

**GENERAL OVERVIEW
OF A
FLOW-THROUGH LIMITED PARTNERSHIP
STRUCTURE FOR AN INITIAL PUBLIC OFFERING**

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GENERAL OVERVIEW OF A FLOW-THROUGH LIMITED PARTNERSHIP STRUCTURE OF AN INITIAL PUBLIC OFFERING¹

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Cassels Brock & Blackwell LLP

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INTRODUCTION

The purpose of this paper is to provide a general overview of the main actors and structure of an initial public offering (“**IPO**”) of a flow-through limited partnership (“**FTLP**”) established under the laws of the Province of Ontario. In addition this paper discusses the role of the agents in the IPO process, an FTLP’s continuous disclosure obligations following closing and the regulation of investment fund managers (*i.e.*, the general partner of an FTLP).

FTLPs are important investment vehicles for Canadians who invested over \$390 million dollars in FTLPs between January 1, 2009 and November 16, 2009. This \$390 million dollar total does not include proceeds from a number of currently active FTLP offerings that have, at a minimum, filed a preliminary prospectus, and which may close before the end of 2009. A list of the names of each FTLP, the general partner, the portfolio manager, the promoter, the month of closing and either (i) the gross aggregate proceeds raised year-to-date in 2009 or (ii) the minimum offering condition for closing, is set forth at “**Schedule “A”**” attached hereto.²

In 2008, Canadians invested over \$910 million dollars in FTLPs. In 2007, Canadians invested over \$1.4 billion dollars.² FTLPs have, along with many other investment vehicles, experienced a sharp decline due to the current global economic conditions.

MAIN ACTORS IN AN FTLP

The main actors in an FTLP are the general partner, the FTLP itself, the portfolio manager and of course the limited partners. Other actors include an independent review committee, a custodian, auditors, legal counsel to the FTLP and the general partner, a registrar and transfer agent, consultants in certain circumstances (such as a mining and/or an oil and gas consultant if the portfolio manager does not have such expertise) and an administrator (*i.e.*, if certain management functions are not performed by the

¹ **Disclaimer:** *The material contained in this paper is for educational purposes only. It deals with technical matters that have broad application and may not be applicable to a particular set of circumstances and facts. As well, the material and references contained herein reflect laws and practices that are subject to change. For these reasons, this paper should not be relied upon as a substitute for professional advice in connection with any particular matter. The authors of this paper accept no legal responsibility for its contents or for any consequences arising from its use. The views of the authors in this paper are those of the authors and not those of Cassels Brock & Blackwell LLP.*

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general partner). In an IPO there are also agents (*i.e.*, investment dealers) involved and their legal counsel. Each of these actors is briefly described below.

General Partner

If an FTLP is an Ontario limited partnership, the general partner of the FTLP is typically a corporation incorporated under the laws of the Province of Ontario. Unless the general partner is subject to an agreement with an investment fund manager, the general partner is the investment fund manager of an FTLP and is generally involved with the organization and management of the FTLP. The general partner, on behalf of a FTLP, contracts with other actors (*e.g.*, the portfolio manager) for services it requires. If the general partner manages the day-to-day affairs of an FTLP, it is required to be registered as an investment fund manager in the Province of Ontario. See “*Registration of Investment Fund Managers*” at **Schedule “C”** attached hereto for the registration requirements of an investment fund manager under Canadian securities law.

FTLP

An FTLP must have a general partner before it is created. In order to create the limited partnership, an initial limited partner and general partner enter into a limited partnership agreement or “**LPA**”. The initial limited partner (*e.g.*, a person or company related to a promoter of the FTLP) typically invests a nominal amount of money (*e.g.*, \$10) and acquires an initial limited partnership unit or units of an FTLP. The initial limited partnership units are generally redeemed on or immediately after the initial closing of the FTLP’s IPO and the nominal investment is returned to the initial limited partner.

A declaration is also filed with the Ontario Ministry of Governmental Services in the case of an Ontario FTLP which legally forms the entity under the *Limited Partnership Act* (Ontario). Prior to the closing of an FTLP offering, each of the general partner and FTLP must be registered under the applicable extra-provincial legislation in each of the offering jurisdictions, with this often being a condition of closing.

The primary constating document of an FTLP is the LPA. The LPA and applicable limited partnership legislation of the offering jurisdictions govern the rights of the limited partners of an FTLP. The LPA is sometimes attached to the prospectus (but usually not) and if not attached to the prospectus, it is filed as a material contract on SEDAR at the time the FTLP’s final prospectus is filed. See also “*Select Features of an FTLP Offering – Limited Partnership Agreement*”.

Portfolio Manager

An FTLP generally receives investment advice from a portfolio manager in connection with the selection of securities of various Resource Issuers (defined below) forming part of an FTLP’s investment portfolio. A portfolio manager must be registered as an advisor under applicable securities legislation in order to provide investment advice to an FTLP. In the Province of Ontario, a portfolio manager must be registered as a “portfolio manager” with the Ontario Securities Commission (the “**OSC**”), the jurisdiction where the FTLP is established. One can easily confirm such registration by a review of the list of registrants on the OSC’s web site.

The main agreement between the FTLP and the portfolio manager is the portfolio management agreement which is filed on SEDAR at the time the FTLP’s final prospectus is filed.

Limited Partners

The investors in an FTLP are the limited partners. Certain jurisdictions, such as Alberta and Manitoba, require an FTLP to file a list of its limited partners within a prescribed period of time following each closing or change in the status of limited partners of an FTLP. Typically, the agency agreement between the FTLP and the agents imposes a covenant for the agents to provide this information to the

FTLP within a specified number of days after the last closing of any offering of limited partnership units such that the FTLTP can ensure it is in accordance with applicable legislation governing limited partnerships

Independent Review Committee

FTLPs must have an independent review committee (“**IRC**”) to deal with conflict of interest matters as required by National Instrument 81-107 – *Independent Review Committees for Investment Funds* (“**NI 81-107**”). NI 81-107 requires all publicly offered investment funds, such as an FTLTP, to establish an IRC to whom the general partner must refer all conflict of interest matters for review or approval.

NI 81-107 also imposes obligations upon the general partner to establish written policies and procedures for dealing with conflict of interest matters, maintain records in respect of these matters and provide assistance to the IRC in carrying out its functions. An FTLTP must comply with such requirements and all other requirements as set forth in NI 81-107. The IRC is required to be comprised of a minimum of three independent members and is required to conduct regular assessments and provide reports to the general partner and to the limited partners in respect of its functions.

A new FTLTP must identify the initial members of its IRC in its prospectus. Each member must be “independent” as that term is defined under NI 81-107 as of the date of the prospectus. The FTLTP is responsible for paying the fees and expenses of the IRC which relate to the FTLTP. Typically, the IRC is involved in considering the rollover transaction when a rollover involves a related party mutual fund of the FTLTP’s general partner. For more information on the rollover transaction, which occurs when an FTLTP’s limited partnership units are exchanged for units in a mutual fund, see “*Rollover Transaction and Liquidity Alternative*”.

Custodian

An FTLTP typically appoints a custodian to hold its portfolio securities. The general partner of an FTLTP may act as the custodian, however, in such circumstances, its fees for performing such a function are typically included in the fees payable by the FTLTP to the general partner.

Auditors

The financial statements included in a prospectus for an FTLTP offering must include financial statements of the FTLTP and in some cases also includes the financial statements of the general partner. These financial statements are audited, usually as of a date on or before the filing of the FTLTP’s final prospectus. The financial statements generally consist of a balance sheet and notes to the financial statements of the FTLTP (and if applicable, the general partner).

Legal Counsel to the FTLTP and General Partner

An FTLTP and the general partner each have legal counsel, which is usually the same law firm. Legal counsel plays a pivotal role in working with the general partner and promoter of the FTLTP in preparing and filing the preliminary and final prospectus, drafting and negotiating the material agreements and preparing all other required deal documents.

Registrar and Transfer Agent

Typically FTLTPs retain an external registrar and transfer agent, a function that may also be provided by the general partner.

Consultants

In certain circumstances where a portfolio manager wants to rely on specific oil and gas and/or mining industry expertise, it may retain the services of mining and/or oil and gas consultants. Although this is not common, it may occur in circumstances where, for example, a new portfolio manager in the FTLP industry is willing to split fees with a consultant who will provide the portfolio manager with additional expertise in order to establish the portfolio manager as a new entrant in the FTLP industry. Such circumstances are rare since a portfolio manager's fees would be reduced to pay any mining and/or oil and gas consultants.

Administrator

In certain circumstances, the general partner may want to retain an administrator to provide some or all of the management services that are ordinarily provided by the general partner of an FTLP. If an administrator provides the management functions of the general partner, it has to be registered as an investment fund manager under securities legislation. See "*Registration of Investment Fund Managers*" at **Schedule "C"** attached hereto.

Agents

Agents involved in an FTLP IPO are often investment dealers that form part of a syndicate and who earn a commission. For more information about the agents, see "*The Agents and their Role in the FTLP IPO Process*". The definitive agreement entered into between the FTLP and the agents is the agency agreement which is filed on SEDAR at the time the FTLP's final prospectus is filed.

Agents' Legal Counsel

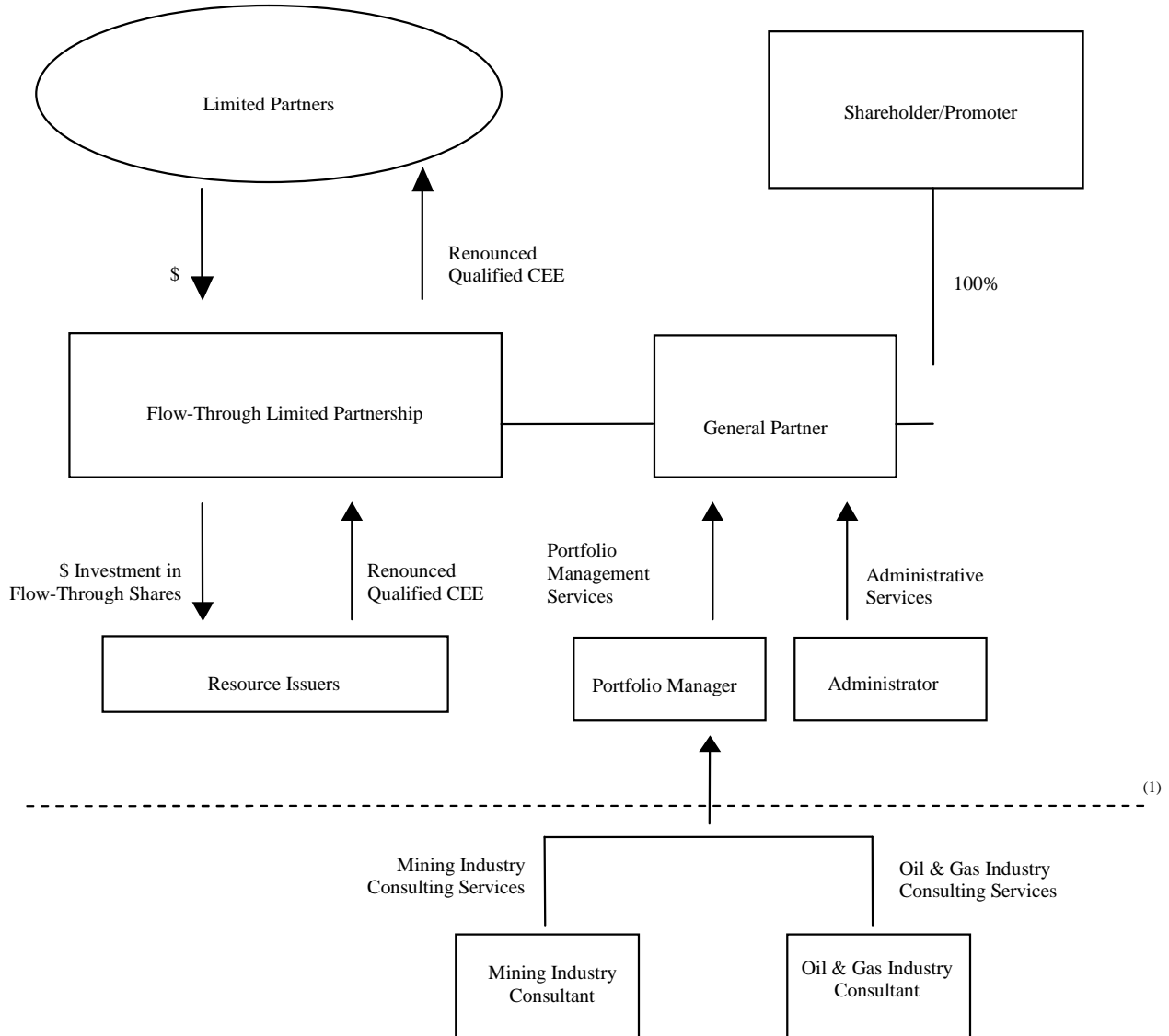
The agents retain their own legal counsel to work closely with counsel to the FTLP and the general partner in any public offering of securities.

Diagram of an FTLP Structure and the Main Actors

The investment structure of an FTLP and the relationship among the FTLP, the general partner, the administrator, the promoter, the portfolio manager, the consultants, the investors (*i.e.*, limited partners) and the Resource Issuers is illustrated in the diagram on the next page.

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Generic Structure of an FTLP



Note:

⁽¹⁾ The dotted line has been added since typically a portfolio manager has the requisite oil and gas and/or mining expertise and consultants are not required. Consultants may be used to provide advice to the portfolio manager to demonstrate the FTLP's overall expertise in circumstances for example where it is a new promoter of FTLP funds.

SELECT FEATURES OF AN FTLP OFFERING

Investment Objectives

An FTLP is a tax-driven investment fund whose investment objectives are to typically invest in “**Flow-Through Shares**”³ of “**Resource Issuers**”⁴ engaged in oil and gas and/or mineral exploration in Canada with a view to the preservation of capital and achieving capital appreciation.

In addition to investments in Flow-Through Shares, at least one FTLP (*i.e.*, Front Street) currently has the ability to invest in qualifying environmental trusts (“**QETs**”). FTLPs can invest in limited partnerships (“**QET Partnerships**”) that will participate financially in the gross production or production revenue (each a “**Production Interest**”) generated from mining and oil sands properties (each a “**QET Property**”) of various resource companies that meet certain criteria (each a “**Resource Company**”) and that will make contributions to qualifying environmental trusts to secure reclamation obligations of Resource Companies.

There is currently a very limited market for QET Partnership units since a very limited number of QET Partnerships have been created. Accordingly, this paper will not go into great detail about QETs and when discussing FTLP objectives and strategies will limit the discussion to Flow-Through Shares of Resource Issuers.

As background information, QETs are associated with the reclamation obligations of Resource Companies which are enforced by various levels of government and law to correct disturbances by non-renewable resource (fossil fuels, minerals, aggregates) extraction and processing and are designed to

³ A “**Flow-Through Share**” means a common share, or a right to acquire a common share in the capital stock of a Resource Issuer which is a “flow-through share” as defined in subsection 66(15) of the Tax Act and not a prescribed share or a prescribed right, as the case may be, for the purposes of Section 6202.1 of the Regulations in respect of which the Resource Issuer agrees to renounce Qualified CEE to the Partnership.

“**Tax Act**” means the *Income Tax Act* (Canada), and the regulations thereunder, as may be amended or replaced from time to time.

“**Qualified CEE**” means CEE, other than expenses which constitute Canadian exploration and development overhead expenses as prescribed by Regulation 1206 and expenses which are specified seismic data expenses as described in paragraph 66(12.6)(b.1) of the Tax Act, that may be renounced as CEE to the Partnership.

“**CEE**” means “**Canadian exploration expense**” as defined in subsection 66.1(6) of the Tax Act, which includes: (a) certain expenses incurred for the purpose of determining the existence, location, extent or quality of an accumulation of petroleum or natural gas or a mineral resource in Canada; (b) certain expenses incurred for the purpose of bringing a natural accumulation of petroleum or natural gas or a new mine in a mineral resource in Canada into production in reasonable commercial quantities and incurred before the coming into production of the new mine; and (c) CRCE.

“**CRCE**” means a Canadian renewable and conservation expense s defined in subsection 66.1(6) of the Tax Act.

⁴ “**Resource Issuer**” means (i) a corporation that is a “principal-business corporation” as defined in subsection 66(15) of the Tax Act or (ii) a partnership or other entity that (a) carries on as its principal business the business of oil and gas exploration and development, mining exploration and development, generation of energy through alternative means or the development of projects for alternative energy generation or (b) invests in equity securities of any such entity;

ensure sustainable establishment and utilization of renewable resources on sites where excavation or other disturbances have occurred. Reclamation of mines and oil and gas sites may profitably utilize the void space for burial of solid wastes while restoring the land surfaces to their original utility. Reclamation obligations in respect of a mine site are generally of two types. The first type is readily quantifiable and consists of dismantling structures, restoring tailings ponds and other land surfaces and neutralization of toxic substances. This work is, to some extent, an ongoing function as mining operations progress and, to the greatest extent, undertaken when production ceases. The second type is difficult to quantify and generally involves the long term requirement for water treatment. Resource Companies are, under the laws of most jurisdictions, required to set aside amounts and/or post security for some or all of their reclamation obligations, which security can take the form of cash, a bond, letters of guarantee, securities or other tangible security.

FTLPs can invest in QET Partnerships that will enter into joint venture agreements with Resource Companies to acquire a Production Interest and to secure the reclamation obligations of Resource Companies by contributing funds to a QET. The amounts contributed to a QET would constitute all or a portion of the security required by the governmental authority and the Resource Company will retain the overall reclamation obligation for a particular QET Property.

Investment Strategy

An FTLP's investment strategy is generally to invest its available funds so limited partners will be entitled to claim certain deductions from income and in certain circumstances be entitled to provincial non-refundable investment tax credits for income tax purposes for the taxation year in which the FTLP files its prospectus.

Generally, the portfolio manager will manage the FTLP's investment portfolio with a view to: (a) the preservation of capital; and (b) capital appreciation of the FTLP's investments. The FTLP's investment strategy often involves investing in Flow-Through Shares of Resource Issuers engaged in oil and gas or mining exploration, development or production or energy production that will incur CEE including CRCE and that (i) have experienced management, (ii) have a strong exploration program in place, (iii) may require time to mature, and (iv) offer potential for future growth.

"Flow-Through Shares" (as previously defined) are common shares or rights to acquire common shares purchased from the treasury of a Resource Issuer under an agreement which provides that, in addition to issuing common shares, the Resource Issuer agrees to incur and renounce Qualified CEE to the FTLP in an amount equal to the subscription price of the Flow-Through Shares. Flow-Through Shares are typically purchased at a premium to the market price of the Resource Issuer's common shares as compensation for the benefit of tax deductions. They are usually subject to resale restrictions since they are typically issued on a private placement basis. Flow-Through Shares are an attractive means of financing Canadian exploration expenditures for Resource Issuers who have significant tax deductions available to them.

The FTLP will use its available funds to subscribe for Flow-Through Shares pursuant to flow-through agreements to be entered into with Resource Issuers. Under the terms of a flow-through agreement, the FTLP will subscribe for Flow-Through Shares of a Resource Issuer issued from treasury and the Resource Issuer will incur and renounce to the Partnership, in an amount equal to the subscription price of the Flow-Through Shares, expenditures in respect of resource exploration which qualify as Qualified CEE and which may be renounced to the FTLP. Investments made by the portfolio manager on behalf of the FTLP will be consistent with the FTLP's investment restrictions and guidelines discussed below.

The portfolio manager typically uses a disciplined process to select Flow-Through Shares, with an emphasis on quantitative factors such as projected cash flow and earnings, net value of resources and reserves, and the expected return on new projects. The portfolio manager also considers qualitative

factors, in particular, management and its expertise in exploration and production and its financial capabilities. Further, the portfolio manager will give consideration to the premium over the current market price that must be paid to acquire Flow-Through Shares to ensure any purchases are aligned with the FTLP's investment objectives and investment restrictions and guidelines.

The portfolio manager manages the FTLP's investment portfolio so as to achieve the FTLP's investment objectives, including after the initial investment period. If the portfolio manager is of the opinion that it is in the best interests of the FTLP to do so, this may involve the disposition of Flow-Through Shares and other investments held by the FTLP and the reinvestment of the net proceeds from any such dispositions (after consideration being given to applicable distributions to partners) in securities of Resource Issuers or use the proceeds to exercise any warrants or invested in High-Quality Liquid Investments⁵.

Investment Restrictions and Guidelines

The investment restrictions and guidelines of an FTLP describe permitted and non-permitted investments of the investment fund. Investment restrictions and guidelines include, but are not limited to such things as, minimum market capitalization requirements, diversification requirements, minimum acquisition amounts of securities of public companies and maximum acquisition amounts of securities of private companies to list but a few. An example of the investment restrictions and guidelines of an FTLP is set forth at **Schedule "B"** attached hereto.

Prior Partnerships

An FTLP prospectus will often contain a section entitled prior partnerships. This section illustrates the past performance history of a family of FTLP funds that are promoted by a common promoter and/or affiliated general partner and/or common portfolio manager and typically includes information such as after-tax total returns and after-tax annualized returns.

This is an important section for retail brokers and their investors/clients who want to know how well a family of FTLP funds has performed in the past. This section usually includes the name of prior FTLPs, the aggregate amount of gross proceeds raised, the net asset value per limited partnership unit as at a date that is close to the date of the prospectus (except for prior partnerships that have completed a rollover and are dissolved, then it is at the rollover date), after-tax total return and after-tax annualized return.

The past performance of prior FTLPs clearly indicates whether prior FTLPs promoted by a family of FTLP funds have achieved their respective investment objectives of capital preservation and appreciation.

⁵ **"High-Quality Liquid Investments"** means, generally, high-quality money market instruments which are accorded the rating category of A-1 by Standard & Poor's, a division of The McGraw-Hill Companies, or R-1 by Dominion Bond Rating Service, interest bearing accounts of Canadian chartered banks or Canadian trust companies with assets in excess of \$15 billion or securities issued or guaranteed by the Government of Canada or by the government of any province of Canada or agency thereof or preferred shares with a remaining term of three years or less and having a rating of P-1 (high) (Standard & Poor's, a division of The McGraw-Hill Companies) or PFD-1 (Dominion Bond Rating Service).

Portfolio Valuation

An important part of an FTLP prospectus includes a description of how the net asset value (“NAV”) of the FTLP is calculated. An FTLP prospectus typically sets forth various valuation principles involving securities of publicly traded companies, private companies and other holdings. The details involving portfolio valuation is outside the scope of this paper, however, the authors note that counsel should often ensure that the party who is calculating the NAV of an FTLP has reviewed and is satisfied with the valuation principles as disclosed in the prospectus and as set forth in the LPA.

Loan Facility

In order to enhance returns, some FTLPs enter into a loan facility with a lender such as a Schedule I Canadian chartered bank (the “**Lender**”) on or before the closing date of an IPO. A loan facility permits an FTLP to borrow an amount which will be used to finance the agents’ fee, the expenses of the IPO and ongoing fees and expenses of the FTLP, in order to maximize the allocation of the gross proceeds of the IPO towards the purchase of Flow-Through Shares. The interest rates, fees and expenses under a loan facility are typical of credit facilities of this nature and generally a Lender will require an FTLP to provide a security interest in the assets held by the FTLP in favour of the Lender to secure such borrowings. Often a Lender will want to make sure it has a relatively liquid portfolio and may influence the investment restrictions and guidelines of an FTLP. For example, it may limit the amount of Flow-Through Shares of private companies that can be acquired by an FTLP to a maximum amount such as 5%.

Often, an FTLP will have two sets of counsel when a loan facility is involved: securities lawyers in connection with the IPO and lending lawyers in connection with the loan facility; typically both are members of the same law firm.

Other than the borrowing by the FTLP under the loan facility, an FTLP is generally not permitted to engage in any other borrowings. Prior to the dissolution of an FTLP all amounts outstanding under a loan facility, including all interest accrued, is repaid in full.

Rollover Transaction and Other Liquidity Alternative

(a) Rollover Transaction

Limited partnership units of an FTLP (“**Units**”) are not publicly traded on a stock exchange and are not liquid investments. In order to provide liquidity, an FTLP only exists for a few years (often less than two years) until the occurrence of a liquidity event. Such an event is disclosed in the FTLP’s prospectus.

A liquidity event or “**rollover**” generally involves the transfer of all of the assets (excluding cash) of an FTLP (*i.e.*, the Flow-Through Shares of Resource Issues held by the FTLP) to a mutual fund corporation in exchange for a class/series of shares of the mutual fund corporation. A class/series of shares of a mutual fund corporation are each a separate mutual fund. The rollover typically involves a resource mutual fund. A mutual fund corporation is usually involved since it provides limited partners, upon receipt of a class/series of shares of a mutual fund corporation (the “**Mutual Fund Shares**”), with enhanced liquidity through their ability to have the Mutual Fund Shares redeemed or to switch to another class/series of shares (each a separate mutual fund) of the mutual fund corporation. The Mutual Fund Shares are redeemable by the holders thereof at the NAV per Mutual Fund Share on any business day, subject to the constating document of the mutual fund and applicable securities laws.

The liquidity event is called a “rollover” since it is intended to be a tax-free rollover or exchange for assets (other than cash) of the FTLP for shares of a mutual fund corporation. Appropriate elections under applicable income tax legislation must be made so that the transfer will occur on a tax-deferred, “rollover” basis and will not result in any tax consequence to the limited partners of an FTLP.

An FTLP will only transfer its assets to the mutual fund corporation if: (a) the mutual fund corporation's acquisition of such assets would be consistent with the mutual fund's investment objectives; and (b) the mutual fund corporation continues to qualify as a mutual fund corporation under the Tax Act and otherwise in accordance with the terms and conditions of the transfer agreement between the FTLP and mutual fund corporation (the "**Transfer Agreement**"). If necessary, a mutual fund corporation will apply to the relevant securities or regulatory authorities to be exempted, for a period of 180 days following the date of transfer of the assets of the FTLP to the mutual fund corporation, from certain investment restrictions under National Instrument 81-102 – *Mutual Funds*. An FTLP will only transfer assets to the mutual fund corporation if the transfer would not result in the mutual fund contravening any investment restrictions under applicable securities laws for which an exemption has not been granted.

On the completion of such transfer, an FTLP will receive Mutual Fund Shares having the same aggregate NAV as the aggregate NAV of the FTLP determined on the same basis as the NAV of the Mutual Fund Shares. Within 60 days following the date of the rollover, the FTLP will be wound-up and upon winding-up, the limited partners and the general partner will receive their *pro rata* interest in the Mutual Fund Shares held by it on a tax-deferred, rollover basis together with any cash remaining in the FTLP. If the FTLP has assets in respect of which elections cannot be made relating to the transfer of such assets to the mutual fund corporation, the LPA provides that such assets will be distributed, before the transfer of all other FTLP assets to the mutual fund corporation as to 99.99% to the limited partners and as to 0.01% to the general partner and will be held by the general partner as agent on behalf of the limited partners.

(b) *Other Liquidity Alternative*

If it is not possible to complete the rollover transaction pursuant to the terms and conditions of the Transfer Agreement, the prospectus and LPA generally states that the general partner may propose to the limited partners at a special meeting of limited partners to be held no later than a dissolution date (as stated in the prospectus and LPA) (the "**Dissolution Date**"), an alternative to the liquidation of the FTLP's assets (a "**Liquidity Alternative**"). Unless extended by an "**Extraordinary Resolution**"⁶ of the limited partners or dissolved earlier in accordance with either a rollover transaction, Liquidity Alternative or the LPA, the general partner must liquidate the FTLP's assets prior to the Dissolution Date and distribute the net proceeds arising from such liquidation on or before the Dissolution Date, after payment or provision for the debts and obligations of the Partnership, as to 99.99% to limited partners and as to 0.01% to the general partner.

(c) *Prospectus Disclosure*

In a prospectus, one will usually find disclosure about not only the rollover transaction and the Liquidity Alternative but also information about the Mutual Fund Shares and mutual fund corporation and a cross-reference to the current prospectus of the mutual fund corporation. This type of disclosure is provided when it is contemplated that a rollover transaction will occur between an FTLP and mutual fund

⁶ "**Extraordinary Resolution**" means a resolution passed by 66 2/3% or more of the votes cast at a duly constituted meeting, or an adjournment thereof, of the limited partners called for the purpose of considering such resolution, or, alternatively, a written resolution signed in one or more counterparts by limited partners holding 66 2/3% or more of the Units outstanding entitled to vote on such resolution at a meeting.

corporation. Some FTLF structures even prepare the form of Transfer Agreement and post it on SEDAR for greater certainty.

In some circumstances, a particular rollover transaction to a specific mutual fund is not known other than in general terms, therefore, there is no prospectus disclosure in connection with any particular mutual fund. In such circumstances, an FTLF must hold a special meeting of limited partners to approve a particular liquidity event, including a rollover transaction, after a mutual fund is identified. This requires an FTLF to prepare meeting materials, including: (a) a management information circular; (b) a notice of meeting; and (c) a form of proxy. This process is more costly for an FTLF than providing for a rollover transaction as contemplated and disclosed in a prospectus.

No Stock Exchange Listing

There is no stock exchange listing for an FTLF because it is a tax-driven investment vehicle that exists for only a short period of time before being wound-up and dissolved following a liquidity event, such as a rollover transaction. Limited partners largely invest in an FTLF for the tax benefits and do not need any immediate liquidity. However, limited partners expect liquidity through a liquidity event, such as a rollover transaction, and upon receipt of Mutual Fund Shares in the event thereof, investors (formerly limited partners) then have the ability to redeem such Mutual Fund Shares upon demand in accordance with the articles of the mutual fund corporation and applicable securities laws.

It is not unusual that promoters of an FTLF will time a liquidity event, such as a rollover transaction, at the same time as its next FTLF IPO. Immediately following a rollover transaction, investors are encouraged to redeem their Mutual Fund Shares and invest the proceeds in the promoters' next FTLF IPO. This is often how successful FTLF promoters raise additional funds; funds from new investors but also funds from previous investors or limited partners in prior partnerships who want to continue to obtain another tax benefit rather than remain invested in a mutual fund, which was typically only set up for liquidity purposes.

Roman Number I and II FTLF Offerings

Typically, there are few FTLF IPOs during the summer months, largely because investors and investment dealers are away for the summer. Private offerings of FTLFs take place throughout the year, including the summer, and are outside the scope of this paper.

In August or September of each year you will see a number of preliminary prospectuses filed on SEDAR by various promoters of FTLF IPOs. Many FTLF promoters undertake a spring offering and a fall offering. One will usually see the Roman numeral "I" associated with a spring offering (e.g., ABC 2009-I Flow-Through Limited Partnership) and the Roman numeral "II" with a fall offering (e.g., ABC 2009-II Flow-Through Limited Partnership).

An FTLF will not ordinarily have a December closing since there must be sufficient time between the closing of an FTLF offering and December 31 – the deadline when all available funds from an FTLF offering must be invested. If not, any uninvested available funds must be returned to investors, usually no later than January 31 of the next year and generally without interest or deduction. Timing is a matter to be negotiated between the general partner of an FTLF and the lead agent of a syndicate of investment dealers. Both parties must balance the likelihood and ability of an FTLF investing all its available funds before the December 31 deadline of a given year.

It is possible to have a closing in mid-December and have all available funds invested before December 31. However, the ability to invest all available funds in such a short time frame is always a concern and, while the authors are not aware of any case where all available funds raised pursuant to an IPO were not invested before December 31 of a given year and a return of uninvested available funds to investors was required, there have been issues with portfolio managers making what might be considered

inappropriately priced investments in order to complete the investments on schedule. If a refund were to take place, arguably it would not bode well for the promoters of said offering in connection with future FTLP IPOs.

As discussed above, since an FTLP must invest all its available funds before December 31 of a given year, you will often find many transactions occurring just before and during the holiday season in December of a given year. These are often private placements between FTLPs and Resource Issuers in connection with the purchase and sale of Flow-Through Shares by an FTLP from a Resource Issuer. Such Flow-Through Shares are usually subject to a four month hold period.

Limited Partnership Agreement

As discussed earlier, the constating document of an FTLP is the LPA. The prospectus includes a summary of the LPA. A summary of the LPA is outside the scope of this paper; however, one can easily review such a summary by reviewing the prospectus of any FTLP. LPAs are generally quite similar so a review of one FTLP LPA is often typical of others. An LPA is a material contract which is filed separately on SEDAR at the time the final prospectus is filed. In past years, the LPA was required to be attached to the FTLP prospectus (although some FTLP issuers received exemptive relief from this requirement), however this requirement was removed with the introduction of National Instrument 41-101 – *General Prospectus Requirements* (“**NI 41-101**”) in March 2008. Notwithstanding the introduction of NI 41-101 and despite the added printing costs, some FTLP issuers still attach the LPA to the prospectus so it is readily available to investors in addition to its summary in the prospectus.

Canadian Taxation Considerations

(a) General

FTLP offerings are popular with individual investors taxed at the highest marginal tax rate because their high tax rate ensures such investors the best possible return from their Flow-Through Share investment.

The Tax Act allows Resource Issuers engaged in certain exploration or development work (such as mining, oil and gas projects, as well as alternative energy projects, such as wind power) to renounce certain expenses (called “**Canadian Exploration Expenses**”, or “**CEE**”) related to that exploration or development work to shareholders. “**Flow-Through Shares**” are shares in these Resource Issuers where renounced expenses may be flowed through to the shareholder pursuant to a flow-through share agreement between the shareholder (*i.e.*, the FTLP) and the Resource Issuer. The amount of expenses that a Resource Issuer can flow through to a shareholder is limited to the amount contributed by that shareholder for the Flow-Through Share.

Although investors in FTLP offerings do not hold Flow-Through Shares themselves, they participate in the benefits of the Flow-Through Shares by being partners in an FTLP that holds the Flow-Through Shares. Under the Tax Act, an FTLP may allocate CEE it incurs or is deemed to incur to the partners in accordance with the LPA. Limited partners to whom CEE is allocated are deemed to have incurred that CEE themselves and can deduct it when computing their income under the Tax Act – hence the term “flow-through”.

When CEE is allocated to a limited partner, the adjusted cost base (“**ACB**”) of a limited partner’s Unit is reduced accordingly. Because the amount of CEE allocated to each limited partner often approximates to the amount paid by the limited partner for his, her or its Unit (*i.e.*, his, her or its investment), the ACB of the limited partner’s Unit will generally be *nil*. This means that any disposition of the Unit will result in a capital gain to the limited partner equal to the amount of the sale price of the Unit.

An FTLP often includes a liquidity mechanism whereby the FTLP transfers all its assets (consisting mainly of Flow-Through Shares) to a mutual fund corporation in exchange for shares of the mutual fund corporation at the end of the term of the FTLP. The FTLP would then be terminated and the shares of the mutual fund corporation distributed to the limited partners on a tax-deferred basis. All of these steps are intended to be done on a tax deferred basis resulting in the former limited partners holding redeemable shares of the mutual fund corporation which would generally have a nominal ACB to the holder.

The following table illustrates the potential tax advantages to an investor resident in the Province of Ontario who invests \$1,000 in an FTLP which invests in Flow-Through Shares. In the example, an investment of \$1,000 would generate \$1,000 worth of CEE deductions for the investor. This table ignores any federal investment tax credits⁷ that could be available to an investor (discussed below).

Break-even Calculation		
Investment	\$1,000	- amount of money invested which results in \$1,000 in CEE expenses flowed-through to the limited partner
Subtract tax savings of:	\$(460)	- \$1,000 in CEE flowed-through to the limited partner is deducted against the limited partner's other income producing tax savings of \$460 (\$1,000 x highest marginal tax rate of 46% in the Province of Ontario)
Money at risk	\$540	- after having the benefit of the tax savings described above, this is the amount that a Limited Partner stands to lose if all the Flow-Through Shares owned by the FTLP prove worthless
Break-even proceeds of disposition:	\$701	- to get their money at risk back and walk away without a gain or loss on their investment, a limited partner would have to sell their Unit for \$701. Selling at this amount would mean a limited partner would have to pay capital gains tax of approximately \$161 (23% x 701), leaving the limited partner with \$540 after-tax dollars (because the Units are often exchanged for Mutual Fund Shares, it is more likely that the Mutual Fund Shares would be sold, meaning this break-even price would apply to the sale of the Mutual Fund Shares after the rollover transaction)

(b) Flow-Through Mining Expenditure Tax Credit

As a further incentive to mining exploration in Canada, the Tax Act offers, in addition to CEE deductions, an investment tax credit for certain mining expenditures. Thus in addition to the benefits obtained on the flow-through of CEE to investors, investors may be entitled to claim an additional tax credit that will reduce their federal taxes payable by 15% of the CEE that relates to certain mining exploration. The investment tax credit is limited to mining exploration activities and is not available for other forms of CEE, such as oil and gas exploration or alternative energy production.

⁷ Certain provinces also offer additional tax credits for exploration carried out in that province and where the limited partner is resident in that province.

Although the flow-through mining expenditure tax credit produces a 15% reduction in taxes in the year the investor is deemed to incur the CEE, generally speaking the amount of the credit must be included in the income of the investor in the following year. Assuming a marginal tax rate of 46% and ignoring the time value of money, the tax credit is generally worth only about 8% in tax savings to the investor after the amount of the credit is added back into income.

Fees and Expenses Payable by an FTLP

(a) Initial Expenses

The initial expenses of an FTLP offering are paid by the FTLP. If the FTLP has obtained a loan facility the initial expenses are paid with funds borrowed under the loan facility. These initial expenses include such things as the costs of creating and organizing the FTLP, the costs of printing and preparing the prospectus, legal and audit and accounting expenses of the FTLP, marketing expenses and other reasonable out-of-pocket expenses incurred by the lead agent and other incidental expenses and are usually between \$300,000 to \$800,000 depending on the minimum and maximum size of the offering.

(b) Management Fee

An FTLP typically pays a management fee to the general partner, administrator or other entity responsible for the management and operation of the FTLP. The fee is typically 1% of the NAV, plus applicable taxes and is usually calculated and paid monthly in arrears based on the NAV at the end of the preceding month.

(c) Incentive Bonus

In addition to the management fees described above, a general partner or portfolio manager is often entitled to an Incentive Bonus payable by the Partnership. An “**Incentive Bonus**” is an amount which is calculated on the earlier of the dissolution date of the FTLP or the business day prior to the implementation of a rollover transaction or Liquidity Alternative, in respect of each Unit then outstanding equal to (i) 20% of the amount, if any, by which the NAV per Unit on the dissolution date and any distributions per Unit paid during the period commencing on the date of the initial closing and ending on the dissolution date exceeds \$28.00 per Unit (assuming limited partnership units are issued at \$25), multiplied by (ii) the number of Units outstanding at the dissolution date.

(d) Portfolio Manager's Fee

The Portfolio Manager is typically entitled to an annual fee of 1% of the NAV calculated and paid monthly in arrears and paid by the FTLP.

(e) Operating Expenses

The FTLP will pay for all expenses incurred in connection with the operation and administration of the FTLP. These expenses generally include, without limitation: (a) mailing and printing expenses for periodic reports to limited partners and for meeting materials prepared in connection with any Liquidity Alternative proposed to limited partners; (b) fees payable to the auditors, legal and other professional advisors of the FTLP; (c) taxes and ongoing regulatory filing fees; (d) any reasonable out-of-pocket expenses incurred by the general partner or its agents in connection with their ongoing obligations to the FTLP; (e) expenses relating to portfolio transactions (including investment management fees); (f) fees and the reimbursement of expenses of members of the IRC; and (g) any expenditures which may be incurred in connection with the dissolution of the FTLP and the exchange of assets of the FTLP for Mutual Fund Shares. Such costs are usually paid by the FTLP from the proceeds of the loan facility, if obtained. However, the general partner is also authorized to fund fees and expenses in excess of the amount reserved through the sale of Flow-Through Shares and other securities held by the FTLP.

Although a general partner may act as custodian of the investments of the FTLP, typically such function is undertaken by a third party custodian. A general partner may also act as the registrar and transfer agent for the FTLP. If the general partner performs these functions, no additional fee will be payable to the general partner by the FTLP for these services; however, the general partner is usually entitled to reimbursement for reasonable out-of-pocket expenses related to its performances of these services. In the event that the general partner has determined to appoint a custodian and registrar and transfer agent for the FTLP, such fees and expenses of such appointees will be borne by the FTLP.

Subscription Procedures

(a) General

A retail broker may contact his or her client or vice versa about a particular FTLP offering and indicate the number of Units he, she or it desires to purchase, subject to a minimum individual subscription amount as described in the prospectus and LPA. The investor pays the amount due either by direct debit from the investor's brokerage account or by cheque made payable to the investor's agent or such other registered dealers or brokers as are authorized by the agents. Fractional Units are generally not issued.

(b) Offering and Acceptance Mechanic

In an FTLP IPO there is no subscription agreement signed by an investor as with a private placement. FTLP offerings state in the prospectus that delivery of the prospectus constitutes an offer and evidences a subscription between the investor and FTLP in accordance with the prospectus and LPA effective upon the acceptance, in whole or in part, by the general partner of the subscription agreement.

(c) Subscription Terms

Pursuant to the subscription agreement so constituted, an investor/limited partner, among other things:

- (i) irrevocably nominates, constitutes and appoints the general partner as his, her or its true and lawful attorney with the full power and authority as set out in the LPA, including the power and authority to execute the LPA on his, her or its behalf;
- (ii) acknowledges and agrees that he, she or it is bound by the terms of the LPA and is liable for all obligations of a limited partner thereunder;
- (iii) makes the representations and warranties set out in the LPA, including without limitation the following:
 - (A) the investor is not a "non-resident" of Canada for the purposes of the Tax Act;
 - (B) the investor is not a "non-Canadian" within the meaning of the Investment Canada Act;
 - (C) the investor is not a financial institution for the purposes of the Tax Act; and
 - (D) the investor has not financed the acquisition of the Units with financing for which recourse is or is deemed to be limited for the purposes of the Tax Act;

and

- (iv) consents to the disclosure of certain information to, and the collection and use by, the general partner and its service providers, including the subscriber's full name, residential address (or address for service), social insurance number (or corporate account number, as the case may be), and the name and registered representative number of the representative of the agent responsible for the subscription, and covenants to provide such information to the agents.

(d) *Book-Entry Only Unit Certificate*

Generally, Unit certificates are not issued to subscribers of an FTLP IPO. Typically, a global book-entry⁸ only certificate representing the Units is issued in registered form to CDS Clearing and Depository Services Inc. ("CDS") or its nominee. Such a Unit certificate is called a global certificate because it is for all Units purchased by subscribers in connection with the closing of an FTLP IPO. Recently, some FTLPs have moved away from having a global certificate and are registering all Units electronically with CDS. This allows the FTLP and the agents to exchange the Units and the gross proceeds of the offering through CDS facilities, thereby eliminating the need for a wire transfer through a bank and the physical delivery of a global Unit certificate to CDS. In any event, under the book-entry system, a subscriber who purchases Units receives only a customer confirmation from the agent through whom the Units are purchased.

However, there are circumstances when individual Unit certificates may be issued by an FTLP to subscribers. This is a book-based⁹ system. For example, an FTLP issuer may retain the services of what some refer to as "Private Placement Sub-Agents". These are sub-agents designated by the agents pursuant to the agency agreement between the agents and FTLP that involve an exempt market dealer or other agent entitled to act in connection with a trade in the Units under exemptions from the dealer registration requirements under applicable law in each jurisdiction in which it may act in connection with the sale of the Units.

For private placements, the FTLP can create an offering memorandum which is the offering document used by the Private Placement Sub-Agents to solicit trades. If an FTLP is utilizing the offering memorandum exemption (Section 2.9 of National Instrument 45-106 – *Prospectus and Registration Exemptions*) it will have to create what is called an "OM wrapper" which adds prescribed disclosure as required by the exemption. There will be a subscription agreement and at the closing there will be a global book-entry only certificate representing the Units issued in registered form to CDS in connection with the public offering and individual Unit certificates issued in registered form to each limited partner in connection with the related private placement with a legend that includes resale restrictions prescribed under applicable laws.

(e) *Power of Attorney*

The LPA includes an irrevocable power of attorney which authorizes the general partner on behalf of the limited partners to, among other things, execute the LPA, any amendments to the LPA and

⁸ The "**book entry**" form of ownership allows an investor to own securities without a certificate. While investors do not receive certificates, a custodian holds one or more global certificates or CDS holds all of the Units electronically without a global certificate.

⁹ The "**book-based**" form of ownership allows an investor to own securities with or without a certificate. Traditionally shares were evidenced by physical certificates registered in the name of the holder. Increasingly, the record of ownership of shares consists of an entry in an electronic record keeping system.

all instruments necessary to effect the dissolution of the FTLTP or any Liquidity Alternative as well as any elections, determinations or designations under the Tax Act or taxation legislation of any province or other jurisdiction with respect to the affairs of the FTLTP or a limited partner's interest in the FTLTP including, without limitation, elections under subsection 85(2) and 85(3) of the Tax Act and the corresponding provisions of applicable provincial and territorial legislation in respect of the dissolution of the Partnership.

The prospectus usually states that by purchasing Units, each investor acknowledges and agrees that he, she or it has given such power of attorney and will ratify any and all actions taken by the general partner pursuant to such power of attorney. The power of attorney survives certain events including the death or bankruptcy of a limited partner.¹⁰

THE AGENTS AND THEIR ROLE IN THE FTLTP IPO PROCESS¹¹

Investment Banking Relationships

An FTLTP seeking to undertake an IPO must have a lead agent or co-lead agents. Typically, a promoter of a family of FTLTP funds will use the same lead agent(s) in subsequent IPOs; however, they are known to change. Changes in lead agents are made for a number of reasons including, a lead agent's distribution capability, the success of one or more prior FTLTP IPOs and generally based on relationships between investment bankers and officers of the general partner/promoter of an FTLTP.

Engagement Letter

The lead agent or top-left agent (meaning the investment dealer whose name appears first on the top left of the agents' certificate page of a preliminary and final prospectus) is often the main actor and book runner in an FTLTP IPO. This is a coveted position among agents since, among other things, the lead agent makes the most money on any successful offering. Often there may be more than one lead agent or co-lead agents especially if bank-owned investment dealers are involved.

Investment bankers of a potential lead agent and promoters of an FTLTP have discussions about the proposed IPO and, if desirous of working with one another, enter into an engagement letter that sets forth the basic terms of the IPO.

In connection with selecting a lead agent, promoters of an FTLTP IPO are often interested in having a large bank-owned investment dealer act as the lead agent since it has a large distribution network which increases the likelihood of a successful offering.

¹⁰ A LPA typically states that the power of attorney created thereunder shall be irrevocable and shall bind the limited partner, his, her or its heirs, executors, administrators and other legal representatives and the successors and assigns of the limited partner, notwithstanding the death or bankruptcy of the limited partner. If, for any reason, this power of attorney shall not bind a limited partner, his, her or its heirs, executors, administrators and other legal representatives and successors and assigns of the limited partner, the general partner shall have the right to sell such limited partner's Units or to purchase the same on behalf of the FTLTP at fair value as determined by an independent party selected by the general partner, whose determination will be final and binding and not subject to review or appeal.

¹¹ **Acknowledgement:** *The authors would like to thank Mark Lerohl, Vice President, Investment Banking and Tim Evans, Director, Head of Managed Retail Products, Investment Banking, both of National Bank Financial Inc. for their comments and advice in preparing this section of the paper.*

Investment bankers are also selective of which FTLP issuers to act for as lead agent. The underwriting committee of an investment bank is involved in approving any deal and in so doing consider a number of factors including, but not limited to, the reputation of the promoters of an FTLP and family of funds, their competency and prior successful FTLP offerings.

After the engagement letter is signed, counsel to the FTLP assumes primary carriage of preparing the preliminary prospectus, final prospectus and all material contracts and filing matters related thereto. Counsel to the agents is selected by the lead agent and both issuer's and agents' counsel work together in the preparation of the legal documents.

Lead Agent Involvement in the FTLP Prospectus

(a) Investment Strategy and Investment Restrictions

The lead agent will generally focus on a few key areas of the prospectus which include, but are not limited to, the investment strategy (or investment guidelines) and investment restrictions of an FTLP. They are looking at it from a business and marketing perspective. For example, they are looking at the investment mix of Flow-Through Shares between (i) oil and gas and/or mining Resource Issuers and (ii) private versus publicly traded Resource Issuers.

(b) Industry Overview Section

The lead agent often assumes carriage of preparing the industry overview section, if any, of a prospectus. This section generally describes the state of the oil and gas and/or mining sectors and explains why exposure to these sectors is a good investment for a subscriber notwithstanding the tax benefits. This information must be appropriately reviewed by legal counsel for the FTLP and agents from a due diligence perspective.

Some FTLP prospectuses do not include an extensive industry overview section. This is because the general state of the oil and gas and/or mining sectors is known to retail brokers and their clients and some issuers believe there is no need for this information. From an FTLP issuers perspective this results in fewer pages to print and savings in time, money and effort that would otherwise be involved in the due diligence of this section.

However, some FTLPs or new promoters of FTLPs do include an industry overview section for marketing purposes and if, they are new to the FTLP sector, to demonstrate their knowledge of the industry but this practice varies among investment dealers and promoters. Some FTLPs and their promoters and agents want to include select graphs and charts in their green sheet involving the oil and gas and/or mining sectors and as a general rule, if something is not in the prospectus it cannot be in the green sheet. Practice varies amongst law firms but there is a legal argument that if a graph or chart is not in the prospectus but included in the green sheet then the prospectus may not contain full, true and plain disclosure. A conservative view requires green sheet disclosure to be consistent with prospectus disclosure to remove any risk of uncertainty and possible regulatory action and sanctions. This is quite relevant today since the OSC has generally requested in the past a copy of an FTLP's green sheet in their comment letters following the filing of a preliminary prospectus.

Syndication

The syndication process determines which investment dealers or agents will become part of the distribution group of Units of an FTLP IPO. These agents sign the agents' certificate page of the preliminary prospectus and final prospectus and incur potential liability for a number of things including if a prospectus does not contain full, true and plain disclosure as required by securities law. Agents that sign the prospectus are also sometimes called "co-managers". Agents that do not sign the prospectus and are not co-managers can still sell Units but form part of what is called the selling group.

Often there are many agents involved with an FTLF IPO, sometimes in excess of 15 agents. One will often see both bank-owned and independent investment banking firms as agents involving a particular FTLF IPO. Smaller dealers are often allowed to form part of a syndicate based on their sales experience selling Units of prior FTLF IPOs. This decision is made by the lead agent in consultation with the promoters of the FTLF.

Agent Compensation

Generally, an FTLF will pay the agents a commission of 6.75% of the offering price per Unit (the “**Total Commission**”) at the closing of an FTLF IPO. This amount is then split amongst the investment bankers, retail brokers and members of the selling group in such amounts and for such purposes as described below.

The apportionments described below are for illustrative purposes only and do not necessarily reflect actual practice.

Potential Breakdown	Nature of Payment	Commentary
0.80% (80 bps)	Work Fee	- this amount of the Total Commission is paid to the lead agent or shared among the lead agents. The top-left investment banker will usually receive the largest part of the work fee. Also, it is not uncommon for a lead agent(s) to share part of the work fee with other members of the syndicate who are on the second row of the agents’ certificate page of an FTLF prospectus.
4.25%	Selling Concession	- this amount represents the largest part of the Total Commission and is paid to the retail brokers of an investment dealer who actually sell Units of an FTLF.
1.00%	Performance Fee	- this amount of the Total Commission is paid to investment dealers based on sales made by their retail brokers. For example, if one investment dealer sells 20% of the deal, it will receive 20 bps of the 1% performance fee. This is truly an incentive based payment and is paid to any dealer forming part of the syndicate exclusively based on performance - even the bottom right investment dealer who signs the agents’ certificate page can earn the largest portion of this amount provided they sell the most.
0.70% (70 bps)	Agency Fee	- this amount of the Total Commission is split amongst the members of the syndicate in accordance with fixed percentages established at the time of syndication. For example, if an investment dealer has 10% of an FTLF IPO it will receive 10% of the agency fee (or 0.07% of the Total Commission).

Lead Agent as Bookrunner

Typically, with an FTLF IPO the lead agent is also the book runner. A book runner essentially maintains a record of all potential subscribers who, through their registered brokers, have provided an expression of interest in acquiring Units of an FTLF. At any given time, if the promoters of an FTLF want to know the aggregate value of the book, they would contact the lead agent/book runner. In such circumstances, a lead agent/book runner will usually send an e-mail to the syndicate and selling group requesting confirmation of expressions of interest from their clients up to that point in time of the IPO. Notwithstanding the desire to understand “where the book is at” as they say on the street, lead agents and promoters are desirous of knowing when they have satisfied the minimum offering requirement – that is the minimum number of Units that must be sold in order to close an FTLF IPO.

Minimum Offering Size

The size of the minimum offering varies amongst FTLPs and can range from \$3 million for small deals to \$20 to \$50 million for larger FTLP IPOs (these larger FTLP IPOs often have maximum offering sizes between \$100 to \$200 million).

Once it has been determined that the minimum offering size has been satisfied, some FTLP issuers file the final prospectus (assuming the prospectus is cleared by the securities regulators to file the final prospectus) and then close some time thereafter (perhaps weeks later). Other FTLP issuers continue selling, knowing the minimum offering has been satisfied and then file its final prospectus and close almost immediately thereafter. The method chosen is something that is decided by the lead agent(s) and the promoters of the offering.

It is not uncommon for an FTLP issuer to file its prospectus at the end of a month (sometimes even the last business day of the month) even though its IPO may close a few weeks later. Retail brokers are usually content with this arrangement since they will receive credit for selling a given FTLP IPO at the end of one month (*i.e.*, September, the month the final prospectus is received) even though it closes the next month (*i.e.*, October).

Plan of Distribution

The plan of distribution is reflected in the agency agreement among the agents, the FTLP and the general partner/promoter of an FTLP. The agency agreement essentially states that the agents have agreed to form and manage a selling group consisting of registered investment dealers to offer Units for sale to the public in each of the applicable offering jurisdictions, on a best efforts basis if, as and when issued by the FTLP, in accordance with the terms and conditions thereof. The Units are generally offered, subject to a minimum aggregate purchase, at a price of \$25 per Unit payable on each closing. The price per Unit is typically determined by the general partner of the FTLP. The offering of the Units takes place during the period commencing on the date a receipt is issued for the (final) prospectus by the securities regulatory authority pursuant to Multilateral Instrument 11-102 – *Passport System* (“**MI 11-102**”) and ending at the close of business on the day prior to the final closing. If less than the maximum number of Units is subscribed for on the initial closing date, subsequent closings may be held. An FTLP typically pays the agents a sales commission equal to 6.75% of the selling price for each Unit sold to an investor.

The general partner, on behalf of the FTLP, reserves the right to accept or reject any subscription of Units in whole or in part. An investor whose subscription has been accepted by the general partner will become a limited partner upon the amendment of the record of limited partners maintained by the general partner to include their name and other information prescribed by the LPA.

While the agents generally agree to use their best efforts to sell the Units, they are not obliged to purchase any Units. The obligations of the agents under the agency agreement may be terminated, and the agents may withdraw all subscriptions on behalf of investors, on the basis of its assessment of the state of the financial markets or upon the occurrence of certain stated events including any material adverse change in the business, personnel or financial condition of the general partner or the FTLP.

In the agency agreement, the general partner, the FTLP, any promoter, the initial limited partner, jointly and severally, usually agree to indemnify the agents upon the occurrence of certain events.

It is not expected that any subscription proceeds will be received by the agents until subscriptions for the minimum offering are received and the other closing conditions of an FTLP IPO have been satisfied. However, to the extent that such subscription proceeds are received prior to such time, they are held by the agents in trust in a segregated account until subscriptions for the minimum offering are received and the other closing conditions of an FTLP IPO have been satisfied. If subscriptions for the minimum offering have not been received within 90 days after a final receipt under MI 11-102 for a final

prospectus, the offering may not continue without the filing of an amendment to the prospectus and absent such an amendment the subscription proceeds are returned to subscribers, without interest or deduction. Additional closings may be held on or before 90 days following a receipt for a final prospectus or a receipt for any amendment to a final prospectus, provided however that no closings may occur more than 180 days following the initial receipt for the final prospectus.

Generally, an FTLP IPO will close if: (a) all contracts described under “*Material Contracts*” in the prospectus and are delivered to the FTLP and counsel to the FTLP has opined that such contracts are valid and subsisting; (b) all conditions specified in the agency agreement for the closing have been satisfied or waived, and the agents have not exercised any right to terminate the IPO; (c) on the initial closing date, the minimum subscription of Units as set forth in the prospectus are accepted by the general partner of the IPO; and (d) the agreement with respect to a loan facility, if any, has been executed and delivered to the FTLP and is valid and subsisting.

Marketing During the Waiting Period

(a) General

During the “**waiting period**”¹² (e.g., in Ontario this means the period of time between the issuance by the OSC Director of a receipt of a preliminary prospectus of an FTLP and the issuance by the OSC Director of a receipt for the final prospectus) the *Securities Act* (Ontario) (the “**OSA**”) severely restricts an issuer’s ability to distribute materials for its IPO. The OSA states that it is permissible during the waiting period to:

- (i) distribute a notice, circular, advertisement or letter to or otherwise communicate with any person or company (the “**Marketing Communication**”) identifying the Units proposed to be issued, stating the price thereof, the name and address of a person or company from whom purchases of the security may be made (*i.e.*, the agents) and containing such further information as may be permitted or required by the regulations, if every such Marketing Communication states the name and address of a person or company from whom a preliminary prospectus may be obtained;
- (ii) to distribute a preliminary prospectus; and
- (iii) to solicit expressions of interest from a prospective purchaser if, prior to such solicitation or forthwith after the prospective purchaser indicates an interest in purchasing the security, a copy of the preliminary prospectus is forwarded to him, her or it (this is typically done by the agents).¹³

Agents must maintain a record of the names and addresses of all persons and companies to whom the preliminary prospectus has been forwarded. Each preliminary prospectus is numbered which assists in this process.

Various policies and notices have been published involving permitted and non-permitted marketing activities that one needs to be aware of in any IPO and counsel to the issuer should generally advise their clients that all Marketing Communication must be pre-cleared by their law firm prior to

¹² Section 65(1) of the OSA.

¹³ Section 65(2) of the OSA.

publication out of an abundance of caution. Securities regulators have made it very clear that the distribution of any Marketing Communication which can reasonably be considered to be in furtherance of a trade is prohibited until a receipt for the final prospectus is issued. This involves not only advertising but also media interviews and using the internet or other electronic means. For example, see: (a) National Policy 47-201 – *Trading Securities Using the Internet and Other Electronic Means*.

The advertising and marketing rules involving IPOs are set out in National Instrument 41-101, Part 13 – *Advertising and Marketing in Connection with Prospectus Offerings*. Under this part, a Marketing Communication used during the waiting period must contain the following legend in **bold face** type that is as large as the text used in the body of the Marketing Communication:

“A preliminary prospectus containing important information relating to these securities has been filed with securities commissions or similar authorities in certain jurisdictions of Canada. The preliminary prospectus is still subject to completion or amendment. Copies of the preliminary prospectus may be obtained from [insert name and contact information for dealer or other relevant person or entity.] There will not be any sale or any acceptance of an offer to buy the securities until a receipt for the final prospectus has been issued.”

Similarly, the following legend is required for a Marketing Communication following a receipt for a final prospectus, again in **bold face** type and as large as the text used in the body of the Marketing Communication:

“This offering is only made by prospectus. The prospectus contains important detailed information about the securities being offered. Copies of the prospectus may be obtained from [insert name and contact information for dealer or other relevant person or entity.] Investors should read the prospectus before making an investment decision.”

In addition, there are additionally rules for investment funds (such as FTLPs) during the waiting period which state that any advertisement during the waiting period may state only the following information:¹⁴

- (a) whether the security represents a share in a company or an interest in a non-corporate entity such as a trust unit or a partnership interest;
- (b) the name of the issuer;
- (c) the price of the security;
- (d) the investment objective(s) of the investment fund;
- (e) the name of the manager of the investment fund;
- (f) the name of the portfolio manager of the investment fund;
- (g) the name and address of a person or company from whom a preliminary prospectus may be obtained and purchases of securities may be made; and

¹⁴ Section 13.3 of NI 41-101.

(h) how many securities will be made available.

One should review these requirements and legal counsel should provide promoters of an FTLP IPO with this information so they do not inadvertently cross the line or “gun jump” as they say in the United States which has similar rules.

(b) *Green Sheets*

Other than the preliminary prospectus, FTLP issuers often also prepare a summary document called a green sheet (since years ago it was typically printed on green paper). This is a confidential document that is only circulated to investment bankers and their retail brokers and not to member of the retail public.

(c) *Road Shows and Conference Calls*

A “**road show**” is a phrase used in the securities industry where an FTLP issuer literally takes its “show on the road” in meeting with retail brokers in various cities in those jurisdictions where an FTLP IPO is being sold. It involves not only group meetings but also individual meetings with the promoters of the FTLP IPO and retail brokers. In group meetings, an FTLP issuer may, for example, host a luncheon or visit a branch office, provide a slide presentation and circulate materials to the retail brokers so the brokers will understand the offering and have the opportunity to ask any questions they may have about the offering. As with green sheets, all information provided to retail brokers through such things as slide shows and webcasts should match the information contained in the preliminary prospectus. Except for the prospectus, none of this information can be provided to the retail public.

The lead agent is often involved in working with the promoters of an FTLP IPO in scheduling such meetings with retail brokers. They may even schedule conference calls (usually in the middle of an FTLP IPO marketing cycle) with a recording available for approximately one month thereafter.

Due Diligence Sessions

Immediately prior to the filing of the preliminary prospectus, final prospectus and sometimes before a closing of an FTLP IPO, the lead agent will organize a due diligence conference call inviting all agents to participate with the officers and directors of the general partner/promoter of the FTLP, their legal counsel, the portfolio manager and the auditors of the FTLP and general partner.

Typically, in advance of the conference call, counsel to the agents, with input from the lead agent, will prepare and circulate written due diligence questions along with the most current version of the draft prospectus. Agents do this since securities legislation has a due diligence defence in the event that agents are sued. This practice assists the agents in possibly availing themselves of this defence.

On filing the final prospectus, the lead agent circulates bring-down due diligence questions to the syndicate and others that simply request the parties to the last due diligence call, in connection with filing the preliminary prospectus, to affirm their answers and ask additional questions.

It is not uncommon for a lead agent to have a due diligence call just before closing. This often does not involve the entire syndicate and is only with certain officers of the general partner/promoter of the FTLP and the lead agent for additional comfort prior to closing.

One Closing or Multiple Closings and Closing Dinners (assuming a successful IPO)

The entire IPO process is about closing the offering which can occur after the final prospectus is filed and receipted. The practice among FTLPs is mixed as to whether there are one or multiple closings. Obviously, the prospectus must contemplate multiple closings as part of the disclosure. If an FTLP IPO is sold out at the initial closing, then the lead agent/bookrunner becomes involved in determining which

agents are allocated Units of the FTLP IPO in a fair and equitable manner. This determination is generally determined prior to the filing of final prospectus and that percentage entitlement of each agent is reflected in their position on the certificate page of the prospectus, with the agents with the highest allocation at the top of the certificate page and agents with the same allocation located on the same line.

Where an FTLP IPO is not sold out certain FTLP issuers may have more than one closing. A determination of the number of closings is often a commercial matter between the lead agent and the promoters of the FTLP IPO, subject to applicable securities laws including an outside limit of 180 days following the issuance of a receipt for any amendment to a final prospectus.

Assuming the FTLP IPO has closed, the lead agent may host a closing dinner where other members of the syndicate are invited to attend along with officers/directors of the general partner/promoter of the FTLP and their legal counsel and other guests to celebrate a successful offering. In certain instances a lead agent will distribute “tombstones” to closing dinner participants. A tombstone is a desk ornament with particulars of the offering inscribed thereon.

CONTINUOUS DISCLOSURE OBLIGATIONS

An FTLP becomes a reporting issuer under Canadian securities law following the issuance of a receipt for the FTLP’s final prospectus and is subject to continuous disclosure obligations pursuant to National Instrument 81-106 – *Investment Fund Continuous Disclosure* (“**NI 81-106**”). A brief overview of some of the disclosure obligations under NI 81-106 is described below.

Financial Statements

(a) *Annual Financial Statements*

An FTLP must file annual financial statements and an auditor’s report for its most recently completed financial year on or before the 90th day after the FTLP’s most recently completed financial year. These statements must include (a) a statement of net assets as at the end of that financial year and a statement of net assets as at the end of the immediately preceding financial year; (b) a statement of operations for that financial year and a statement of operations for the immediately preceding financial year; (c) a statement of changes in net assets for that financial year and a statement of changes in net assets for the immediately preceding financial year; (d) a statement of cashflows for that financial year and a statement of cashflows for the immediately preceding financial year, unless it is not required by Canadian generally accepted accounting principles (“**Canadian GAAP**”); (e) a statement of investment portfolio as at the end of that financial year; and (f) notes to the annual financial statements.¹⁵ The above annual financial statements must include prescribed information as required by Part 3 of NI 81-106 and must be accompanied by an auditor’s report.

(b) *Interim Financial Statements*

An FTLP must file interim financial statements for the FTLP’s most recently completed interim period on or before the 60th day after the end of the FTLP’s most recent interim period. Generally, interim financial statements mean semi-annual financial statements and there is no requirement for an FTLP to file interim financial statements for its second and third quarters. (See “*Quarterly Portfolio Disclosure*” below) These statements must include: (a) a statement of net assets as at the end of that

¹⁵ Section 2.1 of NI 81-106.

interim period and a statement of net assets as at the end of the immediately preceding financial year; (b) a statement of operations for that interim period and a statement of operations for the corresponding period in the immediately preceding financial year; (c) a statement of changes in net assets for that interim period and a statement of changes in net assets for the corresponding period in the immediately preceding financial year; (d) a statement of cashflows for and as at the end of that interim period and a statement of cashflows for the corresponding period in the immediately preceding financial year, unless it is not required by Canadian GAAP; (e) a statement of investment portfolio as at the end of that interim period; and (f) notes to the interim financial statements.¹⁶ The above interim financial statements must also include prescribed information as required by Part 3 of NI 81-106.

Management Reports of Fund Performance

An FTLP must file a management report of fund performance (“**MRFP**”) at the same time that it files its annual or its interim financial statements for that financial period. The content of an MRFP must be in prescribed form as described in Form 81-106F1. An MRFP is the equivalent to the corporate management’s discussion and analysis (MD&A) that is appropriately modified for investment funds.

Delivery of Financial Statements and MRFPs to Limited Partners

Annual and interim financial statements and annual and interim MRFPs must be delivered to limited partners in accordance with the procedures set out in National Instrument 54-101–*Communication with Beneficial Owners of Securities of a Reporting Issuer* at the same time that they are filed with the securities regulators and posted on SEDAR.

NI 81-106 does give an FTLP the opportunity of not sending limited partners annual and interim financial statements and MRFPs if they obtain standing instructions or annual instructions. However, since an FTLP has such a short life span it is the understanding of the authors that few FTLPs, if any, request such instructions.

Board of Directors Approval

The board of directors of the general partner of the FTLP must approve the annual and interim financial statements and MRFP of an FTLP before those statements and MRFP are filed or made available to limited partners.

Quarterly Portfolio Disclosure

An FTLP must prepare quarterly portfolio disclosure prepared in accordance with Item 5 of Part B of Form 81-106F1 and post it on its web site within 60 days of the end of the period for which the quarterly portfolio disclosure was prepared. It must also send it promptly to limited partners upon request after it is posted.

Annual Information Form

An FTLP must file an annual information form (“**AIF**”) if it has not received a receipt for a prospectus during the last 12 months preceding its financial year end as at its financial year end and no later than 90 days after the end of its most recently completed financial year (the “**AIF Requirement**”),

¹⁶ Section 2.3 of NI 81-106.

subject to any exemption order. An AIF must be prepared in accordance with Form 81-101F2 subject to certain modifications.

Many FTLP issuers regularly obtain an exemption order from the OSC and other applicable Canadian securities regulatory authorities granting exemptive relief from the AIF Requirement. The basic argument is that the FTLP has a very short life-span and engages in very limited activities (*i.e.*, investing its available funds in Flow-Through Shares of Resource Issuers). Moreover, limited partners will obtain adequate financial information from the FTLP's annual and interim financial statements and MRFP thereon. The prospectus, the financial statements and MRFP provide sufficient information necessary for a limited partner to understand the FTLP's business, its financial position and its future plans, including any rollover transaction. If a material change takes place in the business and affairs of the FTLP, the FTLP will ensure that a timely material change report is filed with the Canadian securities regulatory authorities in each of the applicable jurisdictions.

The authors note that some promoters have applied for and received blanket exemptive relief for all FTLPs promoted by such promoters from the AIF Requirement involving future FTLP IPOs.

Proxy Voting Disclosure for Portfolio Securities Held

An FTLP must establish policies and procedures that it will follow to determine whether, and how, to vote on any matter for which the FTLP, as securityholder, receives proxy materials from an investee Resource Issuer as well as a proxy voting record.

The FTLP must prepare a proxy voting record on an annual basis for the period ending on June 30 of each year. If an FTLP has a web site it must also post the proxy voting record to its website no later than August 31 of each year and send the most recent copy, without charge, to any limited partner than makes a request after August 31.

The authors note that some promoters have applied for and received blanket exemptive relief for all FTLPs promoted by such promoters from the requirement to maintain a proxy voting record under section 10.3 of NI 81-106 and to prepare a proxy voting record on an annual basis. However, many FTLPs nonetheless prepare a proxy record and make it available free of charge to any limited partners of the FTLP.

Notice of Change in Legal Structure – Winding-up and Dissolution of the FTLP

Upon completion of the rollover transaction and the winding-up and dissolution of an FTLP, the FTLP must file a notice of same on SEDAR as soon as practicable and no later than the deadline for the first filing required by NI 81-106 following these events. The form of notice must include prescribed information.

REGULATION OF INVESTMENT FUND MANAGERS¹⁷

(i.e., General Partner of an FTLP)

On July 17, 2009, the Canadian Securities Administrators (the CSA) published in final form their reforms to the registration regime in National Instrument 31-103 – *Registration Requirements and Exemptions* (“**NI 31-103**”), along with certain consequential amendments to other securities laws (collectively, the “**New Rules**”). NI 31-103 came into force on September 28, 2009 (the “**Effective Date**”).

Under the former regime, the Canadian securities regulatory authorities under securities legislation were largely limited to investment fund rules in regulating conduct in the Canadian investment fund industry. Frequently, that meant regulators had to wait for a breach of the investment fund rules by an investment fund manager before action could be taken.

Under the New Rules, investment fund managers will now be subject to the same “fit and proper” standard by which registered dealers and advisers are measured, while the investment funds they manage will continue to be subject to the applicable investment fund rules. The addition of the investment fund manager (“**IFM**”) registration requirement gives the regulators wider powers in regulating this sector by allowing the regulators to exercise the considerable authority they have over registrants.¹⁸

New Registration Requirement for Investment Fund Managers

NI 31-103 introduces IFM as a new category of registration. All provinces and territories across Canada have amended their securities legislation to require a firm or individual that manages an investment fund to register in this new category.

An FTLP is an investment fund under securities law. Securities legislation in various Canadian jurisdictions defines “investment fund manager” to mean a person or company that directs the business, operations or affairs of an investment fund. This is the administrative aspect of managing an investment fund, which is distinct from the management of the investment portfolio of an investment fund (which requires analysis in connection with the portfolio manager registration requirement — a separate registration category altogether).

The CSA have stated in commentary that the term “manager” should be interpreted broadly and is intended to include, for example, the general partner of an investment fund that is organized as a limited partnership where the general partner acts in the capacity of decision-maker for the fund.

Typically, the general partner of an FTLP is the investment fund manager of an FTLP based on its duties and responsibilities as set out in the LPA. Sometimes the responsibilities of a general partner, by contract, are assigned to another entity.

¹⁷ **Acknowledgement:** The information involving the regulation of investment fund managers is taken from a commentary prepared by the Cassels Brock Registration and Compliance Group in 2009.

¹⁸ For example, the regulators can impose a broad range of terms and conditions on the IFM’s registration at any point in time, including terms and conditions which might materially impact its business.

Whether assigned or not, an FTLF is required to have an IFM that is registered under the New Rules with the Canadian securities regulatory authorities in the appropriate jurisdictions. Since the New Rules came into effect this year, this paper examines the requirements for an entity, whether it is the general partner or some other entity, to become registered as an IFM.

It is noted that even though the general partner typically under an LPA performs functions of an IFM that would trigger registration, the Companion Policy to NI 31-103 states that in the context of investment funds that are limited partnerships and that are part of an affiliated group of limited partnerships, each general partner in the affiliated group may enter into a contract with a single registered IFM within the group. In this case, the IFM would not be the general partner of a particular FTLF but rather another entity would be the IFM for the family of FTLFs. A discussion of the registration requirements of an IFM under the New Rules is set out in **Schedule "C"** attached hereto.

CONCLUSION

This paper identified the main actors involved in an FTLF IPO and the salient parts of the structure of such a fund. The role of the agents in the IPO has also been discussed as well as continuous disclosure obligations an FTLF has as a reporting issuer following the closing of an IPO. The paper has concluded with a brief description of some of the registration requirements under NI 31-103 involving investment fund managers which include the general partner of an FTLF. It is hoped that the reader now better understands these types of investment products, as they exhibit the typical process involved in bringing a product to market. The flow-through funds themselves have become very popular in Canada's capital markets in recent years and have generally provided excellent returns to investors. The fact that an investor can "walk away" with his or her money back even if the value of their investment falls from \$1,000 to \$701, shows the expected risk that such an investment is presumed to have. Nevertheless, the tax benefits available with these types of investments clearly demonstrate the Government's commitment to oil and gas and mineral exploration in Canada and the flow-through funds, with their extensive and knowledgeable investment in exploration companies have gone a long way to helping fulfill the commitment.

SCHEDULE “A”

2009 FTLP IPOs¹⁹

	Size (\$MM)	General Partner	Portfolio Manager	Promoter
November 2009 Closings				
Creststreet 2009 L.P.	\$5.0	Creststreet General Partner Limited	Creststreet Asset Management Limited	Creststreet General Partner Limited
Jov Diversified Flow-Through 2009 L.P.	\$8.4	Jov Diversified Flow-Through 2009 Management Corp.	JovInvestment Management Inc.	Jov Flow-Through Holdings Corp.
October 2009 Closings				
Front Street 2009-II Flow Through L.P.	\$32.2	Front Street Capital Management General Partner II Corp.	Front Street Investment Management Inc.	Front Street Capital Management General Partner II Corp. and Front Street Capital 2004
September 2009 Closings				
CMP 2009 II Resource L.P.	\$38.8	CMP 2009 II Corporation	Goodman & Company, Investment Counsel Ltd.	CMP 2009 II Corporation and Goodman & Company, Investment Counsel Ltd.
Discovery 2009 FT L.P.	\$13.8	Middlefield Fund Management Limited	Middlefield Capital Corporation	Middlefield Fund Management Limited and Middlefield Group Limited
WCSB Oil & Gas Royalty Income 2009 L.P.	\$25.9	WCSB Oil & Gas Royalty Income 2009 Management Corp.	Brickburn Asset Management Inc.	WCSB Holdings Corp., Brickburn Asset Management Inc. and CADO Bancorp Ltd.
July 2009 Closings				
Canada Dominion Resources 2009 L.P.	\$40.0	Canada Dominion Resources 2009 Corporation	Goodman & Company, Investment Counsel Ltd.	Canada Dominion Resources 2009 Corporation and Goodman &

¹⁹ **Acknowledgement.** *The authors would like to thank Mark Lerohl, Vice President, Investment Banking and Tim Evans, Director, Head of Managed Retail Products, Investment Banking, both of National Bank Financial Inc. who provided some of the this information for the paper.*

	Size (\$MM)	General Partner	Portfolio Manager	Promoter
				Company, Investment Counsel Ltd.
Mavrix Explore 2009-1 FT L.P.	\$6.6	Mavrix Explore 2009 – I FT Management Limited	Mavrix Fund Management Inc.	Mavrix Explore 2009 – I FT Management Limited and Mavrix Fund Management Inc.
Pathway Quebec Mining 2009 FT LP	\$4.9	Pathway Quebec Mining 2009 Inc.	Pathway Investment Counsel Inc.	Pathway Quebec Mining 2009 Inc.
June 2009 Closings				
Pathway Mining 2009 FT L.P.	\$8.5	Pathway Mining 2009 Inc.	Pathway Investment Counsel Inc.	Pathway Mining 2009 Inc.
Qwest Energy 2009 Flow-Through L.P.	\$9.0	Qwest Energy 2009 Flow-Through Management Corp.	Qwest Investment Fund Management Ltd.	Qwest Investment Management Corp.
May 2009 Closings				
MRF 2009 Resource L.P.	\$37.0	Middlefield Fund Management Limited	Middlefield Capital Corporation	Middlefield Fund Management Limited and Middlefield Group Limited
MSP 2009 Resource L.P.	\$10.4	MSP 2009 GP Inc.	Mackenzie Financial Corporation	MSP 2009 GP Inc. and Mackenzie Financial Corporation
April 2009 Closings				
NCE Diversified Flow Through 2009 Limited Partnership	\$60.5	NCE Diversified Management (09) Corp.	Sentry Select Capital Inc.	Petro Assets Inc.
March 2009 Closings				
CMP 2009 Resource Limited Partnership	\$42.5	CMP 2009 Corporation	Goodman & Company, Investment Counsel Ltd.	CMP 2009 Corporation and Goodman & Company, Investment Counsel Ltd.
Front Street Flow Through 2009-1 L.P.	\$39.6	Front Street Capital Management General Partner I Corp.	Front Street Investment Management Inc.	Front Street Capital Management General Partner I Corp.
WCSB Oil & Gas Royalty Income 2008-II L.P.	\$7.5	WCSB Oil & Gas Royalty Income 2008-II Management Corp.	Brickburn Asset Management Inc.	GORR Holdings Corp., Brickburn Asset Management Inc. and CADO Bancorp Ltd.
Total	\$390.6			

In addition to the FTLP offerings which have closed as outlined above, there are currently at least five other FTLP offerings which have, at a minimum, filed a preliminary prospectus, but which have not closed as at the date of this paper as set forth below.

	Minimum Offering Size (\$MM)	General Partner	Portfolio Manager	Promoter
Unclosed Offerings				
Connor, Clark & Lunn 2009 FT L.P.	\$3.0	Connor, Clark & Lunn 2009 Flow-Through Management Corp.	Connor, Clark & Lunn Investment Management Ltd.	Connor, Clark & Lunn 2009 Flow-Through Management Corp. and Connor, Clark & Lunn Investment Management Ltd.
EnerVest FTS L.P. 2009	\$2.0	EnerVest 2009 General Partner Corp.	Cypress Capital Management Ltd.	EnerVest 2009 General Partner Corp. and EnerVest Management Ltd.
Faircourt Exploration Flow-Through 2009 L.P.	\$3.0	Faircourt Exploration Flow-Through 2009 Management Ltd.	Faircourt Asset Management Inc.	Faircourt Asset Management Inc.
Jov Diversified Québec 2009 Flow-Through L.P.	\$2.5	Jov Diversified Québec 2009 Flow-Through Management Corp.	Jov Investment Management Inc.	Jov Flow-Through Holdings Corp.
Stone 2009 FT L.P.	\$4.0	Stone 2009 Flow-Through GP Inc.	Stone Asset Management Limited	Stone & Co. Limited and Stone 2009 Flow-Through GP Inc.
Total	<u>\$11.5</u>			

SCHEDULE "B"

SAMPLE INVESTMENT RESTRICTIONS AND GUIDELINES OF AN FTLP

An example of the investment guidelines of an FTLP that has a loan facility are set forth below.

- (a) **Resource Issuers.** The FTLP will invest substantially all available funds in Flow-Through Shares issued by Resource Issuers engaged primarily in oil and gas and mineral exploration, development or production or energy production in Canada that will incur CEE including CRCE. To the extent the FTLP disposes of Flow-Through Shares, the FTLP may reinvest the net proceeds from any such dispositions in securities of other Resource Issuers or additional Flow-Through Shares of other Resource Issuers or use them to exercise warrants.
- (b) **Warrants.** The FTLP may also invest up to 5% of available funds in warrants and/or common shares acquired as a part of or independently of a transaction in which the FTLP enters into a flow-through agreement with a Resource Issuer provided that not more than 5% of the aggregate purchase price under the relevant flow-through agreement shall be used to purchase warrants and/or common shares.
- (c) **Exchange Listing.** The FTLP will invest a minimum of 80% of available funds in Flow-Through Shares of Resource Issuers whose shares are listed and posted for trading on the TSX or the TSX Venture Exchange; provided that at least 30% of the available funds will be invested in Flow-Through Shares of Resource Issuers whose shares are listed and posted for trading on the TSX.
- (d) **Market Capitalization.** The FTLP will invest a minimum of 35% of available funds in Resource Issuers whose market capitalization (determined at the time of purchase) exceeds \$50 million.
- (e) **Diversification.** The FTLP will limit any investment in a single Resource Issuer having a market capitalization of: (i) less than \$50 million to a maximum of 10% of available funds; and (ii) more than \$50 million to a maximum of 20% of available funds.
- (f) **Private Companies and Illiquid Investments.** The FTLP will invest a maximum of 20% of available funds in Flow-Through Shares of Resource Issuers which are not reporting issuers or which are reporting issuers and are quoted on the Canadian National Stock Exchange and will limit its investment in any such issuer to a maximum of 10% of available funds.
- (g) **No Borrowing.** Except for the loan facility, which will be used solely to finance the agents' fee, the expenses of the offering and the FTLP's ongoing fees and expenses, the FTLP may not borrow money.
- (h) **No Other Undertaking.** The FTLP will not engage in any undertaking other than the investment of the FTLP's assets with regard to the FTLP's investment objectives, investment strategies and investment restrictions and guidelines.
- (i) **Purchasing Securities.** The FTLP will not purchase securities other than Flow-Through Shares other than through normal market facilities unless the purchase price therefor approximates or is less than the prevailing market price or is negotiated or established on an arm's length basis from the FTLP and the general partner and the portfolio manager and its affiliates.

- (j) **Fixed Price.** Except for investments in warrants, the FTLP will not purchase any security which may by its terms require the FTLP to make a contribution in addition to the payment of the purchase price provided that this restriction shall not apply to the purchase of securities which are paid for on an installment basis where the total purchase price and the amount of all such installments is fixed at the time the initial installment is paid.
- (k) **No Material Interest.** The FTLP will not purchase securities from or sell securities to the General Partner or any of the general partner's respective affiliates, any officer, director or shareholder of any of them, any person, trust, firm or corporation managed by the general partner or any of their respective affiliates or any firm or corporation in which any officer, director or shareholder of the general partner may have a material interest (which, for these purposes, means beneficial ownership of more than 10% of the voting securities of such entity) unless, with respect to any purchase or sale of securities, any such transaction is: (i) effected through normal market facilities, is not pre-arranged and the purchase price approximates the prevailing market price; and (ii) is approved by the IRC and is not a "related party transaction" as such term is defined in Multilateral Instrument 61-101 which requires limited partner approval. The restriction will not apply to the sale of FTLP assets to the mutual fund corporation in advance of the dissolution of the FTLP, if such a transaction should occur, or as part of a liquidity alternative.
- (l) **No Commodities.** The FTLP will not purchase or sell commodities.
- (m) **No Guarantees.** The FTLP will not guarantee the securities or obligations of any person.
- (n) **No Real Estate.** The FTLP will not purchase or sell real estate or interests therein.
- (o) **No Lending.** The FTLP will not lend money. For purposes of this restriction, investments in high-quality liquid investments are not considered lending.
- (p) **No Control.** The FTLP will not purchase securities of an issuer for the purpose of exercising control or management over such issuer and will not purchase more than 19.99% of the voting securities of any Resource Issuer in which it may invest.
- (q) **Restriction on Underwriting.** The FTLP will not act as an underwriter except to the extent that the Partnership may be deemed to be an underwriter in connection with the sale of securities in its investment portfolio.
- (r) **No Short Sales.** The FTLP will not make short sales of securities other than for hedging purposes against existing positions held by the FTLP.
- (s) **No Mortgages.** The FTLP will not purchase mortgages.
- (t) **No Mutual Funds.** The FTLP will not purchase securities of a mutual fund except, if completed, as part of the rollover transaction or as part of a liquidity alternative, as applicable.
- (u) **No Derivatives.** The FTLP will not purchase or sell derivatives.

SCHEDULE “C”
REGISTRATION REQUIREMENTS OF INVESTMENT FUND MANAGERS
UNDER NI 31-103²⁰
(i.e., General Partner of an FTLP)

Registration of Individuals

An IFM must designate, and apply for registration of, an Ultimate Designated Person (“**UDP**”) and a Chief Compliance Officer (“**CCO**”). Depending on the size and structure of the firm, the UDP and CCO may be the same person.

Ultimate Designated Person: The UDP’s role is to promote compliance at the firm and oversee the effectiveness of the firm’s compliance system. The UDP does not have to be involved in the day-to-day management of the compliance group. The designated UDP must be: (i) the CEO, sole proprietor or equivalent of the firm; (ii) an officer in charge of the division of the firm, if the activity that requires the firm to register occurs only within that division; or (iii) an individual acting in a capacity similar to that of a CEO or an officer in charge of a division of the firm. No proficiency requirements are specified for the UDP function.

Chief Compliance Officer: The CCO is required to: (i) establish and maintain policies and procedures for assessing compliance by the firm, and individuals acting on its behalf, with securities legislation; (ii) monitor and assess compliance by the firm, and individuals acting on its behalf, with securities legislation; (iii) report to the UDP as soon as practicable if the CCO becomes aware of any circumstances indicating that the firm, or any individual acting on behalf of the firm, is in non-compliance with securities legislation; and (iv) submit an annual report to the board of directors (or similar body or authority in a non-corporate structure) for the purpose of assessing compliance by the firm, and individuals acting on its behalf, with securities legislation. Proficiency requirements are specified for the CCO function.

No other individuals are required to be registered in connection with an IFM.

Permitted Individuals

Notwithstanding that only the UDP and CCO of an IFM are required to be registered, all persons involved in an IFM who fall within the category of “permitted individuals” are required to complete and file a Form 33-109F4 under National Instrument 33-109 — *Registration Information* (“**NI 33-109**”), the same form submitted by all individuals who seek individual registration (such as the UDP and CCO).

The following persons are permitted individuals under NI 33-109:

²⁰ **Acknowledgement:** The information involving the regulation of investment fund managers is taken from a commentary prepared by the Cassels Brock Registration and Compliance Group in 2009.

- a director, chief executive officer, chief financial officer, or chief operating officer of the IFM, or a person who performs the functional equivalent of any of those positions, and
- an individual who has beneficial ownership of, or direct or indirect control or direction over, 10 percent or more of the voting securities of the IFM.

The filing requirement for permitted individuals is aimed at the “mind and management” of the IFM (i.e., those who have direct influence or control of the firm). The purpose of the filing requirement is to ensure that permitted individuals are subject to review by the regulator as part of its oversight of an IFM’s fitness for registration.

Fit and Proper Standard, Conduct, and Conflict of Interest Requirements

The regulators assess a firm’s or individual’s fitness for registration at the time of the initial application for registration. The main elements of “fitness” are proficiency, solvency and integrity. If the applicant does not satisfy the fitness criteria, registration will not be granted, or may be granted subject to terms and conditions. Thereafter, registered firms and individuals must continue to satisfy the fitness criteria. Conduct, conflicts of interest, and compliance procedures are also contemplated in NI 31-103.

(i) Fit and Proper Standard

IFMs must meet the fit and proper standard. Non-compliance may result in registration being refused, the imposition of terms and conditions by the regulators, or the suspension of registration.

Proficiency Requirements for CCO: The CCO is subject to a proficiency requirement. The CCO must meet one of the following three proficiency options.

Option A

- A CFA Charter or professional designation as a lawyer, Chartered Accountant, Certified General Accountant or Certified Management Accountant in a jurisdiction in Canada, a notary in Quebec, or the equivalent in a foreign jurisdiction;
- Successful completion of the following exams —
 - (i) the Canadian Securities Course Exam of CSI Global Education Inc. (CSI), and
 - (ii) the “PDO Exam”;²¹ and
- Either of the following —
 - (iii) 36 months of relevant securities experience while working at a registered dealer, a registered adviser or an investment fund manager, or
 - (iv) provided professional services in the securities industry for 36 months and worked for an investment fund manager for 12 months.

²¹ PDO Exam means either (a) the IFIC Officers’, Partners’ and Directors’ Exam, or (b) CSI’s Partners, Directors and Senior Officers Exam.

Option B

- Successful completion of the following exams —
 - (i) any of
 - (a) the Investment Funds Institute of Canada (IFIC) Canadian Investment Funds Exam,
 - (b) CSI's Canadian Securities Course Exam, or
 - (c) CSI's Investment Funds in Canada Course Exam; and
 - (ii) the PDO Exam; and
- Five years of relevant securities experience while working at a registered dealer, registered adviser or an investment fund manager, including 36 months in a compliance capacity.

Option C

- Meeting the proficiency requirements for a CCO of a portfolio manager.²²

Exemptions from the proficiency requirements may be obtained in cases where the regulator is satisfied that an individual's qualifications are equivalent to, or more appropriate in the circumstances than, the prescribed criteria.

Capital Requirements: IFMs are subject to capital requirements. An IFM's excess working capital (calculated as prescribed and certified by management) must not be less than zero for two consecutive days, and the IFM must maintain minimum capital of \$100,000 at all times. Negative excess working capital at any time must be reported to the regulator as soon as possible.

Insurance: IFMs must maintain bonding or insurance coverage containing the following clauses — fidelity, on premises, in transit, forgery or alternations and securities. The coverage must include either a double aggregate limit or a full reinstatement of coverage provision, and coverage must be in the greater of the following amounts for each clause:

- 1% of assets under management or \$25,000,000, whichever is less;
- 1% of the IFM's total assets or \$25,000,000, whichever is less;
- \$200,000; and
- the amount determined to be appropriate by a resolution of the directors (or individuals acting in a similar capacity).

Changes to, claims under, or cancellation of such insurance policy must be reported in writing to the regulator as soon as possible.

Financial Reporting: IFMs must have an auditor and must file the following:

²² For the proficiency requirements for a CCO of a portfolio manager, please ask for a copy of our portfolio manager commentary.

- annual filings (within 90 days of its year end):
 - annual financial statements (with an audit report),
 - a completed Form 31-103F1 Calculation of Excess Working Capital (showing excess working capital as at the end of the financial year, with the comparative amount as at the end of the preceding financial year), and
 - a description of any net asset value (NAV) adjustment made in respect of an investment fund managed by the IFM during the financial year.
- quarterly filings (within 30 days of each quarter end):
 - interim financial statements for the quarter,
 - a completed Form 31-103F1 *Calculation of Excess Working Capital* (showing excess working capital as at the end of the quarter, with the comparative amount as at the end of the preceding quarter), and
 - a description of any NAV adjustment made in respect of an investment fund managed by the IFM during the quarter.

A description of NAV adjustment must contain prescribed information, including the effect of the adjustment on NAV per unit or share and any correction made to purchase and sale transactions.

All financial statements are to be prepared in accordance with GAAP, but on an unconsolidated basis. Fiscal year-end changes, together with the reasons for the change, must also be reported to the regulator in writing within seven days following the change.

(ii) Conduct Rules

IFMs are not subject to the know-your-client, suitability, client complaint handling and relationship disclosure requirements applicable to other registrants. IFMs are also exempt from most of the client account handling requirements for registered firms.

However, NI 31-103 contains detailed and technical conduct requirements for all registrants, including IFMs. The regulators consider compliance to be a firm-wide responsibility to be carried out in accordance with a documented compliance system which must address, among other things, the following elements.

Compliance System: IFMs must establish, maintain and apply policies and procedures that:

- create a system of controls and supervision sufficient to provide reasonable assurance that the firm and each individual acting on its behalf complies with securities legislation, and
- manage the risks associated with its business in accordance with prudent business practices.

Client Assets: Client assets that are held by an IFM must be segregated and held in trust for the client (in the case of cash, in a designated trust account at a Canadian financial institution, a Schedule III bank, or a member of IIROC; and in the case of securities, in accordance with certain requirements).

Record-Keeping and Retention: Record-keeping is mandated, and certain client records must be kept for at least seven years from the date the record was created, and in a manner that permits the records to be provided to the regulator in a reasonable period of time. NI 31-103 does not contain a prescriptive list of records that must be kept. Instead, it requires the retention of all records that demonstrate compliance with securities legislation.

Referral Arrangements: NI 31-103 restricts all registrants, including IFMs, from participating in referral arrangements (*i.e.*, referring clients) unless:

- a written referral agreement exists between the IFM and the person or company making the referral; and
- the referred clients are provided with written disclosure setting out the key terms of the referral agreement.

(iii) Conflicts of Interest

IFMs are subject to the conflicts of interest provisions of NI 31-103 that apply generally to registered firms, but the application of these provisions depends on whether the investment funds managed by the IFM are subject to NI 81-107 — Independent Review Committee (NI 81-107).²³

- **Where NI 81-107 Applies** — For investment funds that are reporting issuers, IFMs are not subject to the conflicts of interest rules of NI 31-103 but are subject to NI 81-107, which sets out extensive conflicts of interest rules.
- **Where NI 81-107 Does Not Apply** — For investment funds that are not reporting issuers, IFMs are subject to the conflicts of interest provisions of NI 31-103. The CSA provide extensive guidance in Companion Policy 31-103CP on the application of the principals governing the conflicts of interest requirement.

Registrations in Multiple Categories

If a firm is registered in more than one category, the firm need only meet the most stringent of the applicable capital and insurance requirements.²⁴ The capital and insurance requirements are not cumulative.

The business of an IFM may give rise to multiple registration requirements. For example, an IFM that is also managing the portfolio of an investment fund under its management, or is otherwise providing investment advice to the investment fund, will be subject to the adviser registration requirement as well as the IFM registration requirement.

There are dealer registration exemptions for an investment fund (as well as the IFM) in respect of dividend or distribution reinvestment plans or optional investment plans of the investment fund or for certain additional investments by fund security holders.

As an issuer of securities, an investment fund may be in the business of trading in securities and, therefore, subject to the requirement to register as a dealer. The application of the dealer registration requirement in such a situation will depend on the facts and the conclusion will vary from case to case.

²³ NI 81-107 also deals extensively with conflicts of interest matters, so it is necessary to specify which rules govern.

²⁴ There is an exemption to the rule that a multiple-category registrant must satisfy the most stringent capital requirement, but it is not particularly relevant to an IFM registrant.

Participation Fees

In Ontario, firms registered as an IFM are required to pay the capital markets participation fees under OSC Rule 13-502 — *Fees*. Annual fees are also applicable in other jurisdictions.

No Renewal Process for Registration

Under NI 31-103, registration does not have to be renewed annually, and will remain in effect until surrendered, suspended or revoked.

Suspension and Revocation of Registration

While registration does not have to be renewed annually, an IFM firm's ability to continue carrying on registrable activities is contingent upon the firm continuing to meet the fit and proper standard. Similarly, an individual's ability to continue serving in the capacity of a CCO or UDP is contingent on the individual continuing to meet the fit and proper standard. Under NI 31-103, the regulators have a more immediate ability to suspend registration. In addition, a firm's registration will be suspended automatically if it fails to pay its annual fees within 30 days of the due date.

Transition Requirements

NI 31-103 provides some transitional relief by allowing time after the Effective Date for meeting the New Rules. The transition periods that apply to IFMs are set out below are based on a September 28, 2009 implementation date being the date the New Rules came into effect.

- (i) *An investment fund manager with its head office in Canada and that is active on the Effective Date:*
- 12 months (September 28, 2010) for the firm to apply for IFM registration in the jurisdiction in which its head office is located (which application will include compliance with all individual and firm requirements, such as the designation of a UDP and a CCO and filings in respect of all permitted individuals).
 - 24 months (September 28, 2011), being a tentative target date for the firm to register in all other Canadian jurisdictions in which the investment funds managed by the IFM are sold.²⁵
- (ii) *An investment fund manager with its head office in Canada and that is not active on the Effective Date:*
- No Transition — If a firm is a new entrant to the investment fund industry, the firm must apply for IFM registration in the jurisdiction in which its head office is located before it can

²⁵ The CSA expect to publish a proposal for comment in the next year to explain circumstances under which an IFM that does not have a Canadian head office will need to register, and in what additional provinces and territories an IFM with a head office in Canada will need to register. As currently presented, the registration requirement for IFMs seems at odds with the termination of the so-called “flow-through” rule for portfolio managers (i.e., Ontario will no longer require portfolio managers to be registered in Ontario solely on the basis of providing advice to an investment fund constituted outside of Ontario which is sold to Ontario investors).

commence operations (which application will include compliance with all individual and firm requirements applicable to the category).

(iii) *An investment fund manager with its head office outside Canada, whether it is active or not on the Effective Date:*

- 24 months (September 28, 2011), being a tentative target date for the firm to register in the applicable Canadian jurisdictions.

Other Registration Reforms

NI 31-103 and the New Rules include other significant changes to registration requirements for dealers, advisers and investment fund managers in Canada which are beyond the scope of this paper.