

From: Craig Burrows [mailto:craig@craigburrows.ca]
Sent: Monday, February 27, 2012 3:27 PM
To: Gordon Smith
Cc: consultation-en-cours@lautorite.qc.ca; comments@wemaonline.ca; 'Richard Korble'
Subject:

Mr. Gordon Smith
British Columbia Securities Commission
PO Box 10142, Pacific Centre
701 West Georgia Street
Vancouver, British Columbia V7Y 1L2

Dear Mr. Smith,

Please find attached my feedback regarding potential changes to the Accredited Investors and Minimum Investment exemptions.

I believe the CSA has taken strides for the improvement and enforcement of new regulations in the Exempt Market Industry. This growing industry offers investors an opportunity to invest in offers that would normally not be offered by IIROC dealers due to size and / or private placements. While it is important to protect investors from fraud, there also has to be an opportunity for investors to invest in exempt market product. The CSA needs to balance risk with economic growth and access to capital for Canada's small to mid-sized companies. It also must allow regular Canadians to invest in a wider range of product to allow them greater diversity for their financial portfolio given world markets and increasing accountability to have self-directed funds for retirement.

The CSA needs to allow time for new policies to be adopted and enforced in our industry before making sweeping changes that could destabilize the private markets and restrict capital flow. Sincerely,

Craig Burrows
President, Front Row Capital Inc

CC:

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, Northwest Territories
Superintendent of Securities, Yukon Territory
Superintendent of Securities, Nunavut

Dear Sirs and Madams:

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

At this time we wish to provide our comments in respect to the questions posed by the CSA in respect to the review of Minimum Amount and Accredited Investor Exemptions.

We are of the opinion that the issues being addressed here do not stand in isolation but are rather tied into a broader discussion about capital formation and investor protection. We see several fronts where the CSA can help to encourage those goals and other areas where their assistance may not be constructive.

Our overarching viewpoints on the subject are as follows:

1. We feel strongly that the CSA has undertaken great strides to improve matters with Registration reform 31-103 but it has already created enormous change to the marketplace and investment in exempt securities. We feel many of the public interest concerns of the past with misuse of investor exemptions can be adequately addressed through the encouragement and proper oversight of the registrant structures created under 31-103. In our opinion the registrant plays a vital role as gatekeeper to the capital market and ought to be forefront in the distribution of these investments. We feel that further changes to the rules at this stage, prior to letting the new rules the opportunity to work is unnecessary and will further disrupt the formation of capital of small and medium sized issuers in our country.
2. We also feel strongly that, unlike the United States, the pool of venture and start-up capital is not nearly as deep and broad and, as such, Canada needs to encourage all avenues of capital formation from as many participants as possible. Without access to individual investor capital through the exemption framework we fear impairment to our vital small and medium sized business' ability to access capital which of course has detrimental effects to the Canadian economy on the whole.

3. We also feel strongly that exposure to investment opportunities typically available in the exempt marketplace offer a much needed boost to investors' portfolios. Historically these issuers have not had direct correlation to stock and bond markets and often times offer unique and specialized opportunities not available in those markets. Furthermore, often times an investment in a small or medium sized issuer allows an investor a greater insight into the operations and management of their investment due to their size and responsiveness to a small group of investors versus an investment in a face-less multinational company

4. In conjunction with the regulatory changes brought in with 31-103 we also feel that issuers using these "public distribution" exemptions should be required to access their investors only through the services of a registrant. In our view an independent and impartial dealer and registrant plays a vital role in helping investors assess their investing needs and can act on behalf of investors to help them fully understand their investment options and ensure that suitability and prudent investment diversification is employed.

5. Generally speaking we feel that the Minimum Amount (MA) exemption ought to be removed as we feel it serves little purpose and encourages imprudent investment decisions and portfolio exposure. We feel that the Accredited Investor (AI) exemptions are generally fair as they currently stand but that the true measure of amount of exposure to exempt securities ought to be based on a simple Net Asset value. We seek a measure that is less risky for investors, that provides greater diversification and one that is universally adaptable and does not discriminate due to arbitrary levels imposed by regulators.

6. Finally we feel very strongly that issuers accessing exempt markets need to have better disclosure of financial matters continuously and not just at the time of offering and that management of issuers need to provide more transparency and communication to investors during the investment time horizon.

Given these viewpoints please find below our concise answers to the consultation questions.

Consultation questions

1. What is the appropriate basis for the minimum amount exemption and the AI exemption?

We feel that the minimum amount exemption should be eliminated and that the AI exemption could be broadened to include additional criteria, especially educational background to include those with professional designations.

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?

We feel strongly that the involvement of impartial and properly regulated registrants and dealers does address most of the concerns associated with these exemptions.

3. Do you have comments on the issues described in background #3?

We feel that the MA exception should be eliminated.

4. Are there other issues you may have with the minimum amount exemption?

We feel strongly that the MA exemption, regardless of amount, is in conflict with prudent investing principles such as diversification and suitability. The very existence of the MA exemption directs investors and registrants towards make a financial decision to concentrate a large amount of one's investment capital in one company rather than taking advantage of prudent diversification to minimize one's risk. Clearly there is no public interest in having investors scrape up to a minimum amount only to then be exposed to the business fortunes of one issuer. As an Exempt Market Dealer we would have great concerns about concentration and suitability for an investor relying on this exemption alone.

We feel that the MA exemption ought to be replaced and captured within redefined AI and OM exemptions.

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

As mentioned above we feel that the MA exemption encourages improper investment decisions by investors and is unnecessary given prudent changes to the other available exemptions.

6. How much should the minimum investment threshold be increased?

Any increase to the threshold will only exasperate the existing concerns and issues with this exemption. You will be encouraging investors to increase their exposure to catastrophic risk and concentration.

Furthermore, we feel that all sales made through general publicly available exemptions should be conducted through the facilities of a registrant.

7. Should the \$150,000 threshold be periodically indexed to inflation?

No, as discussed above the threshold should not be indexed and should be removed.

8. If we changed the \$150,000 threshold what would the impact be on capital raising?

By eliminating this exemption and with the adoption of an OM exemption by all provinces we would see little impact on total capital raising. We would see more prudent investing and with an increased in confidence and fairness to the marketplace, an increase in capital formation would be expected.

9. Should individuals be able to acquire securities under the minimum amount exemption?

If the exemption is allowed to continue than individuals should be allowed to continue to acquire securities under the MA exemptions.

We feel strongly that issuers ought to be held to higher standards with respect to audit and disclosure and that the distribution through a registrant is essential.

10. If individuals are able to acquire securities under the minimum amount exemption, should there be any limitations?

Given the uniqueness of each investor, any limitations should be based on suitability as determined between the investor and a registrant.

11. If we limited the use of the exemption to persons who are not individuals, what would the impact be on capital raising?

Any changes made that exclude individuals from participating will negatively impact the amount of capital raised. Not a desirable choice given our view on the need for individuals to participate in Canada's venture capital market.

12. Are there alternative qualification criteria for the minimum amount exemption?

We are uncomfortable with this exemption generally, particularly for individual investors. Introducing a more arbitrary or tiered qualification criteria will only increase confusion in the marketplace and leave the market more open for potential abuse of the exemption to fit the needs of unscrupulous issuers.

13. Are there other limitations that should be imposed on the use of the minimum amount exemption?

We feel that the registrant model in place can provide the sober second thought and therefore the regulators need not concern themselves with placing arbitrary limits on exemptions generally.

14. Should the minimum amount exemption be repealed?

Yes.

15. If the minimum amount exemption was repealed:

• **would that materially affect issuers' ability to raise capital?**

No, other exemptions could be employed and new ones introduced.

• **is the AI exemption (in its current or modified form) an adequate alternative to the minimum amount exemption?**

No.

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

No.

17. Do you have comments on the issues described above? See Background 16.

Generally speaking we feel that a properly regulated and registered marketplace for the investment in exempt securities can help to alleviate the concerns behind the issues raised in the Background 16.

We feel that in the absence of proper know your client and suitability work that income and asset tests may be one of the only measureable means of determining the sophistication of an accredited investor; however the correlation is modest in many cases.

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

We have no comment at this time.

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

Yes.

20. What should the income and asset thresholds be?

We are comfortable with the thresholds where they are at, especially in light of suggested greater degrees of disclosure and reporting by issuers to investors and the use of a vigorous and regulated distribution network for these investments.

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

Inflation is not necessarily related to income and asset growth, indexing serves little purpose but to encourage to exclude investors and encourage investors to make false claims about those figures. For example the situation for one that has been an accredited investor and indexing is employed they may run the risk of “falling-out” of that group, clearly with no change their sophistication level.

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

If they are raised you will impact the total investment capital raised by definition, fewer investors will be able to access these issuers and therefore less capital will be allocated.

23. What qualification criteria should be used in the AI exemption for individual investors? As discussed above the current criteria for the AI exemption seems to be a fair balance. Would your answer to this question change depending on whether:

- any disclosure is provided to investors, including risk factor disclosure? No
- the security is novel or complex? No
- the issuer of the security is a reporting issuer? Yes
- a registrant is involved in the distribution who has an obligation to recommend only suitable investments to the purchaser? Yes

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

If it were made more broad and increased the pool of potential AI investors you would raise more capital, if restricted you would raise less.

25. Should individuals be able to acquire securities under the AI exemption?

Absolutely, individuals should be able to acquire securities through a registrant under the AI exemption. We also feel that individuals not at the AI level ought to be able to invest as well through other exemptions including the Offering Memorandum exemption to allow regular Canadians a chance to diversify their portfolios.

26. Should an investment limit be imposed on accredited investors who are individuals?

Given our view on the need for a registrant in these situations, an imposed limit is not in keeping with each unique individual's financial situation, risk tolerance, investment objectives and time horizons. Each investor is unique and arbitrary limits are penalizing.

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

Any limitations would simply reduce the total amount of capital raised, there would be a negative impact. In addition you would be alienating those investors and restricting the public's choice to invest in and support Canada's small and medium-sized businesses and ventures.

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?

By independent third parties being licensed and regulated registrants and dealers that would already be expected and performed during the Know your Client process between registrant and investor. Lawyers and accountants are not necessary and may not be a good judge of investor sophistication and personal financial matters.

29. Do you agree with imposing such a requirement?

Verification would be done by the registrant as we see it. If done by the registrant and not an outside third part we would agree with the requirement. We believe the registrant should be accountable and not shirk their responsibilities to another third party consultant.

30. Are there alternatives that we should consider?

No.

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

No.

