

May 26, 2008

Mr. John Stevenson
Secretary - Ontario Securities Commission
Via E-mail

The Honorable Iris Evans
Minister of Finance, Province of Alberta
Via E-mail

Re: Proposed National Instrument 31 -103 / Registration Reform Project

I would like to thank the Canadian Securities Administrators for the opportunity to once again comment on the proposed National Instrument 31-103/Registration Reform Project, and in particular, how it relates to the exempt market.

I, along with my colleagues, competitors, and advisors are hopeful that the Canadian Securities Administrators will give the new round of comments the appropriate consideration, realize the proposed changes are misguided and cancel them in their entirety. Failing that, we would hope the CSA would make critical amendments to the proposals and release a much-needed third draft for discussion.

While the Canadian Securities Administrators, and in particular, the Alberta Securities Commission, should be applauded for some of the recent revisions to National Instrument 31-103, there are still a number of items that need addressing prior to the Registration Reform Project moving forward.

Although the definition of handling clients' cash needs to be re-visited (in the exempt market typically only the issuer or law firm actually handles the cash) the Canadian Securities Administrators clearly gave certain previous items of contention the appropriate consideration as the idea of bonding and audited financials (from dealers) seems to have been taken off the table for the most part.

I hope that the Canadian Securities Administrators will give the same consideration to the two primary items of contention that remain on the table, the implementation of Know Your Client forms and the requirement of those selling exempt market securities to take the Canadian Securities Course. While the underlying goal of these two proposals (better investor protection) is to be commended, the proposals themselves are not compatible within the exempt market.

At a recent consultation session held in Calgary, Alberta Securities Commission staff agreed there was an inherent conflict in implementing Know Your Client forms in the exempt market and that the Canadian Securities Course was not an ideal course for the exempt market industry. Having said that, Alberta Securities Commission staff seemed to take the position that the Canadian Securities Course and Know Your Client forms were essentially the best that the Canadian Securities Administrators could come up with to

reduce the number of investors being “preyed upon.” I believe these two (and a few other) ideas are unfounded, conflicted, and should not be implemented.

“Know Your Client” Forms / Risk Acknowledgement Forms

By the definition afforded by the offering memorandum exemption pursuant to the National Instrument 45-106, all exempt “market” securities are categorized as being high risk. Despite the fact that the contrary is often true, those that invest in exempt securities by way of an offering memorandum are required to sign a form acknowledging that they could lose all their money. This, in conjunction with the Canadian Securities Administrator’s proposal to implement Know Your Client forms, leads to a huge problem for all those who sell exempt market securities. If an investor indicates that their risk tolerance is anything less than high, they theoretically should not be able to invest in ANY exempt security. In fact, since most that we do are backed by real estate, many exempt securities are safer than marketable securities and in many cases, investors are forced to misrepresent themselves by signing a form acknowledging that they could lose all of their money, even though that isn’t the case. When was the last time land was worth NOTHING?

Despite the fact that multiple sound arguments have been made indicating that Know Your Client forms make absolutely no sense relative to exempt market securities, the Canadian Securities Administrators seem to be determined to implement this proposal. If this ends up materializing, I don’t see how the Canadian Securities Administrators have any choice but to re-visit the categorization of exempt market securities as all being high risk. Are the Canadian Securities Administrators prepared to review and categorize each individual exempt market security? If not, this idea must be thrown out.

Another problem with Know Your Client forms is that they need to be renewed on an annual basis. Despite the fact that the Canadian Securities Administrators have defined the investments in question as being exempt “market” securities, the fact is these are usually long-term investments and there is effectively no “market” for these securities. With that, a Know Your Client form again is not compatible. If a client’s financial situation or risk tolerance changes in a 365-day period, they cannot simply sell their exempt securities on the market and move into something “safer,” so why bother with this form in the exempt market? Know Your Client forms are clearly tailored to financial advisors that want to know their “client” and have the ability to alter investment portfolios as their clients’ needs change. They are by no means a form compatible in the exempt market, as “clients” don’t exist, only purchasers do. The Canadian Securities Administrators need to understand the difference between the two and take the appropriate action in aborting this idea.

Fixing the “Problems” within the Exempt Market with Additional Regulation

The Alberta Securities Commission mentioned the significant amount of unscrupulous activity that is present in the exempt market, yet could provide no statistics despite countless requests.

No matter how many rules are put in place, it is unfortunate to say that some investors will inevitably fall victim to the few unscrupulous promoters in the industry. Having said that, if the Alberta Securities Commission were to provide the statistics we’ve

continuously asked for, I suspect that the problems within the exempt market relate to less than 1% of the capital raised. National Instrument 45-106 even covers this small percentage in that those victims that are “preyed upon” have the right to sue for misrepresentations (for up to three years!) as is provided for by the offering memorandum. So in essence, 99% of investors don’t have problems and the 1% that do, have recourse. It seems to me that the Canadian Securities Administrators are trying to fix something that is clearly not broken.

The pendulum of regulation has swung far enough and the current regime is serving investors well. There is no problem and therefore no solution (i.e. additional regulation) is required. Adding additional regulation will only increase the costs of raising capital (which are always passed on to investors) and will not increase investor safety. In fact, investor safety may be compromised if some of the proposals are implemented, as you’ll essentially be “legitimizing” everyone, even the dishonest ones. In fact, creating more complex and harder to follow regulations will not increase investor protection since those that don’t follow the current rules (and didn’t attend the consultation sessions) won’t follow the new ones either.

Canadian Securities Course

Education is always a good thing and should be a requirement in any industry but the Canadian Securities Course is irrelevant to the exempt market industry. If the Canadian Securities Administrators are set on having an educational benchmark for the exempt market to meet, they need to draft something applicable, as the Canadian Securities Course is not it.

Of its hundreds of pages, the Canadian Securities Course has four pages relative to real estate. Most exempt market securities (probably 90% in Alberta) are tied into real estate so how is the Canadian Securities Course going to help anyone?

The Canadian Securities Administrators need to establish a new steering committee to oversee the drafting of a course applicable to those that want to deal in exempt market securities and I for one would be happy to assist in the process.

Conclusion

It is my opinion that new regulation need to have a solid reasoning behind its implementation (more than “it’s the best we’ve got” to deal with the problems we can’t specifically show you).

The investing public is being served extremely well by the current offering memorandum regime provided by National Instrument 45-106. Those investing in the exempt market are receiving more diversified investment opportunities, disclosure, and risk warnings than they ever have before and the billions of dollars being raised should be embraced and treated as a huge success, rather than classified as a problem needing more regulation. The growing perception is that the volume of dollars being handled in the exempt market is only a problem for those losing access to the money, the Mutual Fund Dealers Association and Investment Dealers Association who, not surprisingly, are the ones predominantly steering the Registration Reform Project. These individuals have no business (or required knowledge) to suggest how the exempt market should be regulated! The requirement of exempt market salespersons taking the Canadian Securities Course

and having exempt market investors fill out Know Your Client forms are a clear examples of this. The Canadian Securities Administrators should in turn create an exempt market committee (made up of exempt market participants) to come up with ideas on how to better govern this industry....OUR industry.

I strongly urge the Canadian Securities Administrators (in particular the Alberta Securities Commission) to re-visit the idea of implementing the Registration Reform Project as it will ultimately harm this country's capital markets and do little more than play into the hands of the Mutual Fund Dealers Association and the Investment Dealers Association.

While I cannot comment on what has happened elsewhere, those in the exempt market industry in Alberta have clearly expressed strong opposition to the Registration Reform Project and as such, it should be dropped immediately. If other jurisdictions (aside from British Columbia who has backed out) are set on going forward and following the Registration Reform Project, so be it, but Alberta is different and should act independently.

The presentation at the recent Alberta Securities Commission meeting indicated that approximately 96% (116 of 121) of the letters in reference to the proposed changes in the exempt market were opposed to one or more of the suggested registration requirements. This statistic doesn't even include the 374 "Know Your Client" opposition letters that were sent in on time yet ignored by the Ontario Securities commission. However, little seems to have changed so far.

Albertans responded strongly by attending the consultation sessions in much larger numbers than could be accommodated. It is now up to the Canadian Securities Administrators and the Alberta Securities Commission in particular, to show that they are listening and serve the best interest of the public rather than feed into the perception of buckling to the pressure of the Mutual Fund Dealers Association and the Investment Dealer Association.

The message couldn't be clearer. The exempt market participants and investors do not like what you are doing. As a government body in place to serve the interests of the investing public, the Canadian Securities Administrators and the Alberta Securities Commission need to listen to public opinion and drop this initiative immediately. If, as I suspect, doing so would be incompatible with the various political agendas, I would strongly suggest you redesign the initiative in order to minimize the negative impact on the capital markets of Alberta.

Yours truly,

Chris Charron
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