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Gordon Smith  
British Columbia Securities Commission  
P.O. Box 10142 Pacific Centre  
West Georgia Street  
Vancouver, British Columbia V7Y 1L2  
e-mail: [gsmith@bcsc.bc.ca](mailto:gsmith@bcsc.bc.ca)

Me Anne-Marie Beaudoin  
Corporate Secretary  
Autorité des marchés financiers  
800, square Victoria, 22e étage  
C.P. 246, Tour de la Bourse  
Montréal, Québec H4Z 1G3  
e-mail: [consultation-en-cours@lautorite.qc.ca](mailto:consultation-en-cours@lautorite.qc.ca)

for the attention of:

British Columbia Securities Commission  
Alberta Securities Commission  
Saskatchewan Financial Services Commission  
Manitoba Securities Commission  
Ontario Securities Commission  
Autorité des marchés financiers  
New Brunswick Securities Commission  
Superintendent of Securities, Prince Edward Island  
Nova Scotia Securities Commission  
Securities Commission of Newfoundland and Labrador  
Superintendent of Securities, North West Territories  
Superintendent of Securities, Yukon Territories  
Superintendent of Securities, Nunavut

**Re: CSA Staff Consultation Note 45-401 – Review of Minimum Amount and Accredited Investor Exemptions**

By way of introduction, Highstreet Asset Management Inc. (“Highstreet”) is an Ontario based Portfolio Manager, Exempt Market Dealer and Investment Fund Manager. We manage, advise and distribute the Highstreet Pooled Funds.

Our pooled fund clientele includes high net worth private clients who rely on the Accredited Investor exemptions and the minimum amount exemption to purchase units of the funds.

Pooled fund distributions are subject to the minimum distribution exemption and the accredited investor exemption which were introduced as a proxy for client attributes that would alleviate the risk exposure, either through expertise or financial assets tests. Other types of investments that rely on these exemptions to make distributions are known as “capital ventures” and of course, securitized products.

The only common risk in the NI 45-106 exempt markets is the lack of a prospectus or regulatory review and, for some exempt products, an ongoing disclosure requirement.

In our opinion, the diversity of risk and the compensating controls (if any) that these distribution channels exhibit makes a simple or singular answer for the CSA’s questions around the minimum amount or the accredited investor model impractical.

### **Framework for review**

As stated in the Consultation Note, the framework for this undertaking is governed by a mandate to:

- Protect investors from unfair, improper or fraudulent practices
- Fostering fair and efficient capital markets and confidence in those markets

Decisions driven by this review will be guided by:

- Effectively address identified risks to investors and markets
- Cost/benefit analysis of proposed changes

Highstreet will consider those objectives in our discussion below.

Because Highstreet only has experience in the use of the Accredited Investor (“AI”) and minimum distribution rule as they pertain to pooled funds, we will limit our comments to the application of the Rule to our product/business model.

### **Compensating Controls**

Pooled funds are exempt from the prescriptive regulations found in NI 81-101, NI 81-102, NI 81-107 and some sections of NI 81-106 that govern marketing and ongoing disclosure for funds issued under a prospectus. Much of the disclosure required by these regulations accommodates a distribution structure whereby a dealer who is at arms-length from the portfolio manager will be the client’s primary contact. In the past few years there have been a number of regulations that, while more principal based, require anyone who deals with a client to provide comparable disclosures.

Pooled funds distributed in Ontario have a regulatory framework that includes:

- Financial statement preparation and distribution as required under NI 81-106
- Investment Fund Manager registration which includes ongoing regulatory filing relating to the financial strength of the Fund Manager, NAV exception reporting, minimum insurance requirements, annual audited financial statements.
- Registered sales persons under the Exempt Market regime which imposes minimum proficiency requirements for those selling or managing client relationships
- Advisors that are registered as portfolio managers
- Forthcoming regulation regarding performance disclosure and costs under NI 31-103
- KYC information gathering, KYP information dissemination under NI 31-103
- Continuous disclosure of trade matching targets under NI 24-101
- Continuous disclosure on Use of client brokerage under NI 23-102

Funds that are trusts will be governed by a trust agreement and supervision by a trustee. The trust agreement will govern frequency of NAV calculation, investment objective and material changes to the fund.

Pooled funds may also be registered with Canada Revenue Agency as qualified investments for deferred savings plans and subject to the qualified investment restrictions of the Act.

Funds may be structured to address the investment restrictions of Schedule III of the Pension Benefits Standards Act (Canada). This schedule has been adopted by most provinces as prudent investment restrictions for pension plans.

Pooled funds provide a cost effective way for advisors to serve private clients, smaller institutional investors and not for profits. They are a separate distribution chain that permits the advisor to accumulate performance and to ensure the continuity of performance outside of the segregated account world.

Pooled funds allow an investment advisor to have a direct relationship with many clients. They are an acknowledgement that for certain investors, their investment goals are not that different from each other and the benefit of a common investment policy statement executed by a professional advisor will achieve their investment objectives within an economy of scale.

#### **“Life time” vs “one time” client interaction**

The life cycle of the distribution of a pooled fund to a client versus a capital venture distribution is notable. Because the current minimum investment amount and accredited investor rules are only relevant at the time of a distribution, they are a better fit for ‘one off’ opportunities afforded by venture capital distributions and their inherent risk.

Pooled funds, by their nature, are designed to meet the long term needs of a client. Very few if any of our distributions are not based on a client relationship that is predicated on picking an asset mix that will serve the client over an investment horizon.

As noted above, pooled funds may be qualified investments for RSPs, RRIFs and TFSAs that span the life of a client. Trying to fit what is best for the client inside of the constraints of the minimum amount and accredited investor exemptions is often the most challenging task for an exempt market dealer distributing pooled funds. The discussion should be around what is best for the client, not what is allowed because of the legal status of the distribution.

A private client risks losing their AI status at retirement. At this time they are probably not going to have or need annual income of \$200,000/\$300,000 and what may have been \$1 million of investible assets is now funding their retirement. It is completely plausible that there will be some erosion of capital.

Since these clients are now primarily redeemers as opposed to subscribers, this does not have an impact on the client until their asset mix no longer fits their investment horizon or risk profile. If they are no longer accredited, they can only deal with their pooled fund holdings under the \$150,000 dollar rule. "All of a sudden" there is a very significant change in how they can arrange their pooled fund investments. A desire to hold a small exposure to a pooled money market fund to manage risk and short term cash flow may not be possible because such a trade results in an 'illegal' distribution. There is nothing 'fair' in this outcome.

### **Principles underlying the minimum amount exemption and AI exemption**

As described above, Highstreet's experience with the minimum amount exemption and the AI exemption has been that basing these exemptions on arbitrary amounts of income, financial assets or ability to make a large initial contribution have some unfortunate consequences for individual investors that creates risk rather than compensate for it.

#### **Accredited Investor rule:**

The AI exemptions available to individuals use the client's financial attributes as a proxy for the client's ability to withstand or understand the risk in a product distributed under NI 45-106.

It has been our experience that although we document how the client meets an Accredited Investor definition, we do not and we cannot rely on these measures to ensure that our clients understand their own risk tolerance, the risk in a proposed asset mix, how we manage

risk in a fund and the risk/return profile. There is no comfort in quantifying an investor's capacity to withstand loss unless there is an understanding of the investor's willingness to assume risk.

Over the long term relationship that we establish with a client, we reinforce and revisit these concepts at every opportunity.

### **Minimum Amount Exemption**

As discussed in the Consultation Notes, one of the outcomes of the minimum amount exemption is that \$150,000 is an arbitrary number that does not consider the risk of the investment, especially when "it may have made more sense to invest only \$50,000".

For this reason alone, Highstreet would encourage the CSA to consider an alternative exemption to the minimum exemption and would not endorse indexing or increasing this exemption.

### **Alternative considerations**

The Consultation Note provides some interesting concepts that recognize and differentiate risk among such a diverse investment scheme collectively known as the 'exempt market'.

We believe that the CSA is going down the right path in considering the following factors:

- Disclosure, including risk disclosure
- Novelty or complexity of the security
- The reporting status of the issuer
- The obligation to conduct a suitability analysis

To that list we would add:

- Does the security strike a market based NAV

We believe that this factor captures the risk difference between a true 'capital raising' venture and a pooled fund. The NAV requires a daily/weekly pricing mechanism based on an independent, verifiable consensus such as an index. It is a public valuation of a private distribution which is subject, in certain jurisdictions, to an annual audit.

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We thank the CSA for the opportunity to participate in the consultation process and look forward to a continuing dialogue on the exempt market.

Best regards,



Paul A. Brisson  
President & CEO.