

A large, abstract graphic in the top right corner features a network of interconnected blue nodes and lines, resembling a globe or a complex web structure, set against a light blue background.

Canada

Regulation

FUNDS AND FUND MANAGEMENT 2009

2.1 Type of funds

Mutual funds may be established as corporations under the various provincial and federal corporation acts, as trusts or as limited partnerships in certain cases.

2.2 Laws

Canada has a well-developed fund management sector with a sophisticated regulatory framework. The regulatory framework falls under the jurisdiction of the provinces of Canada and there is no federal framework established in this area. Each province has its own securities regulatory standards, which are formulated to set standards of investor protection. A fund must be separately registered in each province in which it wishes to market.

Although the legislation varies as between provinces, national policies have been established which are applied in all provinces. The standards relate to the marketing and administration of mutual funds as well as the permitted investment activities. In addition, the Investment Funds Institute of Canada (IFIC) publishes guidelines and rules to which its members are expected to adhere. Although not a self-regulatory organization in the accepted sense of the term, the IFIC is able to ensure a discipline amongst its members.

2.3 Managers, trustees, and custodians

Banks and trust companies may act as custodians and as trustees of funds. Trust companies are incorporated and regulated under the Trust and Loans Companies Act (federal legislation) or under the applicable provincial legislation. There are specific requirements to be a trust company including a minimum share capital. A manager of a fund must have at least one individual qualified for registration as an investment counsel or portfolio manager under the regulations of one of the securities commissions.

The fees of managers and of trustees are not legally restricted but there are extensive disclosure requirements relating to the fees.

2.4 Investment restrictions

There are several restrictions on the investments which a fund may make under the regulations laid down by securities authorities. The principal restrictions are shown below.

A fund may not without prior approval of the securities authorities:

- invest more than 10 percent of the net assets of the fund in any one issuer other than a government security or a security issued by a clearing corporation;
- hold more than 10 percent of any class of securities of any one issuer;
- purchase real property such as real estate;
- purchase mortgages, except where the fund is established as a mortgage fund, other than permitted mortgages not exceeding 10 percent of the total assets of the fund;
- invest more than 10 percent of the total assets in illiquid investments such as unlisted limited partnership interests or securities of a private company;
- purchase securities for the purpose of exercising control or management of the issuer of the securities;
- purchase or sell commodities other than gold or approved gold certificates, the holding of which is limited to 10 percent of the total assets of the fund;
- purchase or sell derivatives except for permitted derivatives, which are those used for hedging purposes, for non-hedging where there is no leverage, or to close out a position in a derivative. The rules governing the use of derivatives are fairly restrictive;
- invest in securities of any other mutual fund with certain exceptions such as another mutual fund qualified for sale by one of the securities authorities. Prior approval by the securities authority is required if more than 10 percent of the net assets are to be invested in another mutual fund;
- purchase securities on margin or sell securities short other than as specifically permitted in connection with derivatives transactions;
- engage in lending money (other than by way of purchasing debt obligations), engage in underwriting or guarantee securities;
- pledge any of its assets (except as may be required for posting margin to effect permitted derivative transactions); and
- purchase securities other than through normal market facilities on an arms-length basis.

2.5 Borrowing

A fund may not borrow money without the prior approval of the supervisory authorities, except as a temporary measure to facilitate redemption of units.

2.6 Accounts and prospectus

A fund is obliged to publish its accounts and to make them available to the public. A fund is also obliged to publish a prospectus, which must be approved by the appropriate securities commission prior to publication. A fund may have different accounting and tax year-ends. Generally, the year-ends are the same but this is not always the case; for instance, a unit trust may choose an accounting year-end other than 31 December whereas such a trust must have a 31 December year-end (or for some funds that qualify, a 15 December year-end if it so elects) for income tax purposes. Other than the tax year-end of an (inter-vivos) trust being 31 December (or 15 December), there are no other corporate, trust, or tax prohibitions on choosing a year-end.

A tax year cannot exceed 53 weeks whereas for accounting purposes, the fiscal period is generally 365/366 days (and possibly as long as 370) although in some unusual cases, the accounting fiscal period (for reporting purposes) may be longer such as the situation where the normal 12 month year is combined with a shorter period because of a change in the year-end. Under securities law, the fiscal year cannot be longer than 12 months.

2.7 Supervision

Each province and territory of Canada has its own supervisory authority for funds. There are ten provinces and three territories. The largest authority is the Ontario Securities Commission but its authority is confined to the province of Ontario. Its address is 20 Queen Street, West, Suite 800, Toronto, Ontario, N5H 2S8.

If not marketed to the public a fund need not comply with all of the regulations established by the various securities commissions. However, the taxation treatment of a fund may be affected by inadequate public distribution as it may then fail to qualify as either a mutual fund trust or a mutual fund corporation.

2.8 Fund ownership

There are no restrictions on the percentage of units/shares in the fund which may be held by any one person or group of persons.

2.9 Fund structure

Funds of funds are permitted but are subject to many restrictions. Umbrella funds are not specifically precluded.

2.10 Stock exchange

A stock exchange quotation is not available in Canada for locally registered open-ended funds but the popularity of exchange-traded funds in Canada has grown substantially over the past few years.

2.11 Bank secrecy

New privacy legislation was introduced for Canadian companies on January 1, 2004. Canada also has laws relating to money laundering and banks are required to report certain transactions to FINTRAC.

2.12 Fund set-up

It takes approximately three months on average to create a fund in Canada and the costs, including professional fees, etc, are likely to amount to approximately CAD 100,000.

2.13 Foreign funds

Foreign funds are not permitted to market in Canada. They cannot be registered with the Securities Commission of a province because in order to register, funds must be created (either under the incorporating document or the Declaration of Trust) in Canada.

2.14 Bearer shares

Bearer units are not known to be used.

2.15 Use of the internet

The internet is a widely used medium for providing information regarding mutual fund products in Canada. It is therefore an increasingly important part of the overall marketing strategy of most mutual fund companies in Canada. Advertising and marketing on the internet are subject to the same regulations governing these activities in other media forms, such as print, radio, and television.

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act upon such information without appropriate professional advice after a thorough examination of the particular situation.