GreensKeeper
ASSET MANAGEMENT

a division of
LIGHTWATER
PARTNERS LTD

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Dear Sirs/Mesdames,

I am writing to you in response to CSA Staff Consultation Note 45-501 and to the request for written submissions made by James Turner at the roundtable consultation session held at the offices of the Ontario Securities Commission (OSC) in Toronto on February 1, 2012.

By way of background, I am currently registered as an Associate Advising Representative (AAR) with the OSC. I have spent my entire 15-year career in the securities industry, first as a lawyer (Securities & M&A) and then as an investment banker. My current role at Lightwater is to assist in managing the GreensKeeper Value Fund (the "Value Fund") under the direct supervision of Jerome Hass, an Advising Representative and Chief Compliance Officer. The Value Fund was launched on November 1, 2011 and offers its units in the Exempt Market relying almost exclusively on the Accredited Investor (AI) exemption or the $150,000 exemption (collectively, the "Exemptions").

In response to your request for comments regarding the possibility of amending the Exemptions, I respectfully submit the following five items for your consideration.

1. Limiting Investment Choices for the Non-Wealthy

By further restricting the Exemptions, you would effectively limit access to hedge funds and some of Canada's best investment managers to the rich. As a person whose mother grew up in poverty, I find this form of discrimination to be unworthy of our country despite the well-meaning goal of protecting the vulnerable. My own preference would be to offer access to the Value Fund to all investors. However, the costs associated with running a mutual fund at start-up are prohibitive. I believe that *all* investors should have access to different investment vehicles. Diversification in their investment choices should actually lead to improved performance with lower risk.

I also respectfully submit that people that have the financial ability to invest $150,000 (without borrowing to do so), and those that fall under the current definition of an "accredited investor" are generally capable of deciding whether or not a particular Exempt-Market fund is right for them. If the Exemptions are being abused by the industry (e.g. certain registrants are allowing ineligible investors to rely on the Exemptions), the solution isn't to increase the Exemption limits. Those that abuse the current rules will continue to abuse the new ones while those that actually follow them will be punished.

Individuals in Canada, regardless of their financial sophistication, can easily and quickly open up a discount brokerage account on their own and buy options, derivatives, foreign exchange contracts, use leverage (margin), etc. I believe that they would be better off having access to professional managers, even if those managers offer their products by way of the Exempt Market. People that have the freedom to do dumb things on their own should have the freedom to choose to hire a professional to help them.

2. Not All Private Funds are Inherently Risky

There are existing mutual funds in the Canadian market that invest using risky strategies (e.g. high portfolio concentrations in junior mining stocks). Conversely, there are Exempt-Market funds that are very conservatively managed.

The Value Fund uses a long-only investment style, based on the principles of value investing and does not use leverage. It does not invest in asset-backed commercial paper (ABCP) or offer clients expensive and inferior products like principal-protected notes (PPNs). In effect it operates like a "plain vanilla" mutual fund. The Value Fund has KPMG audit its financial statements and uses CIBC World Markets as its prime broker and custodian. Please don't tar all Exempt Market funds with the same brush as you consider changes to the Exemptions.

3. Reducing Competition

It has been well-documented that the Canadian mutual fund industry has some of the highest asset management fees and MERs in the world. This is clearly the result of our concentrated market structure whereby the vast majority of the investment management firms in the country

are owned and/or controlled by our major chartered banks. Like any rational oligopoly, there is really no incentive for the Canadian banks to compete on fees. In addition, the bank-owned funds create formidable barriers to accessing their distribution systems for independent firms.

Speaking from experience, raising capital is already very difficult for start-up investment funds. During the first consultation session, an OSC staff member stated that the Exempt Market in Ontario alone was estimated to be approximately $45 billion. Any tightening the Exemptions would inevitably lead to even less competition in the Canadian market and steer these clients and their investment capital to the bank-owned firms. Perhaps it was not a coincidence that the larger firms did not appear to be in attendance at the session. I believe that promoting competition in the industry by allowing independent firms to exist and thrive is ultimately good for Canadian investors and the Canadian economy.

4. A Prospectus Provides Little Additional Protection

Having drafted many prospectuses as a lawyer and sat through many drafting sessions as investment banker, I can honestly say that a prospectus provides limited protection for most investors. Most investors don't even read it prior to making an investment decision and for the few that do, many don't understand it. Most prospectuses only get read in great detail by lawyers *after* something has gone wrong.

The Value Fund is offered by way of Offering Memorandum (OM) and when I drafted the OM, I strived to ensure that the disclosure provided to investors was very similar to that contained within a prospectus. A copy of the OM has been filed with the OSC as required and they have every opportunity to review it if they so choose.

I have reviewed other examples of OMs that provide investors with a level of disclosure that is on par with the level of a prospectus. Both OMs and prospectuses contain statutory rights of rescission and investors can sue for a misrepresentation. Perhaps the CSA could consider an "OM exemption" that would allow smaller investment managers to access the Exempt Market provided that the OM contained certain mandated disclosures. In my opinion, from the perspective of Exempt Market fund managers, the reticence to operate as a mutual fund isn't the requirement to draft a prospectus or have it reviewed by the CSAs; rather, it is the ongoing cost associated with complying with the rules that apply to mutual funds.

5. The True Gatekeepers

The Exempt Market is not an unregulated market. Exempt Market funds in Canada are managed by regulated Portfolio Managers (Advising Representatives) who have both a know-your-client (KYC) obligation and a duty to ensure that the investment is suitable for each client. I am convinced that the only way to truly protect the investing public is to keep bad operators out of the industry via the registration system. It is the integrity of the investment manager and the advisor/ dealer that is paramount.

One improvement would be to impose a fiduciary duty on financial advisors as opposed to the current duty to act "fairly, honestly and in good faith". Another very simple way to improve the protections provided to the investing public is to *mandate* that an investment manager (for both mutual funds and Exempt-Market funds) must invest in any fund that they manage and that the size of that investment is a material one to that individual.

I speak from experience when I say that an investment manager with his/her own capital at risk is focused on delivering returns to clients and avoiding excessive risk. By being forced to "eat-their-own-cooking" the interests of the manager and the client are completely aligned and most of the problems that you are trying to address will simply disappear.

Best regards,

Michael P. McCloskey