PMAC
PORTFOLIO MANAGEMENT ASSOCIATION OF CANADA
Advancing Standards™

August 29, 2012

Brian Ernewein,
General Director, Legislation
Tax Policy Branch
140 O'Connor St.
Ottawa, ON K1A 0G5

Re: "Prohibited Investment" Rules under Part XI.01 of the *Income Tax Act* - RRSPs and RRIFs

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Following our letters of December 13, 2011 and March 8, 2012 and past discussions with the Department of Finance staff where we discussed our concerns with the "prohibited investment" rules (the "Rules") under Part X1.01 of the *Income Tax Act*, we were very pleased to review your letter of June 12, 2012 (the "Letter") which addressed a number of concerns raised by PMAC and other industry associations.

We are delighted that the Department of Finance has agreed with some of the concerns we raised and will be recommending to the Minister of Finance that technical amendments be introduced to modify the impact of some of the Rules.

As you are aware, one of PMAC's key advocacy priorities has been to seek clarity with the Federal government on the impact of the Rules as they apply to investments made by RRSPs and RRIFs. The Rules currently require for example, certain portfolio managers or investment fund managers (who are caught by the rules due to owning in excess of 10% of their firms that manage pooled funds) to liquidate their (and family) registered accounts from these funds as a result of the possible interpretation of such relationship being non-arm's length. As noted in your Letter, the arm's length test is not as bright-line a test as the "related" party test and that, while many taxpayers who currently hold prohibited investments appear to be part of a group with very close ties to the investment entity, it is possible to hold a portfolio position that, unknown to the taxpayer, is in fact a prohibited investment for the taxpayer's RRSP due to the combination of family holdings and/or non-arm's length relationships.

We are pleased that the Department of Finance has agreed with us and others that the scope of the definition of "prohibited investment" is too broad in certain cases and could apply in circumstances where a particular individual's registered plan holds a comparatively small investment in, for example, an investment fund controlled by their employer or by the employer of a family member.

We support the Department of Finance's recommendations for significant changes to the Rules to address these and other concerns. In particular, we applaud the recommendation to narrow the definition of "prohibited investment" such that the rule stating that investments in entities with which you (or any entity in which you have a significant interest) do not deal at arm's length is repealed. This would ensure that the prohibited investment rules do not apply in circumstances where the planholder both lacks a significant interest in the Issuer in question and deals at arm's length with the Issuer.

It is worth noting however, that there is still some uncertainty as to whether a planholder who holds a *controlling interest* in a fund manager, could be considered not to deal at arm's length with funds managed by that fund manager, and thus an investment in such a fund could be a prohibited investment. We would appreciate further clarity in this regard. In addition, we still believe there is room for further clarity regarding the application of the arm's length test generally in order to provide more certainty regarding the application of the Rules. Similarly, there is still difficulty in trying to determine whether the 10% threshold is triggered. For example, an individual and fund manager, may not know what investments relatives such as siblings, parents, children and in-laws have made. Moreover, privacy laws may prevent financial intermediaries from disclosing information necessary to determine ownership thresholds. Consequently, portfolio managers may not be able to determine whether the 10% rule may be triggered by a client, thereby having potentially disastrous results for the client.

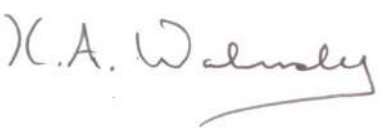
We will continue to monitor the impact of the Rules on our membership and are also awaiting a response from the CRA to a request for interpretation we submitted in March 2012.

We would like to express our gratitude to the Department of Finance for acknowledging that the Rules are inappropriately broad and should not catch many of the investments discussed in our prior submissions that are not the target of the Rules.

We look forward to your continued efforts in recommending the proposed changes outlined in your Letter and would be pleased to respond to any further questions you may have.

Yours truly;

PORTFOLIO MANAGEMENT ASSOCIATION OF CANADA



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