



THE INVESTMENT FUNDS INSTITUTE OF CANADA
L'INSTITUT DES FONDS D'INVESTISSEMENT DU CANADA

BY ELECTRONIC MAIL: gsmith@bcsc.bc.ca, consultation-en-cours@lautorite.qc.ca

February 29, 2012

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
Superintendent of Securities, 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
P.O. Box 10142, Pacific Centre
701 West Georgia Street
Vancouver, BC V7Y 1L2

and c/o 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

Dear Sirs / Madames:

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

We are writing to provide the comments of the Members of The Investment Funds Institute of Canada in response to the Public Consultation being conducted in relation to National Instrument 45-106 *Prospectus and Registration Exemptions* (the "Consultation") as described in CSA Staff Consultation Note 45-401 *Review of Minimum Amount and Accredited Investor Exemptions* (the "Note").

We would like to acknowledge and thank the CSA for engaging in this preliminary form of consultation, where broad stakeholder commentary is requested on the "big picture" in order to help formulate the regulators' views on whether reforms are needed at all, and if they are, what they might reasonably look like. This approach is preferable than being able to comment only on proposed rules that CSA staff have

already formulated and published, as those rules may not have had the benefit of a good understanding of cost/benefit or business impact analysis. Early, conceptual consultation should, in our view, lead to a better, more appropriate regulatory framework, and we highly encourage the CSA to carry out consultations in this manner whenever possible.

Although the majority of our Members' business operations are in the retail fund area, complying with the full prospectus disclosure and participant registration system, some Members do participate in distributions which rely on the minimum amount and accredited investor prospectus exemptions. Accordingly we would like to offer our Members' comments on the appropriateness of these exemptions and suggest some improvements to the current rules. Immediately below we set out some general remarks about the exemptions, followed by specific responses to the questions raised in the Consultation.

General Remarks on Prospectus Exemptions

IFIC Members support improved disclosure with respect to investment funds and competing securities products, and believe that investors should receive clear disclosure that provides them with appropriate and relevant information. Such information empowers investors to make informed choices about the various securities that may be recommended to them for purchase. Similarly our Members strongly believe in the value of advice; empirical research shows that Canadian investors who use advisors reap durable economic benefits and are better off than those who choose to invest without advice. As such, for the vast majority of individual investors we believe that advice together with good disclosure is the preferred model for investment.

At the same time, we recognize that there are many types of investors, and the full prospectus distribution route does come with some cost.

There is a segment of investors who are independently qualified or otherwise self-sufficient to conduct or obtain the appropriate due diligence they require to invest and to manage their investments. Whether their self-sufficiency is measured by their business experience, education, size of assets or another criteria that qualifies them to do so, these investors prefer to invest in reliance on prospectus and registration exemptions.

From the perspective of capital markets participants who are seeking investments in their securities, the exemptions provide a cost-effective and efficient avenue to raise capital without the expense and required lead time of a full product qualification and product disclosure process under the current prospectus regime. In an economy such as Canada's where there are many smaller issuers seeking financing for particular projects or other purposes, the exemptions offer a financing alternative to traditional banking relationships. Other countries with such exemptions have made adjustments from time to time, but the exemptions have always been preserved.

This divergence of capital raising needs and ready availability of willing investors, suggests to us the need to preserve choice in the markets. As such, our Members recommend that the CSA not only maintain the current prospectus exemptions, but expand the availability across Canada of the exemptions that are currently in place only in individual jurisdictions.

Review Should Seek National Uniformity of Exemptions

IFIC Members are also proponents of efficient, well-functioning capital markets. Our Members have uniformly remarked that the current review of these exemptions offers an opportunity for the CSA to consider enhancing the uniformity across Canada of the existing set of exemptions. The fact that prospectus exemptions are not uniform in application across the country simply adds complexity and cost for issuers that operate in more than one jurisdiction, which is contrary to the main benefit of the exempt distribution channel. Canadian investors who are qualified to purchase securities under these exemptions should be equally so qualified anywhere in Canada; their status should not depend on their province of residence. As such we hope that one objective of the CSA's current review is to ensure a uniform application (including the uniform expansion) of the exemptions across the country, thereby allowing qualifying investors to benefit from the exemptions equally regardless of their residence.

Qualifications to Permit Use of Exemptions

In addition to our Members' views that the exemptions should be maintained, and uniformly expanded, we also believe that the principles supporting the qualifications to permit use of the exemptions are sound, and should be retained. We believe that the following general principles listed in the Consultation, are the appropriate enduring concepts for determining an investor's status. The specific tests and thresholds that may be used at any time to measure each investor's "score" on these principles are rather arbitrary, open to debate and subject to change over time¹. Accordingly our comments and responses are less focused on the dollar amounts and thresholds of the exemptions and more in the underlying principles.

Fundamentally, an investor who does not have

- 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.

should not be able to invest in reliance on these exemptions.

Responses to Questions Posed in the Consultation

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

As we noted immediately above, we believe that the four principles are the appropriate enduring principles on which these exemptions should be based. We do agree that there must be thresholds although the Consultation is not clear on whether the thresholds would apply each alone, or in some combination.

We do not agree that educational background is a good measure, although investment experience is, and work experience, if generated in an investment firm, may very well be (perhaps the test should be whether the investor is a registrant). Without practical experience, however, the completion of a

¹ We will provide some specific examples later in this letter, in our responses to the questions posed in the Consultation.

program of education does not, by itself, uniformly provide an investor with the appropriate level of sophistication or ability to withstand financial loss.

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?

Yes, the involvement of a registrant who is obligated to recommend only suitable investments does interpose an individual with an over-arching and regulatory responsibility to make only suitable recommendations, although we recognize that an investor is not obligated to adhere to the registrant's recommendations.

3. Do you have comments on the issues [involving the minimum amount exemption] described above?

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

It would be a reasonable expectation that an investor who is about to make a significant amount of money, as is provided in this exemption, would exercise care and caution before making such investment. Dealer firms have robust compliance programs in place, and there is across Canada, a robust enforcement system encompassing IIROC and MFDA rules, and overarching CSA regulations, applicable to dealers and advisors.

5. Do you agree with maintaining the minimum amount exemption in its current form? 6. How much should the minimum investment threshold be increased?

We have responded to these questions in our general comments above.

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

We are not convinced that indexing the threshold to inflation serves any purpose other than to regularly and consistently increase the threshold. This may do no more than continually erode the pool of potential investors who qualify for the exemption, which reduces the value of the exemption to issuers.

8. If we changed the \$150,000 threshold what would the impact be on capital raising? 9. Should individuals be able to acquire securities under the minimum amount exemption?

We have no specific responses to these questions.

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

A fixed exposure limit, perhaps based on a specific percentage of the investor's investable assets, might be a useful addition. This would serve to restrict the individual's investment under the minimum amount exemption to no more than that limit amount.

11. If we limited the use of the exemption to persons who are not individuals, what would the impact be on capital raising? 12. Are there alternative qualification criteria for the minimum amount exemption? 13. Are there other limitations that should be imposed on the use of the minimum amount exemption?

Apart from our stated preference to retain the exemptions essentially as they are, we have no additional responses to these questions.

14. Should the minimum amount exemption be repealed?

We have responded generally to this point in our general comments above. However we would also add that the situation should be different if the securities issuer is a reporting issuer. Adding more criteria to the exemption adds to the complexity of the determination whether a particular individual meets the threshold, which in turn, creates a more difficult to implement compliance regime and a more difficult to manage regulatory oversight process.

15. If the minimum amount exemption was repealed:

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

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

17. Do you have comments on the issues [involving the AI exemption] described above? 18. Are there any other issues you may have with the AI exemption?

Again, apart from our stated preference to retain the exemptions essentially as they are, we have no additional responses to these questions.

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

Our Members believe that the AI exemption and the definition of "accredited investor" should be maintained in their current forms, subject to some minor revisions so that the exemption and definition are not inconsistent between any of the Canadian jurisdictions.

20. What should the income and asset thresholds be? 21. Should the income and asset thresholds be periodically indexed to inflation? 22. If we changed the income and asset thresholds, what would the impact be on capital raising? 23. What qualification criteria should be used in the AI exemption for individual investors? 24. If we changed the qualification criteria, what would the impact be on capital raising?

Apart from our general comments, and our responses to the similar questions raised in connection with the minimum amount threshold, which we would also echo here, we have no additional responses to these questions.

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

Our Members note that the AI exemption already applies to registered persons. Our recommendation would be that an individual who is a “professional” in the securities industry, having access to all of the expertise within his or her firm should be permitted to rely on the AI exemption. The trading frequency test applied in the UK is not, in our view a true measure of an individual’s abilities as an accredited investor; such a test only identifies that investor as being a frequent trader. More consistent with our recommendation is the UK test as to whether the person has worked in the securities industry for a minimum period of time, which we would consider an appropriate qualification for the AI exemption.

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

As we responded earlier in connection with the minimum investment exemption, we would consider it appropriate to add a fixed exposure limit based on a specific percentage of the investor’s investable assets. This would restrict the individual’s investment under the AI exemption to no more than that amount.

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

Apart from our stated preference to retain the exemptions essentially as they are, we have no additional response to this question.

28. Should [requir[ing] an investor's accredited investor status to be certified by an independent third party, such as a lawyer or qualified accountant] 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? 31. Are there other options we should consider for revising the AI exemption or for substituting an alternative exemption?

We do not think that requiring such independent certification would in any way enhance compliance with the criteria, and should not therefore be pursued by the CSA. If an individual is willing to attest that he or she qualifies under this exemption, that should be sufficient. It would not add any additional credibility to the individual’s assertion to have a lawyer or accountant’s signature, as there is no way to verify that the individual was being truthful to that third party. It is much more compelling to require the individual to support their attestations by producing appropriate financial and background documentation to verify their qualifications. Dealer firms must look beyond the checkbox on the application form and obtain and examine financial statements, bank statements and other relevant documentation.

We hope the CSA finds our comments and responses to the questions in the Consultation helpful, and look forward to participating in further consultations with the CSA on these exemptions as this review proceeds through its next stages.

If you have any questions regarding our comments, or would like to discuss any aspect in greater detail, in this letter please contact Ralf Hensel, IFIC's General Counsel, Corporate Secretary and Director, Policy – Manager Issues, by phone at 416-309-2314 or by email at rhensel@ific.ca.

Yours truly,

THE INVESTMENT FUNDS INSTITUTE OF CANADA



Joanne De Laurentiis
President and CEO

JDL:rh