Compliance Support Services

3377 Bristol Dr.
Burlington, ON
L7M 1Y8
Tel. 905-331-0389
Cell:289-208-1979
www.compliancesupport.ca
email: smcmanus@compliancesupport.ca

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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

c/o Gordon Smith
British Columbia Securities Commission
PO Box 10142, Pacific Centre
701 West Georgia Street
Vancouver, British Columbia V7Y 1L2
Fax: 604-899-6814
e-mail: 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
Fax : 514-864-6381
e-mail: consultation-en-cours@lautorite.qc.ca

Dear Sirs and Madams:

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

Compliance Support Services is a legal and regulatory compliance consulting firm offering compliance services and advice to market participants in all registration categories, including exempt market dealers. **Compliance Support Services** has the benefit of both regulatory and industry experience bringing arguably, a highly balanced perspective to the issues raised in the above consultation process. We are grateful for the opportunity to comment on this important initiative.

General Comment on Policy Approach

Before we comment on select issues raised in the consultation, we would like to comment on the general policy approach which seems to be driving the consultation: a concern that investors need more protection than is currently available to them in the exempt market structure.

While recent events require that a certain scrutiny be applied to existing investor protection, we feel it is critically important that the balancing interests of the health of the Canadian capital markets be given at least equal air time in the debate, particularly at this critical point in Canadian and world economic struggles. Regulatory action must not only be reactive (i.e. attempting to protect investors from past transgressions) but proactive and forward-looking. Stimulation of investment and growth must be a priority of governments and any of their delegates and initiatives designed to protect investors must be tempered with this in mind.

Further, given the volatility of the public markets, a situation which many critics say is here to stay for the foreseeable future, consideration ought to be given to the advantages of the “quieter” landscape on the private side and the choice that offers to Canadian investors who haven’t the stomach for the ups and downs of traditional equities. This is not to say that exempt products should be touted as the panacea to public market volatility. But with appropriate risk management measures in place, they can offer a worthwhile alternative or diversification to traditional equity and fund investment.

It is our view that it would meet the ends of both economic stimulus and of providing investors with an alternative approach if we examine the ways in which *more* Canadians can be offered access to the exempt market, rather than fewer. It is our general view then that measures such as increases in minimum investment amounts, increased education and eligibility criteria for investors and yet heavier compliance burdens on market intermediaries are counter-productive to

the prevailing economic demands and ought to be thoroughly weighed against their likely effects before they are implemented.

Minimum Amount Exemption

In our view, the minimum investment threshold should not be increased. Before any change is made to this threshold, it would be useful to determine whether the threshold, which admittedly has been eroded over time by inflation, is *in fact* too low. The consultation paper underlines that this base amount was set in 1987 and has not been changed since. But the question bears asking: is there overwhelming evidence to demonstrate that investors (individual or otherwise) using this exemption are not being adequately protected? Dollar value erosion by itself is not evidence of a decrease in protection, especially when counterbalanced by the massive increase in available research and information available to every investor with the advent of the internet since 1987. It is important here, we feel, not to jump too quickly on the bandwagon of regulatory action in foreign jurisdictions but to look plainly at whether here, in Canada, the threshold does not meet investor protection concerns.

Experience in dealing with purchases under this exemption has, in our view, rarely shown investment by a client who a) misunderstood the investment or b) was unsuitably placed in the investment. As mentioned in the consultation document, the minimum amount exemption, like the AI exemption, is 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.

We believe that the monetary threshold of $150K continues to ensure these underlying premises are met. The erosion to the base amount over time has not changed this fact. The $150K amount, in our view, continues to offer appropriate protection.

As to whether individuals should be permitted to purchase under this exemption, there appears to be no rational basis for prohibiting individuals from making use of this exemption. If they have $150K to invest in one investment at one time it is highly likely (and arguably, Canadian experience has shown) they have a certain level of sophistication, the ability to withstand loss, the resources to get advice and the incentive to evaluate the investment given its size. This

#3377 Bristol Dr., Burlington, ON L7M 1Y8 tel. 905-331-0389, cell 905-875-7219
www.compliancesupport.ca

exemption works well in its present form and there is no supportable reason for changing it, on balance.

Finally, it may be appropriate to index this amount to inflation or to provide for a periodic (every 5 year) increase to reflect inflation or economic growth over that period.

Accredited Investor Exemption

The consultation paper again raises the issue that the monetary thresholds for individuals under this exemption were originally set by the SEC in 1982, and subsequently adopted by the CSA in the early 2000s. 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.

Again, increasing monetary thresholds on the basis of dollar value erosion alone, without evidence of a corresponding actual erosion in investor protection is a high risk policy position to take at a critical time in Canadian economic development. Let us not forget too that the nature and quality of private products and access to information on private issuers has changed dramatically over those years as well.

In our view the model of the Offering Memorandum exemption and the Eligible Investor definition under it is the most appropriate policy direction to take for a variety of reasons.

First, it levels the investor playing field across Canada. Currently, Canadians in most jurisdictions other than Ontario have far easier access to private markets than Ontarians, a precarious state of affairs from the investors' perspective, the issuers' perspective and the Ontario Minister of Finance's point of view, we would think. There is no doubt that such a restrictive approach to the exempt market in Ontario will eventually have a chilling effect on investment and as a consequence, economic growth, given recent upward trends for investing in private markets in Canada overall. One need only look to the 2011 census figures to confirm that western Canada is growing while Ontario is shrinking. Regulatory initiatives that restrict investor and issuer freedom can only be expected to worsen the trend, at least from the perspective on Ontario.

Second, it permits a certain level of investment ($10K) to be made by any investor, regardless of financial "eligibility" so long as certain other criteria are met, such as the delivery of an OM and the signing of a risk acknowledgement. In our view, capping the amount of investment for investors of lower means and sophistication reduces the risk to them while still opening the door to greater private investment. Arguably, a $20K cap would be a more appropriate figure so long as suitable disclosures and offering documents are provided.

Third, it offers investors the option of qualifying as "eligible" if they receive the blessing of an eligibility adviser as defined in s.1.1, in much the same way as the CSA is here suggesting that the Accredited Investor status be certified by a third party.

Fourth, the income threshold is lower ($75K rather than $200K) and the net worth is lower ($400K rather than $1M Financial Assets) for an eligible investor than it is for an accredited investor, providing greater investor access to the exempt market at a time when the economy needs it and investors arguably want it.

If there is a legitimate concern as to whether investors are actually qualifying and whether intermediaries are following the appropriate steps, then investor and participant education are far more supportable options than increasing barriers to the private markets through tighter criteria. It may also be appropriate to "tier" investment options according to whether the issuer of this private offering is a public issuer (and therefore arguably more transparent and less risky) and to increase private issuer disclosure requirements to some extent, for example, by requiring that they contractually agree to provide periodic financial reporting to investors.

Also, the issue of "suitability" is already adequately addressed under NI 31-103. Any intermediary distributing exempt products (unless the Northwest exemption is available or the client is a permitted client and has waived the suitability requirement) must comply with suitability requirements. It is therefore not necessary to build any suitability component into revisions to either the Minimum Amount or Accredited Investor exemptions.

The Minimum Amount and Accredited Investor Exemptions are the most widely used exemptions in Ontario. They also already provide the most stringent eligibility criteria of the many exemptions available under NI 45-106. Tightening of these two exemptions will have the effect of creating a massive imbalance for investors across Canada. In British Columbia for example, by receiving an Offering Memorandum and signing the appropriate risk acknowledgement, an investor can put as much money as he or she sees fit into the private market. However, if the proposed changes take the tack of tightening requirements, this will effectively shut the door for Ontario investors wanting access to the private markets and drive away legitimate private issuers seeking to raise capital in the province. Surely that cannot be helpful to either investors or the capital markets.

We thank you for this welcome opportunity to comment and look forward to further developments in the area.

Yours Truly,

S. A. McManus

Stephanie A. McManus LL. B.
Compliance Support Services

cc. Western Exempt Market Association