



RAINTREE
FINANCIAL SOLUTIONS

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, Securities Commission of Newfoundland and Labrador, Superintendent of Securities, Northwest Territories, Superintendent of Securities, Yukon Territory, and Superintendent of Securities, Nunavut

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Dear Sirs and Madames:

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

Raintree Financial Solutions (“**Raintree**”) is an Exempt Market Dealer (“**EMD**”) currently registered in BC, Alberta, Saskatchewan and Manitoba with plans underway to expand into Ontario. We are an independent EMD in that we have no financial interests in any product or investment that we offer nor do any of our product / investment offerings have a financial interest in Raintree.

As an EMD, our dealing representatives primarily rely on the Offering Memorandum exemption available under National Instrument 45-106 for distribution of approved issuer securities to clients, however we do have some clients who invest under the current form of Accredited Investor (“AI”) exemption. Raintree does not use or allow our dealing representatives to use the Minimum Amount (“MA”) exemption of \$150,000 for reasons which are articulated later in this discussion paper.

Our philosophy as a dealer is simple in that suitability for the investor is paramount. In our opinion, the fact that we offer only 3rd party securities to our clients removes any product bias or even the perception of such bias. As an added level of protection, our product due diligence process always involves independent, unrelated 3rd party professionals to ensure that suitability of investment is protected at both the introductory and purchase level of investment. As an example of the importance we place on due diligence and finding only suitable products for our investor clients, at the time of preparing this letter Raintree offers only 16 of the over 170 products/companies/offerings we have reviewed and been asked by issuers to provide to investors.

This opportunity being provided to industry participants by the CSA, allowing industry commentary on the current AI and MA investments is of significant value to the investors that we all serve as an industry. Since our over sixty dealing representatives are at the front lines of investor-contact, we believe that they are invaluable in communicating to us what is (or isn't) working to help protect our investor's interests. For that reason, we have encouraged our registered exempt market dealing representatives to respond on an unbiased and independent basis to the CSA's request for comment. Although the opinions of our dealing representatives may not in all circumstances be shared by Raintree, we support their opportunity to voice any concerns they might have on behalf of the investors they represent.

Response to Consultation Questions

Each consultation question below is numbered in accordance with the consultation questions listed in CSA Staff Consultation Note 45-401. We have not answered all of the questions posed by the CSA and have instead focused only on those where we feel our input is both warranted and constructive from an industry protection perspective. In this respect, certain of our positions on certain later consultation questions were articulated in responses to earlier questions, so we have chosen not to duplicate these responses in an effort to minimize redundancy.

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.

To us, the general premise of a “prospectus exemption” is that it allows investors to purchase securities without the substantial levels of disclosure available in a prospectus - disclosure that is otherwise intended to allow investors to make educated investment decisions. Perhaps more specifically, the underlying premise of prospectus requirements is “informed investing” with the assumption being that the investor reads, learns and understands the contents of the disclosure document before choosing to invest. Whereas a prospectus leads to a “high-disclosure” investment, prospectus exempt distributions under National Instrument 45-106 (with the limited exception of Offering Memorandum exemptions) lead to a “low-disclosure” investment. Low-disclosure investments should only be permitted if they limit investor harms and from this basic premise the components we view as fundamental to determining the appropriateness of any low-disclosure investments are (a) trust (b) sophistication and (c) the ability to withstand loss.



While examining the exemptions that are subject to the current review, we have considered certain elements that play into qualifications and have come to a number of rhetorical considerations on whether or not we believe the three fundamental elements of appropriateness are being met. With brevity in mind, we will not provide them all, but instead provide some examples that allowed us to raise our concern:

- i. Does the act of writing a cheque for \$150k typically encourage an investor to do their own due diligence on an investment?
- ii. Do people take an investment more seriously when the subscription costs are high?
- iii. Is a person necessarily sophisticated because of salary alone?
- iv. Is a person necessarily sophisticated because of net worth alone?
- v. Is a person better able to withstand loss based on salary being considered exclusive of net worth?
- vi. What happens when a spouse is considered as part of the asset or income test but is not a joint investor or otherwise consulted about the purchase?

The answers to these questions are obviously not simple, and speak to the significant undertaking being performed by the CSA during this review. For Raintree, the point here is that specific tests such as income, inheritance, education, and work experience, etc. should not be used as *exclusive* determinants for an exemption but should rather form a foundation in the determination of *suitability*, which we view as the ultimate (and ideal “investor-based”) test in any exempt market purchase.

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 believe that the recent work done by regulators to impart greater responsibility on the registrants who deal with investor clients has vastly improved the commercial exempt market distribution process by consolidating the “fundamentals” we referred to into a single concept of “suitability”. At Raintree, our processes (ie. “know your product”), paperwork (ie. “know your client”) and philosophies (ie. independence from investment products) are designed to facilitate a determination of suitability above and beyond whether or not our clients meet an exemption under National Instrument 45-106.

Having said that, we also understand that there may be situations or investment opportunities where it would be reasonable to rely on exemption such as the accredited investor exemption that are perhaps not met under the current parameters of the accredited investor definition. We will address this later on in more detail.

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

This arbitrary amount of \$150,000 would imply that simply having access to that lump sum (which in many cases is only available due to an inheritance, home equity line of credit, or other external financing mechanism) either overrides or presumes risk tolerance, sophistication and the ability to absorb losses when the exact opposite may in fact be true. This, above all else, creates a risk to investors that is disproportionate to the significant investment amount required to qualify for the investment exemption in the first instance.

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

We have two thoughts on this question:

- i. A successful exempt market needs for the protection of the investor to be at least equal to the considerations of the companies raising this capital, which is not always achieved by the MA exemption; and
- ii. Modification of the AI exemption (and/or the definition of “Accredited Investor”) may help off-set any impact created by eliminating the MA exemption.

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

Our base opinion is that the MA Exemption, in its current form, should be eliminated in its entirety because it fails to account for any of the fundamental concepts of suitability. Simply put, the ability of any one investor to purchase \$150,000 or more of any one investment could be entirely circumstantial based on quantity alone, and seems to be directly opposed to the concepts of suitability, diversification, risk mitigation and to some degree, liquidity.

• What if the security is novel or complex?

Our thought here is that it would be too difficult to determine the novelty, uniqueness or complexity of the offering other than through complex applications for exemptive relief. At times, complex or novel investments offer greater protections to investors, but simultaneously confuse them and require greater guidance from registered dealerships and product providers. We believe that the complexity of introducing this concept basically precludes its utility.

We do reiterate our earlier statement that RFS currently does not allow our dealing representatives to use the Minimum Amount (“MA”) exemption as a matter of policy.

17. Do you have comments on the issues described above (regarding the Accredited Investor Exemption)?

Ultimately, we believe that there is merit in the Accredited Investor exemption, however any modification of it will require employing a more holistic approach that recognizes the fundamental need to protect investors and ensure that the investments they make are *suitable* for them.

A few suggestions that apply to our industry model are:

- i. **Income:** There is no de facto correlation between income and investment sophistication nor is there a correlation between income and the ability to withstand losses. To clarify: if two people each earn \$350,000K, but one is debt free while the other lives on credit, they should not have the same suitability analysis. That difference alone illustrates how potentially dangerous to investors the income test can be when used in a vacuum.
- ii. **Financial Assets:** Many investors are now investing in real estate, which if held in a holding company qualifies as a financial asset, but if held personally does not count as a financial asset. This test should be modified to only exclude the primary residence of an investor to allow portfolios to be diversified into real estate holdings without removing these investments from the financial asset test.



- iii. **Offering Memorandum:** The exclusion of the offering memorandum in exemption in Ontario appears to undermine the highest level of protection available to exempt market participants. Of all available exemptions, the offering memorandum exemption is the most likely to ensure that the greatest level of disclosure is provided to investors. Based on the industry model we employ, allowing an unsophisticated investor who has inherited \$150,000 to invest into a single security in Ontario while simultaneously prohibiting sophisticated investors from placing \$10,000 under an offering memorandum appears counterintuitive.

We wish to take this opportunity to thank each of the regulators and the Canadian Securities Administrators for allowing us, and other market participants, the opportunity to provide input and suggestions during the review of these exemptions. For more information on Raintree and its business philosophy as an independent Exempt Market Dealer brokerage, please visit our website at www.raintreesolutions.net.

Yours truly,

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