Reduced regulatory burden for investment funds and managers - progress for 2022

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Recent rule amendments made by the Canadian Securities Administrators to various investment fund-related instruments represent a step in the right direction in reducing the regulatory burden for investment funds and their managers. These amendments are part of the long-standing regulatory burden reduction initiative of the Canadian Securities Administrators that commenced in 2017, known as Project RID.

- Final rule amendments came into force on Jan. 5 and Jan. 6, 2022. These amendments provide for consolidation of the mutual fund Simplified Prospectus (SP) and Annual Information Form (AIF), as well as conditional codifications of commonly granted exemptions, which can be relied on by investment funds that are reporting issuers and, in some instances, by investment funds that are offered by prospectus exemption.
- On Jan. 27, 2022, the CSA published proposed amendments to the mutual fund and ETF prospectus rules, seeking to achieve even greater regulatory burden reduction through the lengthening of timing to file a prospectus for mutual funds and ETFs from annually to every two years (although Fund Facts and ETF Facts must still be updated and filed annually). The CSA also published for comment a consultation paper that sets out a conceptual framework for a base shelf prospectus filing model that could apply to all investment funds in continuous distribution. Comments are due on these proposals by **April 27, 2022.**

Annual information form not required for publicly offered mutual funds

Through amendments to National Instrument 81-101 *Mutual Fund Prospectus Disclosure* (NI 81-101), the CSA repealed the requirement for a mutual fund in continuous distribution to file an AIF, in addition to an SP, and instead requires the SP to include certain disclosure currently contained in the AIF. These amendments came into force on Jan. 6, 2022, although mutual funds filing prospectus documents after this date and before Sept. 6, 2022, are not required to comply with the new requirements, but may do so if they choose. All new or renewal prospectus filings made on and after Sept. 6, 2022 must comply with the new requirements.

The SP will still consist of a Part A (general information about all mutual funds covered in the document) and a Part B (specific information about each mutual fund) and, for the most part, the contents of, and requirements for, Fund Facts documents are unchanged. However, some minor changes are necessary and new disclosures for new funds are mandated.

Creating the initial consolidated SP will take some effort for fund managers. However, in subsequent years, we expect to see more substantial savings in updating the document. The new consolidated disclosures are simpler than the old form requirements, and some of the more time-consuming disclosure elements of the SP and AIF have been dropped or streamlined, including those described below:

- There is no longer a requirement to disclose the principal holders of 10 per cent or more of the securities of any class or series of a mutual fund.
- The amount of information to be disclosed in respect of individuals involved with the investment fund and investment fund manager has been reduced. For instance, disclosure relating to occupational history and principal occupation of these individuals has been streamlined.
- The amount of information to be provided about portfolio advisers has been reduced. For instance, an individual's length of time of service and their business experience in the last five years will no longer need to be disclosed.
- There is no longer a requirement to disclose the percentage of the management fee that was paid to dealers as compensation in connection with the distribution of securities of the mutual funds or paid for any marketing, fund promotion or educational activity in connection with the mutual funds in the last completed financial year.
- There is no longer a requirement to disclose the suitability of the mutual fund for particular investors, including the level of risk tolerance appropriate for investment in the mutual fund, since this information is duplicative of the disclosure in the Fund Facts and ETF Facts.
- The table disclosing the fund expenses indirectly borne by investors has been dropped.

The CSA have clarified that previously granted exemptions relating to prospectus disclosure continue to apply:

- Exemptions previously granted from a requirement prescribed by Form 81-101F1 and 81-101F2 continue to apply to any substantively similar requirement prescribed in the amended Form 81-101F1.
- Any conditions to an exemption required to be disclosed in the AIF, may be disclosed in the SP.
- Mutual funds that have an exemption to file an AIF and SP in accordance with Form 81-101F1 and F2 instead of filing a prospectus in accordance with Form 41-101F2 (e.g. for ETF series of a mutual fund), may comply with the conditions to such an exemption by filing a SP in accordance with the amended Form 81-101F1.

Pursuant to amendments to National Instrument 81-106 *Investment Fund Continuous Disclosure* (NI 81-106), the CSA continue to require an AIF to be filed for investment funds not in continuous distribution. The form to be used will depend on the date and nature of fund's last prospectus:

- An ETF no longer in continuous distribution will use Form 41-101F2.
- A mutual fund which last distributed securities under the revised Form 81-101F1 will use this document.
- A mutual fund, which ceased distribution before updating its prospectus documents to use amended Form 81-101F1 will continue to use the AIF Form 81-101F2.

Designated regulatory disclosure websites for investment funds

Under amendments to NI 81-106, every public investment fund must identify a designated website on which it will post all required regulatory disclosure. This website must be publicly accessible, and maintained by the fund, or on behalf of the fund, by the investment fund manager or a person designated by the investment fund manager. Designated websites should be maintained and monitored by the compliance systems of the applicable investment fund manager.

It is clear that the CSA are not yet ready to permit "access equals delivery" through postings of offering and continuous disclosure documents on designated websites, which would negate having to deliver physical or electronic documents. They did state, however, that they view the designated website as a *potential* launch point for other burden reduction initiatives, which might include modifications to the acceptable means of delivering offering and continuous disclosure documents. The January 2022 proposed amendments did not refer to this concept.

Notice and access system for securityholder meetings

In 2013, the CSA amended National Instrument 54-101 *Communication with Beneficial Owners of Securities of a Reporting Issuer* to permit non-investment fund reporting issuers to deliver a notice and summary information about proxy-related materials to registered and beneficial owners of securities, along with instructions on how to access the complete materials (the notice-and-access system). Many investment fund managers sought exemptions in order to use the notice-and-access system, which we spearheaded in 2016 through an industry group application and subsequent decision. Effective Jan. 5, 2022, amendments to NI 81-106 codify the previously granted relief and now allow all investment fund managers to use the notice-and-access system for investment fund securityholder meetings.

Personal information form filings with prospectuses - streamlined

In amendments to NI 81-101 and National Instrument 41-101 *General Prospectus Requirements* (NI 41-101), the CSA eliminated the requirement to file a Personal Information Form (PIF) for those individuals who are registrants or "permitted individuals" and therefore have already filed a Form 33-109F4 *Registration of Individuals and Review of Permitted Individuals* (and thus have already been vetted by the regulators). As the PIF and the Form 33-109F4 require the disclosure of similar

information, the CSA have acknowledged that the PIF requirement for these individuals is an unnecessary regulatory requirement.

We urged the CSA to reconsider the frequency with which the remaining individuals have to submit an updated PIF so that at a minimum, the timing requirements for updated PIFs are consistent between the stock exchanges and securities regulators. The CSA noted, as a future initiative, that they are opening discussions with the exchanges on further streamlining information requirements concerning PIFs, and are considering the request to strive for consistency with the five-year PIF filing requirement of the exchanges.

Exemptions codified in respect of certain related party transactions

Through amendments to National Instrument 81-102 *Investment Funds* (NI 81-102) and National Instrument 81-107 *Independent Review Committee for Investment Funds* (NI 81-107), the CSA codified frequently granted types of exemptions concerning related party transactions, which would otherwise be prohibited. Subject to specified conditions, including, most notably, approval of an independent review committee (IRC), these amendments permit:

- Investments by non-reporting issuer funds in other non-public investment funds through a new exemption in NI 81-102. The underlying funds can be either Canadian or non-Canadian funds, but must comply with restrictions on holding illiquid investments and have available financial statements. Specified disclosure about these investments must be provided to investors in the top funds. Despite our comment that the underlying fund should not be required to comply with the restrictions concerning illiquid investments in NI 81-102, the CSA has maintained this restriction in the final amendments. The CSA notes it is consistent with the conditions of prior relief and is needed for the purposes of ensuring liquidity exists at the lower level of a fund-on-fund arrangement (though we consider that this may have been better achieved by a liquidity matching requirement instead).
- "Dealer managed investment funds" subject to NI 81-102 to purchase non-exchange traded debt securities of reporting issuers (there is no longer a rating requirement for such debt) underwritten by related dealers and privately placed, along with continuing to permit exchange-traded securities issued under a prospectus offering.
- Inter-fund trading among publicly offered investment funds, privately placed investment funds and managed accounts of same portfolio manager. Previously, NI 81-107 only permitted inter-fund trading between publicly offered investment funds under common management. Now, inter-fund trades may be made at the last sale price for exchange-traded securities, in addition to the other options. The requirement for "bid and ask prices" of securities to be "readily available", with CSA commentary as to what this means (which is troublesome for non-exchange traded debt securities), has not been amended.
- Investment funds that are not reporting issuers to invest in securities of exchange-traded securities of related issuers, in the same way as publicly offered investment funds.

- Investment funds (both publicly offered and non-reporting issuers) to invest in non-exchange traded debt securities of a related issuer in the secondary market provided such debt has a designated rating and the other conditions are met.
- Investment funds (both publicly offered and non-reporting issuers) to invest in long-term debt securities of a related issuer made under a distribution of such debt, provided such debt has a designated rating and the other conditions are met.
- Portfolio managers of investment funds (both publicly offered and non-reporting issuers) and of managed accounts to trade, as principal, in debt securities with a related dealer, subject to conditions, including a condition that the bid and ask price of the debt security is readily available (and if it is not, to obtain an independent quote).

The CSA did not proceed with proposed amendments published for comment in 2019 that would permit in specie subscriptions and redemptions involving related managed accounts and mutual funds. The CSA explained that they want to consider the implications of this activity against the guidance set out in the 2020 CSA Staff Notice 81-333 *Guidance on Effective Liquidity Risk Management for Investment Funds.* The CSA state that this guidance necessitates a reconsideration of the conditions of in specie relief decisions and how liquidity management practices should align with the transfer of illiquid securities as part of an in specie transfer. The CSA note they will continue to consider these exemptions on a case-by-case exemption application basis.

The CSA have confirmed that funds and their managers with previously obtained exemptions that have now been codified by these amendments have the choice of continuing to rely on those earlier decisions, which may have specific tailored conditions, or to rely on the codified exemptions. This flexibility will provide certainty to managers, which would otherwise have to consider whether any changes to their operations were necessary in order to comply with the new conditions.

The codified conditions must be carefully considered. In particular, for funds not otherwise subject to NI 81-102 and NI 81-107, to rely on the conditions, they must establish an IRC, which will have a focus on the applicable transactions and must comply with specified provisions of NI 81-107.

Pre-approval criteria for investment fund mergers broadened

Amendments to NI 81-102 broadened the pre-approval criteria for investment fund mergers where the proposed merger transaction is neither a tax-deferred transaction nor a qualifying exchange, or where the investment objectives, valuation procedures and/or fees for a terminating and continuing fund are not considered to be “substantially similar”.

The amendments deem these transactions to meet the pre-approval criteria (and therefore do not require regulatory approval), if the manager reasonably believes that the transaction is in the best interest of the investment fund, despite the tax treatment or the investment objective, valuation or fee differences, as the case may be. Mergers proceeding under the broadened criteria remain subject to securityholder approval and IRC recommendation, and the related information circular must disclose how the merger

is in the best interest of the investment fund, in light of not meeting these criteria, amongst other prescribed disclosures.

No regulatory approval for change of manager, change of control of manager and change of custodian that occurs in connection with a change of manager

The CSA repealed the regulatory approval requirements in NI 81-102 for a change of manager, a change of control of manager and a change of custodian that occurs in connection with a change of manager. Given that National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* requires notices of certain transactions involving registrants, including investment fund managers, to be filed with the applicable regulators, and regulatory non-objections to be received, the NI 81-102 requirements were duplicative.

Securityholder approval is still required for a change of manager and certain prescribed information about the proposed change in manager must be disclosed in the Information Circular. The disclosure obligations are broad and include, amongst others, required disclosure of all material information regarding the business, management and operations of the new manager and a description of all material effects the change will have on the investment fund's securityholders.

Delivery obligations for Fund Facts in specific circumstances

Amendments to NI 81-101 expand existing exceptions from the Fund Facts delivery requirements to include purchases of mutual funds made in managed accounts or by permitted clients that are not individuals, as well as subsequent purchases under model portfolio programs or products, portfolio rebalancing services and automatic switch programs. The latter exceptions have a number of conditions, which are intended to mirror, with modifications, the existing exceptions permitted for pre-authorized payment plans (PACs). The CSA also amended NI 41-101 to provide for the same exemptions from the ETF Facts delivery requirements in respect of investments in ETFs.

Amendments to Form 81-101F3 will allow a single consolidated Fund Facts document to be filed for all classes or series of securities of a fund offered in an automatic switch program. We encouraged the CSA to permit the consolidation of series or class-specific Fund Facts and ETF Facts for a fund, even in the absence of an automatic switch program, as a significant burden reduction mechanism. While the CSA has not included those amendments in this initiative, the CSA noted that they might publish proposed amendments to the Fund Facts and ETF Facts forms in the future in response to support from industry for consolidation.

Proposed amendments to investment fund prospectus filings

Under the January 2022 proposed amendments to NI 41-101 and NI 81-101, the CSA propose to change the filing deadline for renewals of investment fund prospectuses, from annually to biennially (every two years). ETF Facts and Fund Facts will still be required to be filed annually. In addition, the CSA propose to drop the so-called "90-day" requirement, which requires a final prospectus to be filed within 90-days of a preliminary prospectus. More problematically, the CSA also propose that all amendments to prospectuses, for instance required because of a material change to a fund, be filed as an "amended and restated prospectus" instead of a "slip sheet" amendment to the prospectus.

The CSA explain that these proposed amendments are also part of the burden reduction initiative. They caution that the various members of the CSA will be reviewing their fee schedules and rules – the CSA state that "the adoption of this change will be contingent on not having a negative impact on filing fees".

We will be commenting on some technical issues with the proposed amendments, as well as giving our views on the proposal to require all prospectus amendments to be filed as amended and restated prospectuses, but otherwise we support the proposed changes. We will encourage the CSA to complete their examination of filing fees and urge them to not hold up these changes unnecessarily.

The Ontario Securities Commission published a qualitative and quantitative analysis of the anticipated costs and benefits of the proposed amendments. Among other things, the OSC suggests that shift to a biennial prospectus filing model will result in annual cost savings to all public funds and fund managers of $15,792,030 across all CSA jurisdictions (this cost savings is the result of anticipated reduction in legal costs, audit costs and translation costs – all of which are estimated).

The OSC's cost benefit analysis contains more information about regulatory filing fees. In this analysis, the OSC suggests that local fee rules will be changed such that current filing fees for prospectuses will instead be replaced with filing fees for ETF Facts and Fund Facts. Specifically, the OSC proposes that OSC Rule 13-502 *Fees* will be amended such that investment funds will pay an activity fee on the filing of preliminary or pro forma ETF Facts and Fund Facts, and will reduce the amount of activity fees payable by ETFs to be the same as the activity fee for conventional mutual funds. We note that there is still a higher activity fee payable by ETFs from that payable by mutual funds on prospectus filings – there is no change to this activity fee proposed in the recent significant revamp of OSC Rule 13-502 which was published for comment on Jan. 21, 2022. These OSC fee rule changes are out for comment until April 21, 2022.

The CSA's conceptual framework for a new base shelf prospectus filing model for investment funds refers to National Instrument 44-102 *Shelf Distributions* for inspiration, and although it is lacking in details, would seemingly require:

- Fund Facts and ETF Facts to be filed annually and delivered as currently required;
- A Base Shelf Prospectus to be filed, which "could" have a lapse date beyond 25 months – this document would contain only information that would not change annually;

- A document to be filed [the timing of such filing is not set out] that would contain information that changes annually and that would be incorporated by reference into the Base Shelf Prospectus; and
- The certificates for a Base Shelf Prospectus would be forward looking, which continue to give investors protections for misrepresentations.

The CSA then ask for responses to various open ended questions on their proposal. This model can be expected to take some time to develop.

BLG can help you adjust to the changes and answer your questions

Please contact any of the authors of this Bulletin or your usual member of BLG's Investment Management Group if you would like to discuss how the final amendments to the investment fund rules affect your business and operations. We would be pleased to assist you in providing comments on the January proposed amendments – either the prospectus filing methods or the Ontario fee rule changes.

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