



Feb 29,2012

To:

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

Subject: CSA staff consultation note 45-401

Background and Conclusions

The purpose of this note is to provide Tralucent Asset Management`s (TAM) views on Minimum Amount and Accredited Investor Exemptions.

Accredited Investor Exemption

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As the staff note has documented, these standards were set many years ago. As CFAs with over thirty years of experience, we observe that the ultimate standard for making sound investment decisions is indeed knowledge, awareness of risks and returns etc, and not the amount of money an entity possesses. We would therefore make the case that rules be tilted towards a knowledge-and skills-based model.

With the advent of NI 31-103, a significant amount of work was done to establish that the CFA designation would become the standard of measuring skills, knowledge and awareness of financial systems.

As a society we have come a long way over the last thirty years. In 1986, there were barely 8000 CFAs around the world. According to the CFA website now there are over 90,000. We estimate there are some 9,000 of them in Canada alone.

A model where investment actions are whetted by CFAs, CFAs registered with the Commission as Portfolio Managers or those individuals that are registered with the Commission as Portfolio Managers would lead to a more sound and functional environment.

We note that the current rules for the Accredited Investor definition do allow for a registered advisor to act on the behalf of fully managed accounts. This definition is not valid in Ontario though. By making it available in Ontario as well, the regulator would be further harmonizing rules throughout Canada. This would also help those corporations that want to raise capital in the capital markets by making such opportunities available to a wider set of the population. There is considerable evidence available that with the aging of the baby boomers there is indeed a significant amount of wealth in the hands of retired people and the elderly so that

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they pass the hurdle of having a million dollars in liquid assets. However, as securities products become ever more complex, many of them may need the advice of registered advisors even more. By doing away with the hurdle of having a million dollars, but ensuring that investors seek the advice of registered PMs, we would be ensuring a more functional investment environment.

This is also an opportunity for the regulator to further harmonize rules throughout Canada. Currently in Ontario, firms registered as PMs cannot offer their pooled funds to ALL of their managed accounts.

Such pooled funds do offer numerous advantages whereby PM firms offer it as a strategy to all of their clients such as Global Equities, Canadian Equities, Corporate Bonds and the like. Pooled funds then allow ALL managed accounts to participate in all investment opportunities on a similar basis. Oddly, in Ontario such pooled funds are only available to those who meet the accredited or the minimum amount exemption thereby creating two classes of investors by regulation even though other subsets of the regulation would like to see all investors being treated equally.

Of course, if such pools were to be available to all the managed accounts on whose behalf the registered advisor is acting, then investors would be treated equally to begin with. Currently, the burden of ensuring all clients are treated equally is borne by the advisor through proper policies and procedures, as well as the regulator who, through sweeps and audits, ensures that the law is upheld. However, the current regulation means extra work for everyone including the regulator. Some may feel that this would even allow mutual fund companies to bypass the prospectus requirement and just have pooled funds for all their clients. We feel such an outcome is very unlikely as most mutual funds companies sell their

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mutual funds through MFDA dealers and brokerage houses and do not have the business model to be offering managed accounts. This carve-out has created inequality amongst provinces, where in all provinces except Ontario PMs can serve their clients in a certain manner, has caused extra commission and allocation costs to the managed accounts that are not accredited, has caused extra costs to comply with regulations and has created more work to for the regulators to ensure clients are indeed being treated fairly.

Minimum Amount

As in the AI exemption, we would like to advocate a knowledge- and skills-based model where registered PMs may decide on behalf of individuals. The minimum should be repealed in cases where fully managed accounts are being acted upon by advisers who are registered as PMs with the respective commissions.

Specific answers to your questions

We now offer specific answers to your consultation questions.

1. The criterion should be based on skills and knowledge. We advocate a model where individuals seek the advice of Portfolio Managers.
2. It is indeed a concern but not one that cannot be easily overcome. By now we do have pretty stringent regulations about collecting KYC info about clients and, through sweeps and audits, the regulator can ensure that securities distributed to clients are indeed suitable. In Ontario there is this fear that registrants should not distribute their pooled funds to even their fully managed accounts unless they are accredited investors because they may not be suitable. However through appropriate KYCs it can be fairly easily ascertained that such funds do meet suitability criterion.

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3. We firmly believe that the staff is on to something very significant when they note that a sensible amount to invest may not be “\$150,000 but less and may be only \$50,000”! We think in many, many cases it is even less. We feel a lot of accounts are simply not diversified well enough and a lack of diversification can lead to significant losses and frustration. Most individuals are simply not qualified enough to make that distinction and often make the wrong choices. If the minimum had been \$50,000 and not \$150,000 we feel there would have been significantly fewer heart aches. As well, the \$150,000 investment does no favors to investors when markets or the fund itself does not do very well. If investors are required to put in that sum, it could be quite a pill to swallow if it is, say, halved. Instead, if an investor can instead put a smaller sum (say, \$10,000) then that investor can better diversify their risk amongst various funds, and not rely simply on the diversification within the fund itself. So, we do advocate a lower threshold.
4. As we articulated above, individuals in general do not have the sophistication to make such decisions. At a time when we did not have 9,000 CFAs in Canada alone, it may have been appropriate to look to means such as a financial threshold to establish such criterion. But, now with a proliferation of CFA and other worthwhile designations, it is appropriate to tilt the rules towards a skills-based model. We advocate that inside fully managed accounts being acted upon by advisors, the minimum be set to as small as \$5,000. In addition, we advocate that if individuals are allowed to act on their own behalf then it be lowered to \$25,000 so that if individuals make mistakes then they are more manageable.
5. As we articulated in point 4, we advocate changing this criterion.
6. We advocate \$25,000 for individuals acting for themselves on the basis that the cost of mistakes would be more manageable. Though, we would prefer to see individuals seek advice on exempt products from registered PMs. It is wonderful that over the years the

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regulators have required an increasing amount of disclosure. We do feel strongly that the vast majority of individuals do not have the time or the wherewithal to understand a lot of disclosures and their context. And, by putting the responsibility on to the registered advisor, the regulator would then be able to hold someone responsible and accountable.

7. As described above, we ought to index awareness, skill and accountability standards as opposed to amounts of money. We are aware that it is a more difficult task but nonetheless achievable. After all, the regulators were able to do it with the advent of NI 31-103 where several skill sets were recognized and emphasized.
8. By lowering it significantly but going through a gatekeeper such as a registered PM, we could make it significantly easier and more effective to raise capital.
9. We have nothing against well meaning individuals nor want to make their lives any more difficult but the sad reality is that the securities evaluation is simply a very complex issue and most, almost 99% of the individuals we come across have neither the education nor the time to evaluate such securities. We therefore advocate that individuals be severely restricted from participating in the exempt market unless there is a bona fide gate keeper. They should have either a managed account with a PM who is then accountable for decisions.
10. If individuals are allowed they should not be allowed to put more than a certain percentage of their assets into any one security. This would lessen the impact of having made a wrong decision.
11. The impact may not be that significant as there is increasing evidence that money management has become and is becoming institutionalized at an increasing rate. It would not surprise us to find out that as is a vast majority of the decisions are being made at the institutional level.
12. We believe we have answered this question in items above.

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13. We believe we have answered this question in items above.
14. We would be in favor of repealing the exemption as it does not serve any particular purpose except to magnify the impact of mistakes made by individuals. To the extent the product is purchased by institutions, they are well protected as they do have the knowledge to make the informed choices.
15. If the exemption was repealed, it would actually make it easier and even for smaller corporations to raise money in the capital markets.
16. The purpose of setting a minimum threshold had been to increase the chances that only more sophisticated investors who are able to assess the product come in. Time has shown that it is not necessarily the case. A high skill level is really the preferable option. We again advocate the use of PM's as gatekeepers for individuals.
17. As in question 16, the purpose of setting thresholds had been to increase the chances that only more sophisticated investors who are able to assess the product come in. Time has shown that it is not necessarily the case. A high skill level is really the preferable option. We again advocating the use of PM's as gatekeepers for individuals. To the extent that most of the capital is raised thru institutions anyway, by using the PM's as gatekeepers for individuals, it may not negatively impact the capital raising by issuers and in fact is likely to make it significantly easier. As Sam Walton used to put it, that one's best customer is an informed customer and the issuers are likely to have an easier time dealing with PM's who are more educated about the subject.
18. We have detailed our issues with the AI exemption as it pertains to the Ontario carve out. We feel strongly that it is causing a significant cost to the investing public in numerous ways. Just imagine a PM shop run by qualified CFA's approved as Portfolio Managers with 300 accounts all being run under the value approach. Well, these 300 people are paying 300 sets of commissions for their portfolios whereas one pooled fund with one set of transaction costs would have sufficed! This is then being repeated

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in a lot of PM places again run by qualified PM's that have been approved. Then there are all those procedures to make sure every client is treated equally and if there is a 'hot' stock it is allocated equally. Whereas just one Pooled fund would have done the trick and the stock whether there were 300 or 5000 shares available be available to all. Ironically, in the same shop it is allowed to place another family that just happens to have a million dollars into a pooled fund and then exemption are available to the family relatives and all. Then there is the other irony: a million dollar account can participate in an exempt product in this shop but not one that is 100,000 dollars even though it is being advised by the same PM! We think such was not the order the OSC had in mind when the Ontario carve out took place. We advocate this carve out be repealed; Ontario PM's be able to set up their Pooled funds open to ALL of their accounts and not just the million dollar ones.

19. We advocate that the definition of AI be modified particularly as it pertains to individual investors. We find that a vast majority of the individuals are not able to evaluate risk and returns adequately, let alone understand the place of a security in their overall portfolio. Sadly, higher levels of income and level of assets give them little protection.
20. We advocate that both these thresholds be eliminated and replaced with gatekeeper PM's who would then be responsible for ensuring suitability. If these PM's are registrants who are distributing their securities, they are naturally obligated to make sure they meet the suitability criterion for the investor. We do not think the last aspect is an issue as all PM's are required to keep KYC information and keep it up to date.
21. As we have observed earlier, income and asset thresholds do nothing more than create a sort of a class distinction and feel indexing them would not serve the purpose that such rules were designed for.
22. By eliminating such thresholds it is likely to have a significantly positive result on capital raising activities as a larger set of population will be able to participate.

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23. As we observed earlier, we find the vast majority of individual investors without proper education to be not adequately equipped to handle disclosures what to talk of dissecting novel and or complex securities. Yet education and knowledge is the only way out. Therefore we would advocate the Regulator to lean and or move into that direction. With the popularity of CFA's and some other equivalent designations, the Regulators task in protecting the investor may be a bit easier. We also advocate the use of a rigorous 'licensing' exam that the Regulator may experiment with where individual investors can seek such 'licenses' much like we have to take prior to obtaining a drivers' license. We are continuously surprised at how complex the securities business has become and how ill equipped the individual investor is in determining the effect of a certain security on his portfolio in a volatile environment and keep thinking in terms of PM gatekeepers.
24. The more educated people we have making capital raising decisions, the better our economies would be at allocating resources. In the long run, by allowing larger set of population to participate then the results would be positive.
25. As you can tell, we are indeed very concerned about individuals purchasing securities under the AI exemption. Additional disclosure, novel or complex security or that it is being purchased from a reporting issuer leaves us very uncomfortable. We do feel it makes a huge difference if there is someone qualified to judge the security's suitability and that should be allowed. Of course under such conditions, then all investors large and small should be treated equally and request that the Ontario carve out be reviewed.
26. Our response to this question is more or less the same as in 25 above.
27. We think the effect would be positive as we make better decisions through the use of more educated decision makers.
28. It would make every one's job easier if we could get Accountants or Lawyers to certify

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the AI for individuals. We advocate that it be considered.

29. We do agree with imposing such a requirement.

30. In addition, there are Revenue Canada Notices of Assessments that reveal levels of Income and may also be considered as options.

31. We believe we have covered most of our points above.

We thank you for giving us the opportunity to express our views. If we can clarify any of our points, please do not hesitate to call us or write.

A handwritten signature in black ink, appearing to read 'Bill Siddiqui', is written over a horizontal line.

Bill Siddiqui, CFA

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