

February 15, 2012

Via email: dean.murrison@gov.sk.ca

Dean Murrison
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Financial Services Commission
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Dear Dean:

In reference to your letter of February 9th in regards to the proposed changes to National Instrument 45-106 *Prospectus and Registration Exemptions* (NI 45-106) I would make the following comments. It was very difficult for me to answer these questions within the confines of the present rules and regulations. I personally believe that this whole area should be relooked at and that the onus should be put upon properly registered and regulated distributors of these types of products. I believe in a free society that every legal adult has a right to make his or her own decisions and reap the rewards of such or suffer the consequences of such. That it is not up to any governing party to dictate who and who cannot buy specific products which would discriminate against one human being as to another.

I believe for fair and just regulation, but this regulation needs to take place on the manufacturing of product end, and also more importantly, on the distribution network being utilized.

If the sale of these products are restricted as to being sold through the appropriate registered and regulated bodies then I believe then that the capital market and the end consumer will be better served and protected.

These are my thoughts and I take the opportunity of thanking you for your consideration of them.

Yours sincerely,

SENTINEL FINANCIAL MANAGEMENT CORP.



Merlin H. Chouinard
President/Chief Compliance Officer

MHC/sm
Enclosures

CSA Staff Consultation Note 45-401

REVIEW OF MINIMUM AMOUNT AND ACCREDITED INVESTOR EXEMPTIONS

Consultation Note

1. Introduction

Purpose of consultation

Staff of the Canadian Securities Administrators (CSA) are reviewing the \$150,000 minimum amount prospectus exemption (minimum amount exemption) and the accredited investor prospectus exemption (AI exemption) contained in National Instrument 45-106 *Prospectus and Registration Exemptions* (NI 45-106).

We are consulting with stakeholders, including investors, issuers, dealers, and legal and other advisors. This consultation note provides background information and sets out consultation questions for input from stakeholders.

At the conclusion of the review, CSA staff may recommend either retaining the exemptions in their current form or may propose changes.

Reason for review

The global financial crisis and recent international regulatory developments have raised questions about the use of the minimum amount exemption and the AI exemption.

The CSA is engaging in this consultation to identify any issues that stakeholders may have about the use of the exemptions and to obtain information that will assist in deciding whether changes are necessary or appropriate.

Framework for review

In deciding whether changes to the minimum amount exemption and the AI exemption are necessary or appropriate, and if so, in developing recommendations for changes, we will be governed by our regulatory mandate of:

- protecting investors from unfair, improper or fraudulent practices, and
- fostering fair and efficient capital markets, and confidence in those markets.

We will also be guided by the principles that

- regulatory initiatives must effectively address the risks to investors and markets that are identified, and
- the benefits of any regulatory initiative must be proportionate to its cost to industry and the restrictions it imposes on market participants.

Proposals regarding securitized products

On April 1, 2011, the CSA published for comment a proposed new regulatory regime for certain securitized products in a Notice of Proposed National Instrument 41-103 *Supplementary Prospectus Disclosure Requirements for Securitized Products* (NI 41-103 Notice). Among other things, the CSA has proposed amendments to NI 45-106 to create a new regulatory regime for the distribution of securitized products on a prospectus-exempt basis. The new regulatory regime would narrow the class of investors who can buy securitized products on a prospectus-exempt basis, and require issuers of securitized products to provide disclosure at the time of distribution, as well as on an

ongoing basis. The NI 41-103 Notice seeks comment on a number of aspects of the proposal, including whether there are any existing registration categories or registration exemptions that should be modified or made unavailable for the distribution and resale of securitized products in the exempt market.

While the NI 41-103 Notice is focused on the distribution of securitized products in the exempt market, we will consider the comments we received in response to that notice as part of our general review of the minimum amount exemption and the AI exemption. We believe it is important that our assessment of those exemptions be informed by the CSA's proposals concerning securitized products and the comments of stakeholders with respect to those proposals.

2. Principles underlying the minimum amount exemption and the AI exemption

The minimum amount exemption and the AI exemption have been premised on an investor having one or more of:

- a certain level of sophistication,
- the ability to withstand financial loss,
- the financial resources to obtain expert advice, and
- the incentive to carefully evaluate the investment given its size.

Consultation questions

1. What is the appropriate basis for the minimum amount exemption and the AI exemption? For example, should these exemptions be premised on an investor's:

- financial resources (ability to withstand financial loss or obtain expert advice),
- access to financial and other key information about the issuer,
- educational background,
- work experience,
- investment experience, or
- other criteria?

Please explain.

2. Does the involvement in the distribution of a registrant who has an obligation to recommend only suitable investments to the purchaser address any concerns? *It address all concerns as*

per present "rules + regs".

3. Minimum amount exemption

Background

The terms of the current minimum amount exemption, a background discussion of the exemption, and a summary of comparable exemptions under the exempt market regimes in foreign jurisdictions are included at Appendix A.

Issues involving the minimum amount exemption

- **No assurance of sophistication.** The size of investment alone does not assure investor sophistication or access to information, particularly where the minimum amount exemption is used to sell novel or complex products without any accompanying disclosure. At most, the size of the investment is an indicator only of the investor's ability to withstand financial loss.
- **Current threshold for the minimum investment.** The current \$150,000 threshold for the minimum amount exemption was set in 1987 and has not been changed or adjusted for inflation since. The \$150,000 threshold is equivalent to over \$265,000 in 2011 dollars.¹ Some stakeholders have suggested that the \$150,000 threshold is too low and allows unsophisticated, retail investors to participate in the exempt market. Conversely, if the threshold is increased, the exemption may not be available to investors who do not need the protections provided by a prospectus offering.
- **Impact of a minimum amount concept on investment decisions.** An exemption based on a minimum amount invested may cause an investor to invest more than business or investment considerations may dictate solely to meet the threshold; for example, by investing \$150,000 when it may have made more sense to invest only \$50,000. Similarly, a higher minimum threshold may cause an investor to make a single investment of \$150,000 or more when a staged investment in smaller increments may better protect the investor's interests.
- **Use of the exemption to raise capital.** The minimum amount exemption is widely used by issuers to raise capital in some jurisdictions. If the investment threshold was increased or the minimum investment exemption was repealed, this could affect capital raising, especially by small and medium sized enterprises.

Consultation questions

3. Do you have comments on the issues described above?
4. Are there other issues you may have with the minimum amount exemption?

Potential options regarding the minimum amount exemption

Depending on the results of this consultation process, we may propose:

- (1) retaining the minimum amount exemption in its current form,
- (2) adjusting the \$150,000 threshold,
- (3) limiting the use of the exemption to certain investors, such as institutional investors and not individuals,
- (4) using alternative qualification criteria,
- (5) imposing other investment limitations, or
- (6) repealing the exemption.

Consultation questions

(a) Maintain the status quo

5. Do you agree with maintaining the minimum amount exemption in its current form?

I simply do not except the principle of "qualification" for legal advice.

¹ Source for inflation adjustments: Bank of Canada Inflation Calculator (<http://www.bankofcanada.ca/rates/related/inflation-calculator/>)

(b) Adjust the \$150,000 threshold

6. How much should the minimum investment threshold be increased? Would your answer to this question change depending on whether:
- ☒ any disclosure is provided to investors, including risk factor disclosure?
 - ☒ the purchaser is an individual, instead of an institutional investor?
 - the security is novel or complex?
 - the issuer of the security is a reporting issuer?
 - ☒ a registrant is involved in the distribution who has an obligation to recommend only suitable investments to the purchaser?
7. Should the \$150,000 threshold be periodically indexed to inflation?
8. If we changed the \$150,000 threshold what would the impact be on capital raising?

(c) Limit the use of the exemption by individuals

9. Should individuals be able to acquire securities under the minimum amount exemption? Would your answer to this question change depending on whether:
- ☒ any disclosure is provided to investors, including risk factor disclosure?
 - the security is novel or complex?
 - the issuer of the security is a reporting issuer?
 - ☒ a registrant is involved in the distribution who has an obligation to recommend only suitable investments to the purchaser?
10. If individuals are able to acquire securities under the minimum amount exemption, should there be any limitations? *This should be left up to the prudent responsibility of the seller, with all the consequences.*
11. If we limited the use of the exemption to persons who are not individuals, what would the impact be on capital raising? *I suggest this would have a detrimental effect and assumes a "caretaking role" which is not justifiable.*

(d) Use alternative qualification criteria or impose other limitations

12. Are there alternative qualification criteria for the minimum amount exemption?
refer to C(6) & C(7)
13. Are there other limitations that should be imposed on the use of the minimum amount exemption?
N/A

(e) Repeal the exemption

14. Should the minimum amount exemption be repealed? Would your answer to this question change depending on whether:
- ☒ any disclosure is provided to investors, including risk factor disclosure?
 - the purchaser is an individual, instead of an institutional investor?
 - the security is novel or complex?
 - the issuer of the security is a reporting issuer?
 - ☒ a registrant is involved in the distribution who has an obligation to recommend only suitable investments to

the purchaser?

15. If the minimum amount exemption was repealed:

- would that materially affect issuers' ability to raise capital? *Yes*
- is the AI exemption (in its current or modified form) an adequate alternative to the minimum amount exemption? *w/k*

(f) Other options

16. Are there other options for modifying the minimum amount exemption that we should consider?

4. AI exemption

Background

The terms of the current AI exemption, a background discussion of the exemption, and a summary of comparable exemptions under the exempt market regimes in foreign jurisdictions are included at Appendix B.

Issues involving the AI exemption

- **Current thresholds for income and assets.** The thresholds for individuals to qualify as accredited investors were originally set by the Securities and Exchange Commission (SEC) in 1982, and subsequently adopted by the CSA in the early 2000s. The thresholds have not been changed or adjusted for inflation since. Some stakeholders submit that these thresholds are too low by today's standards. The current threshold for an individual's income is \$200,000; in 2011 dollars, the threshold would be over \$443,000 based on 1982 dollars (the year of SEC adoption) or \$245,000 based on 2001 dollars (the year the Ontario Securities Commission first adopted the exemption).² As with the minimum amount exemption, some say these thresholds are too low and allow unsophisticated, retail investors to participate in the exempt market, yet an increase in the thresholds may exclude investors who do not need the protections provided by a prospectus offering.
- **Qualification criteria.** Some stakeholders have suggested that income and asset thresholds are not adequate proxies for sophistication. Individuals may have significant wealth, but may lack investment or other experience that enables them to make an investment decision without the protections afforded by a prospectus offering.
- **Use of the exemption to raise capital.** The AI exemption is widely used by issuers to raise capital. If the exemption was changed or repealed, this could affect capital raising, especially for small and medium sized enterprises.
- **Compliance with qualification criteria.** Regulators have concerns that some individuals purchasing securities under the AI exemption are not, in fact, accredited investors.

Consultation questions

17. Do you have comments on the issues described above?

² Ibid.

18. Are there any other issues you may have with the AI exemption?

Potential options regarding the AI exemption

Depending on the results of this consultation process, we may propose:

- (1) retaining the AI exemption in its current form,
- (2) adjusting the income and asset thresholds in the definition of accredited investor,
- (3) using alternative qualification criteria for individuals,
- (4) limiting the exemption to certain investors, such as institutional investors and not individuals, and
- (5) imposing other investment limitations.

Consultation questions

(a) Maintain the status quo

19. Do you agree with retaining the AI exemption and the definition of "accredited investor" in their current form?

Yes - in line of my other comments

(b) Adjust income and asset thresholds in the definition of accredited investor

20. What should the income and asset thresholds be? Would your answer to this question change depending on whether:

- ☒ any disclosure is provided to investors, including risk factor disclosure?
 - the security is novel or complex?
 - the issuer of the security is a reporting issuer?
- ☒ a registrant is involved in the distribution who has an obligation to recommend only suitable investments to the purchaser?

21. Should the income and asset thresholds be periodically indexed to inflation?

yes

22. If we changed the income and asset thresholds, what would the impact be on capital raising?

Dramatic reduction

(c) Use alternative qualification criteria for individuals

(refer to attached letter)

Alternative qualification criteria for individual investors could be required such as:

- *investment experience* (for example, the investor has carried out transactions of a significant size in securities markets at a given frequency),
 - *investment portfolio size* (for example, the investor's securities portfolio must exceed a specified amount),
 - *work experience* (for example, the investor works or has worked in the financial sector in a professional position which requires knowledge of securities investment), and / or
 - ☒ *education* (such as the investor has completed the Canadian Securities Course, achieved a CFA designation or has received an advanced degree in business or finance).
23. What qualification criteria should be used in the AI exemption for individual investors? Would your answer to this question change depending on whether:
- any disclosure is provided to investors, including risk factor disclosure?
 - the security is novel or complex?

- the issuer of the security is a reporting issuer?
- a registrant is involved in the distribution who has an obligation to recommend only suitable investments to the purchaser?

24. If we changed the qualification criteria, what would the impact be on capital raising?

negative

(d) Limit the use of the exemption by individuals

25. Should individuals be able to acquire securities under the AI exemption? Would your answer to this question change depending on whether:

- any disclosure is provided to investors, including risk factor disclosure?
- the security is novel or complex?
- the issuer of the security is a reporting issuer?

- a registrant is involved in the distribution who has an obligation to recommend only suitable investments to the purchaser?

(e) Impose other investment limitations

26. Should an investment limit be imposed on accredited investors who are individuals? If a limit is appropriate, what should the limit be? Would your answer to these questions change depending on whether:

- any disclosure is provided to investors, including risk factor disclosure?
- the security is novel or complex?
- the issuer of the security is a reporting issuer?

- a registrant is involved in the distribution who has an obligation to recommend only suitable investments to the purchaser?

27. If investment limitations for individuals were imposed, what would the impact be on capital raising?

decrease

(f) Compliance with qualification criteria

An issue with the AI exemption is ensuring compliance with the qualification criteria. One way to improve compliance with the AI exemption would be to require an investor's accredited investor status to be certified by an independent third party, such as a lawyer or qualified accountant.

28. Should this be considered in a review of the AI exemption?

29. Do you agree with imposing such a requirement?

30. Are there alternatives that we should consider?

(g) Other options

31. Are there other options we should consider for revising the AI exemption or for substituting an alternative exemption?

Appendix A

Information on the minimum amount exemption

Current form of the minimum amount exemption

The minimum amount exemption in section 2.10 of NI 45-106 currently reads:

- (1) The prospectus requirement does not apply to a distribution of a security to a person if
 - (a) that person purchases as principal,
 - (b) the security has an acquisition cost to the purchaser of not less than \$150,000 paid in cash at the time of the distribution, and
 - (c) the distribution is of a security of a single issuer.
- (2) Subsection (1) does not apply to a distribution of a security to a person if the person was created, or is used, solely to purchase or hold securities in reliance on this exemption from the prospectus requirement set out in subsection (1).

There are no limitations on the type of securities sold under the exemption, the number of solicitations, the number of purchasers, or on the number of times the exemption may be relied on. No disclosure materials are required to be provided to investors.

Background on the minimum amount exemption

The minimum amount exemption was originally created in 1966 by the Ontario Securities Commission and set at \$97,000 (a figure of \$100,000 less a commission or discount of three percent) and was not available to individuals.

Over time:

- other CSA jurisdictions adopted a similar exemption,
- the exemption was expanded to individuals, and
- the threshold was raised to \$150,000 in some jurisdictions.

For a period from 2001 to 2005, the Ontario Securities Commission eliminated the minimum amount exemption and replaced it with the AI exemption, believing that the minimum amount threshold was not as good a proxy for sophistication as the new accredited investor exemption. With the adoption of NI 45-106 in 2005, the CSA jurisdictions all adopted (or re-adopted) the \$150,000 minimum amount exemption in section 2.10.

Exempt market regimes in foreign jurisdictions

The following summarizes the approach taken to an exemption based on a minimum investment amount in certain foreign jurisdictions.

Jurisdiction	Approach
Australia	Australia has had a minimum amount exemption of A\$500,000 since 1989. ³
United Kingdom	The United Kingdom has had the following minimum amount exemption limits: 40,000 euros (1995), 50,000 euros (2005), and 100,000 euros (since 2010). ⁴
United States of America	<p>The United States Securities and Exchange Commission (SEC) adopted a minimum amount exemption of US\$100,000 in 1979. In 1982, this limit was raised to US\$150,000, so long as the amount was at most 20% of the investor's net worth.</p> <p>With the introduction of the accredited investor exemption in 1988, the minimum amount exemption was rescinded. According to the SEC, it had concerns:</p> <p>...that size of purchase alone, particularly at the \$150,000 level, does not assure sophistication or access to information. While some persons previously accredited would no longer be accredited (i.e., individuals with net worths of \$750,000 but less than \$1 million). . . , many of the persons who used the \$150,000 purchaser item will now become accredited investors by virtue of [the accredited investor exemption].</p>

³ A\$500,000 was equivalent to approximately C\$509,000 on September 15, 2011 according to the Bank of Canada daily currency converter (<http://www.bankofcanada.ca/rates/exchange/daily-converter>).

⁴ 100,000 euros was equivalent to approximately C\$137,000 on September 15, 2011 according to the Bank of Canada daily currency converter (<http://www.bankofcanada.ca/rates/exchange/daily-converter>).

<p style="text-align: center;">Appendix B</p> <p style="text-align: center;">Information on the AI exemption</p>
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Current form of the AI exemption

The AI exemption set out in section 2.3 of NI 45-106 currently reads:

- (1) The prospectus requirement does not apply to a distribution of a security if the purchaser purchases the security as principal and is an accredited investor.

There are no limitations on the type of securities sold under the exemption, the number of solicitations, the number of purchasers, or on the number of times the exemption may be relied on. No disclosure materials are required to be provided to investors.

The definition of “accredited investor” as set out in section 1.1 of NI 45-106 includes, among others:

- (j) an individual who, either alone or with a spouse, beneficially owns financial assets having an aggregate realizable value that before taxes, but net of any related liabilities, exceeds \$1,000,000,
- (k) an individual whose net income before taxes exceeded \$200,000 in each of the two most recent calendar years or whose net income before taxes combined with that of a spouse exceeded \$300,000 in each of the two most recent calendar years and who, in either case, reasonably expects to exceed that net income level in the current calendar year, and
- (l) an individual who, either alone or with a spouse, has net assets of at least \$5,000,000.

Background on the AI exemption

The AI exemption was first enacted by the Ontario Securities Commission in 2001 and replaced the minimum amount exemption. It was enacted with the same thresholds as the current exemption in NI 45-106. A similar exemption was subsequently also enacted in 2002 by the British Columbia Securities Commission and Alberta Securities Commission under Multilateral Instrument 45-103 *Capital Raising Exemptions* (MI 45-103), although MI 45-103 retained the minimum amount exemption of \$97,000. When NI 45-106 came into force in 2005, all CSA jurisdictions adopted the current version of the exemption.

Exempt market regimes in foreign jurisdictions

The following summarizes the approach taken to an exemption based on the nature of the purchaser in certain foreign jurisdictions.