

We are not supportive of semi-annual reporting. Any such initiative would be highly detrimental to investors. The combination of the current lag between reporting requirements and the beginning of a quarter (as much as 5 months or more at year end), and the use of technology, social media and other factor accelerating the rate of pace of change in markets impacting investment decisions suggest more, not less timeliness and transparency is appropriate. Any changes to decrease reporting frequency would be highly detrimental to the efficiency of capital markets.

Research has shown that quarterly reporting increases transparency and decreases the cost of capital. Investors can better price in risk and growth trends and deter fraudulent activities. While that same research has also indicated that quarterly reporting, fosters short-term thinking and increases costs to issuers, it would be inconsistent with other jurisdictions like the US. This, in turn, would put investors in reporting issuers in Canada at a disadvantage with respect to information flow, relative to other jurisdictions. The SEC continues to monitor this situation and Canada should look to other jurisdictions to ensure investors are not disadvantaged[5].

<u>Item #7</u>: Introduce an alternative offering model for reporting issuers

It is not clear on how the alternative offering model is consistent with the investor protection mandate, particularly for retail investors, when the civil and statutory protections would not be available. Rather than removing the prospectus requirements, streamlining those requirements to better cross-reference to documents incorporated by reference would likely be a better option. Correspondingly, we suggest making point-of-sale disclosures a little bit more robust with the view to

[5] https://www.sec.gov/comments/s7-26-18/s72618-4826123-177031.pdf

better utilize the currently available documentation, in a user-friendly and timely manner, rather than eliminating documentation, especially those on which certain legal rights are based.

Item #8: Introduce greater flexibility to permit reporting issuers, and their registered advisors, to gauge interest from institutional investors for participation in a potential prospectus offering prior to filing a preliminary prospectus

This would be helpful to allow for institutional investors to receive pre-marketing in the context of private placements. Accredited investors are currently considered to be sufficiently sophisticated to purchase securities without the benefit of a prospectus, being viewed as able to withstand the corresponding risk associated with less disclosure. The pre-marketing option should be within the context of available prospectus exemptions under NI 45-106 to ensure that the criteria for sophisticated investors is met.

Should these initiatives be advanced, it would be appropriate to impose conditions:

- Limits on the pre-marketing time period to ensure that the option to invest is prescribed within a limitation rather than being open-ended;
- Confidentiality and standstill agreements should be entered into. Currently, many large hedge fund managers are approached by issuers and enter into standstill agreements which assists in avoiding tipping and insider trading rules. Institutional investors who engage in these pre-marketing activities should be subject to review on their policies, procedures and processes to mitigate such risks.
- Limits on the number of potential investors that can be approached.
- A requirement that a large portion of the offering be made up of investors (including retail investors) that were not approached beforehand.

Item # 9: Transitioning towards an access equals delivery model of dissemination of information in the capital markets, and digitization of capital markets

We are supportive of the option of electronic delivery of documentation, though would like to submit that an annual opt-in request may be excessive and costly operationally, especially for emerging managers and that opt-in at the time of initial purchase probably should be sufficient (which currently often occurs in practice). Investor consent would still need to be obtained as to which option is preferred (receipt of electronic documents, receipt of physical documents or the investor's initiative of obtaining the information on their own). Many alternative investment managers already seek to obtain consent to provide electronic delivery as part of their subscription agreements. Many fund managers already post their continuous disclosure documents to their website.

It may not be possible to move to a single electronic model since not all investors will have the appropriate technology or knowledge to access the information. Continuous disclosure documents can be posted to a website which often already occurs (and which are made publicly available on SEDAR). The regulatory requirements with respect to electronic delivery (i.e. NP 11-201) are significantly outdated and revisited, though it was our understanding that many of these concepts were being considered with the OSC's regulatory burden reduction initiative.

Item #10: Consolidating reporting and regulatory requirements

We agree that there should be a review of documentation that is currently required to be produced for regulatory and investor protection purposes and eliminate duplicative information that is simply being presented via different media (eg. information between the AIF and MD&A or MRFP is duplicative). An initial reconciliation could be completed to determine what information is required to be produced, what form of documentation provides such information in a meaningful and appropriate manner, frequency, form and the best location for this information to reside. These changes should be considered in the context of enhanced technology and digitalization.

Item #16: Enact a prohibition on registrants benefiting from tying or bundling of capital market and commercial lending services, and a requirement for an attestation by a senior officer of the appropriate registrant under the applicable disclosure requirements.

We believe that competition and innovation is essential to fostering confidence in capital markets and creating a modern securities regulatory framework to strengthen the economy. We note the CSA comments published on this topic, and look forward to participating in this consultation.

Item #18: Introduce a retail investment fund structure to pursue investment objectives and strategies that involve investments in early stage businesses

We would be supportive of general retailization of private equity and venture capital models, though it would need to ensure appropriate investor protection and adequate terms (especially liquidity and asset-liability matching. For example, we do not believe that liquidity nor investments in early stage companies would be sufficient to support an accurate daily NAV. Currently, IIROC dealers are engaging with select private equity asset managers to deliver retail access through their advisors. In these structures, dealers negotiate custom access with specific terms, including monthly, quarterly or annual liquidity. Our dealer members note these products are certainly not intended or appropriate for every client due to their lack of daily liquidity and are more appropriate for accredited investors at this time. While it is noble to consider a potential new source of financing for small business, we believe a number of considerations would need to be established to proceed.

In conjunction with any retail private equity initiative, we believe that the definition of the term “illiquid asset” in National Instrument 81-102 – Investment Funds should be revisited. This term restricts the types of assets which may be held by mutual funds and alternative mutual funds and does not reflect the current reality of liquidity options that are available in relating to certain types of asset classes. The modernization of this term would broaden the types of investments which may be made by public mutual funds and investment funds thereby encouraging further capital markets activity.

We generally support the position recommended by McMillan LLP and have briefly summarized key aspects of the McMillan LLP comment letter on this item below.

Private equity funds and investment funds have been treated very differently from a regulatory perspective historically. Due to the nature of private equity capital investments in new or emerging private issuers, liquidity for investors in private equity funds is usually extremely limited. Most private equity funds do not permit the redemption of interests in the fund except in exceptional circumstances.

The current forms of Canadian retail fund structures and investment company model appear to be inadequate solutions for the retail offering of a private equity fund. Conventional and alternative mutual funds require more frequent liquidity than would be ideal for a private equity strategy and closed-end funds typically trade at a discount to NAV. Each of these structures also require a portfolio manager and an investment fund manager. An investment company is not limited regarding the type or nature of investments it may make and its securities must be offered by means of a long-form prospectus. If retail private equity funds are to become a reality, we believe that a new fund structure must be created.

We agree with McMillan LLP's proposal that the OSC be directed to work with the CSA and Canadian stock exchanges to develop a new "private equity investment entity" ("**PEIE**") structure incorporating, at a minimum, the following elements:

(i) a new retail investment product category be created either by way of amendment to existing National Instruments (e.g. NI 81-102 and NI 81-101)[6] or pursuant to a new National Instrument;

(ii) the PEIE must have an investment objective of investing its assets in the securities of private issuers;

(iii) the investment strategy of the PEIE must include active involvement by the manager in the business of investee issuers

(iv) the securities of the PEIE must be listed on a recognized Canadian stock exchange;

(v) the securities of the PEIE must be offered by means of a simplified prospectus, annual information form and PEIE facts document;

(vi) the securities of the PEIE must be distributed through registered securities dealers;

(vii) the manager of the PEIE is not required to be registered as either a portfolio manager or investment fund manager; and

(viii) the PEIE is generally subject to the same continuous disclosure obligations as other reporting issuers.

We believe a PEIE model similar to the one described above would achieve the Taskforce's objective for a professionally managed private equity investment product that provides retail investors with access to this category of investment strategy. As a listed entity, the PEIE would generally be eligible for investment by Registered Plans and, as such, could achieve a significant size and scale to permit meaningful investments in start-up and early stage issuers. These issuers would benefit from greater access to capital as well as the management experience and expertise of the PEIE manager.

Item #19: Improve corporate board diversity

We note the increasing industry awareness of the many corporate benefits of more diverse teams across multiple levels, including at board level, especially as investors increasingly base ESG considerations in their investment decision making process. This is reflected in AIMA's work to empower firms that are seeking to do more in this area, which in 2019 saw the publication of The Alternatives, with a list of 45 action items firms might consider adopting to expand their inclusion and diversity policies and practices. Despite industry positivity surrounding the importance of diversity and inclusion, we would highlight that there is not a consensus view as to the effectiveness of more

[6] *National Instrument 81-101- Mutual Funds Prospectus Disclosure*, Unofficial Consolidation online (pdf): *Ontario Securities Commission* <https://www.osc.gov.on.ca/documents/en/Securities-Category8/rule_20190103_81-101_unofficial-consolidation.pdf>.

interventionist approaches such as targets. Locally, Women in Capital Markets continues to examine the evolving profile and sentiment regarding diversity and inclusion within Canada's financial services industry.

More broadly, we note that firms already place emphasis on broader issues related to board diversity in the context of overall corporate governance, in many cases due to legal obligations. Such obligations impact the nomination and selection process for directors, as well as ensuring that directors have the requisite expertise and ongoing training to fulfill their duties. These are ultimately designed to support effective decision-making and oversight of senior management at board level and should be evaluated before any further regulatory changes are made to improve the participation of underrepresented groups at board level. In addition to term limits (with the exception of any large shareholders), the committee might also consider encouraging setting diversity targets for type and number of candidates interviewed for various positions.

Item #23: Require TSX-listed issuers to have an annual advisory shareholders' vote on the board's approach to executive compensation

We agree this proposal being applicable to all reporting issuers. In doing so, boards will be held to account and investor protection ideals will be fulfilled. Executive compensation should be tied to improved shareholder value and executives should be held accountable if they are not delivering on the objectives set forth by the board nor if shareholder value has not improved. Shareholders are the ultimate beneficiary of the decisions made by management and therefore, should have a say on the compensation of such management. Similar to the type of management and performance of management being important considerations in due diligence, careful attention should be given to compensation levels of executive management.

Item #27: Amend securities law to provide additional requirements and guidance on the role of independent directors in conflict of interest transactions

There have been significant concerns suggested regarding changes to board composition that have preceded major transactions requiring independent board approvals. Restrictions should be imposed on new directors being deemed independent within a certain time frame, particularly when there is a large shareholder that can influence board composition. In addition, it is important to consider board nominee of a shareholder with a large ownership to have representation, regardless of the duration of their tenure.

Item #30: Eliminate the non-objecting beneficial owner (NOBO) and objecting beneficial owner (OBO) status, allow issuers to access the list of all owners of beneficial securities, regardless of where securityholders reside, and facilitate the electronic delivery of proxy-related materials to securityholders.

We agree with the proposals. Part of regulators' investor protection mandate is to ensure that investors have adequate and meaningful information to make informed decisions. Notwithstanding that a portion of investors will hold their investments in nominee name, the ultimate beneficial owner should have appropriate information about their investments and have the ability to affect change, through their votes, if they seek changes. The provision of such information should be coordinated through enhanced technology. The enhanced use of open data must be considered within the context of privacy rules. The potential benefit of open data may be for data sharing across jurisdictions, for those companies/registrants that conduct business activities internationally, so there is consistent information being reported that doesn't require companies/registrants to spend time reproducing information that is substantially similar but in different form. There must be a level playing field - if provide issuers with additional information, then certain activist investors (and difficult to know what percentage of these) may be at a disadvantage vs. others.

<u>Item #31</u>: Create an Ontario Regulatory Sandbox in order to benefit entrepreneurs and start-ups. In the longer term, consider developing a Canadian Super Sandbox

It is not clear what the issues are that this Sandbox would solve. We are supportive of regulatory services and relief that would spur innovation, capital raising, reduce burden and more, though identification of what specifically we are attempting to solve (especially beyond the current regulatory burden reduction initiatives) would be beneficial to provide more meaningful comment.

<u>Item #32</u>: Requirement for market participants to provide open data

It is not clear to the extent that open data may assist businesses in providing new products and services, such that the privacy of investors and investor protection generally is not compromised. Capital markets work on the basis of participants having access to trade data (e.g. provided by trading venues) which is costly and subject to complex licencing arrangements. So as much as it's good to think about how to ensure that retail client data flows between providers properly, it's as important to look the supply of regulated data.

We would reference the McMillan LLP comment letter on this item and highlight that initiatives carried out in other jurisdictions globally have occurred at the federal level and relate primarily to retail banking, as opposed to investment products.

We suggest the Taskforce consider the development of a centralized investor portal rather than an OSC or CSA mandate for capital markets participants to share open data. An Open Data Portal would enable investors to provide all relevant data in a centralized location in a standardized format that would be accessible to all capital markets participants (including Fintech companies) on the Portal. Investors would voluntarily participate on the Portal with the understanding that the data they provide would be made available to capital market participants for the purposes of offering or designing investment products which may be of interest to them. We believe that the development of an Open Data Portal would enable Ontario and/or Canada to assume a global leadership role in this area.

<u>Item #34</u>: Consider automatically reciprocating the non-financial elements of orders and settlements from other Canadian securities regulators and granting the OSC a streamlined power to make reciprocation orders in response to criminal court, foreign regulator, SRO, and exchange orders

We agree with the proposals, which align with the harmonization between jurisdictions that the CMRA will hopefully address and which is consistent with the investor protection and capital markets integrity mandate of the regulators. A registrant who is a bad actor is such regardless of the jurisdiction in which issues have arisen.

<u>Item # 36</u>: Create a prohibition to effectively deter and prosecute misleading or untrue statements about public companies and attempts to make such statements

We agree with the proposals; misrepresentation gives rise to civil liability under the Canadian securities regime. We recommend the same requirements be imposed on reporting issuers to ensure consistent and accurate information is being provided to investors from which an informed investment decision can be made. This ensures a level playing field as institutional investors may receive information behind closed doors (because they have access to management) while retail investors generally don't have the same level of access. If similar requirements that are required of registrants, were imposed on public companies (e.g. statements cannot be misleading, claims must be substantiable, and opinions and views should be identified as such), then this would assist in combatting abusive behavior. We would point back to our comments in Item #13.

<u>Item #43</u>: Clarify that requiring production of privileged documentation is not allowed

We believe market registrants would challenge the request for privileged information, as occurs in the US; therefore, it would be appropriate for a position to be taken which would ensure a level playing field in the industry.

<u>Item #44</u>: Implement OSC procedural change to provide an invitation to discuss OSC Staff's proposed statement of allegations at least 3 weeks before initiating proceedings

We suggest that OSC invite respondents to discuss alleged infractions and a potential resolution with OSC staff at least four weeks before it delivers a notice that OSC staff will be initiating administrative enforcement proceedings. There needs to be a better ability to consider issues, respond and provide feedback privately before a public process starts.

<u>Item #47</u>: Give the power to designated dispute resolution services organizations, such as the Ombudsman for Banking Services and Investments (OBSI), to issue binding decisions ordering a registered firm to pay compensation to harmed investors, and increase the limit on OBSI's compensation recommendations

The proposal to give a designated dispute resolution services organization the power to issue binding decisions may be a potential issue and may not be best to make it binding if parties agree to arbitration.

Conclusion

We appreciate the opportunity to provide the Capital Markets Modernization Taskforce with our views. Please do not hesitate to contact the members of AIMA set out below with any comments or questions that you might have. We would be pleased to meet with you to discuss our comments and concerns further.

Yours truly,

ALTERNATIVE INVESTMENT MANAGEMENT ASSOCIATION CANADA

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