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June 17, 2014

The Secretary
Ontario Securities Commission
20 Queen Street West
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Dear Sirs and Mesdames:

Re: Notice and Request for Comment
Proposed Amendments to National Instrument 45-106 *Prospectus and Registration Exemptions* and Companion Policy 45-106CP Prospectus and Registration Exemptions
Proposed Amendments to OSC Rule 45-501 *Ontario Prospectus and Registration Exemptions*
Proposed Multilateral Instrument 45-108 *Crowdfunding* and Companion Policy 45-108CP *Crowdfunding*

Proposed Form 45-106F10 *Report of Exempt Distribution for Investment Fund Issuers (Alberta, New Brunswick, Ontario and Saskatchewan)* and Form 45-106F11 *Report of Exempt Distribution for Issuers Other Than Investment Funds (Alberta, New Brunswick, Ontario and Saskatchewan)*

(OSC Request for Comment)

A. <u>Introduction</u>

Walton International Group Inc. (**Walton**) welcomes the opportunity to comment on the OSC Request for Comment. Walton is an issuer/promoter of exempt market investment products and Walton Capital Management Inc. (**WCMI**), an affiliate of Walton, is an exempt market dealer (**EMD**) that is registered in all Canadian provinces where it sells Walton's exempt products.

The exempt market plays a crucial role in capital raising in Canada and Walton supports a regulatory regime for the exempt market that provides adequate protection to investors, fair and efficient capital markets and promotes economic growth.

The slow growth of the economy in Canada and around the world has led governments to find ways to spark growth and investment. In particular, governments are focusing much of their efforts on promoting investments in businesses and economic activity. While banks and large investment houses play a significant role in the Canadian economy, they may have less interest in funding small and medium sized enterprises (**SMEs**).

As a result, many companies must seek alternative means to raise capital. The exempt market is integral to these businesses in order to meet their capital requirements. The Canadian Securities Administrators (**CSA**) estimated the exempt market to be over $150 billion in 2011, compared to the public market, at over $60 billion. Clearly, the exempt markets are one of the main engines of growth for the Canadian economy, or, as was stated in an "Op-Ed" article on May 22, 2014 in the Financial Post (by Chuck Strahl, former federal member of parliament and federal cabinet minister), "the exempt market is the flagship of the Capital Markets in Canada".

Awareness of the exempt market has led policy makers to look at ways to increase access to it by issuers and investors. We applaud the Ontario Securities Commission's (**OSC**) recent efforts in this regard, particularly as it relates to its proposed adoption of an offering memorandum prospectus exemption as set out in the OSC Request for Comment (**OM Exemption**).

We submit that the proposed adoption by the OSC of an OM Exemption is one of the most significant regulatory matters to occur in the exempt capital markets in Canada since the adoption by the CSA of National Instrument 45-106 *Prospectus and Registration Exemptions* (**NI 45-106**). This is an opportunity to open up capital markets in Canada in a significant manner, not just to SMEs, but to all capital raising entities irrespective of their size. This could, if handled properly, result in a significant boost, not only to the Ontario economy, but to the Canadian economy as a whole, with little or no increase in risk to Canadian investors. That is why it is important that this be handled by the OSC in an appropriate manner.

The OSC Request for Comment also proposes the adoption of a new Founder, Control Person and Family Exemption, a new Existing Security Holder Prospectus Exemption and a new Crowdfunding Prospectus Exemption. While we support the adoption of new and reasonable prospectus exemptions, based on our experience in the exempt capital markets across Canada, we are of the view that these other new prospectus exemptions will not open up capital markets to SMEs in a material way, and certainly not in the way that an appropriate OM Exemption could. As are result, in this comment letter, we will focus primarily on the OM Exemption proposed by the OSC.

Concurrent with the publication of the OSC Request for Comment, certain members of the CSA (other than the OSC) published Multilateral CSA Notice of Publication and Request for Comment Proposed Amendments to National Instrument 45-106 *Prospectus and Registration Exemptions* Relating to Offering Memorandum Exemption (**CSA Request for Comment**). In the CSA Request for Comment, some members of the CSA propose to adopt the $30,000 Restriction for the OM exemption used in those jurisdictions (see Item C below). We will refer to the CSA Request for Comment below.

B. <u>Commentary on Certain Assumptions Regarding the Exempt Capital Markets</u>

In our experience, a number of general assumptions continue to be made about the exempt capital markets in Canada and certain participants in those markets. During the course of the OSC's review of the exempt capital markets in Ontario and particularly the question of whether they should be broadened, the OSC has appeared to adhere to some of these assumptions. We believe that the OSC has based its approach to the broadening of the exempt capital market partially in reliance on the accuracy of those assumptions. Before we provide specific comments on the proposed OM Exemption, we wish to discuss this further.

1. The Exempt Capital Markets are a "limited" part of the Canadian capital markets.

Many assume that the exempt capital markets in Canada take a backseat to the Canadian public markets in terms of size and impact on the Canadian economy. This assumption may arise from the more "public" nature of the public markets, which, of course, requires its participants to provide ongoing and significant amounts of disclosure to the Canadian public.

However, as we indicated above, the CSA estimated that the Canadian exempt markets raised over $150 billion in 2011, compared to the amounts raised in the Canadian public markets in 2011, at over $60 billion.

In addition, in a recent article in the Canadian Business Law Journal, "The IPO Market in Canada: What a Comparison with the United States tells us about a Global Problem" (Bryce C. Tingle, J. Ari Pandes and

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Michael Robinson (2013) 54:2013 Canadian Business Law Journal), it was stated that, between 1993 and 2000, there was an average of 42.6 IPOs on the TSX each year. From 2000 to 20011 the average was 18.2 IPOs in a year.

Not only are the exempt capital markets in Canada materially important to the Canadian economy (and potentially more important than the Canadian public markets), but it appears that Canadian capital raising entities are turning more to exempt markets and less to public markets for their capital needs.

While one can debate why this is occurring, it is clear that extreme care needs to be taken in the regulation of the Canadian exempt markets to ensure that any such regulation does not hamper these markets by imposing on them unreasonable and unnecessary restrictions that have a materially negative impact on them and the Canadian economy as a whole.

We agree that investor protection is one of the fundamental requirements of modern securities regulation. We are, however, of the view that sufficient regulation is already in place (through the existence of NI 31-103 and NI 45-106) which, if utilized appropriately, will provide more than adequate protection to Canadian investors in the Canadian exempt markets.

2. Eligible Investors are "retail" investors requiring the protections normally afforded to "retail" investors.

It is clear from the OSC Request for Comment that the OSC considers "eligible investors", being the group of investors (in addition to accredited investors) that can invest through the OM Exemption, to be "retail" investors. We believe that the term "retail investors" is a term that is used frequently without appropriate definition. As a result, using the term "retail investors" to describe a particular grouping of investors can hide the true practical issue of whether such grouping requires the protections generally afforded to "retail investors".

We believe that the investors that require the most significant level of protection afforded by securities regulation are those that exist in the "lower" portions of the investing public in terms of income and assets. It is those investors that the primary rules of securities regulation – the prospectus and registration requirements – are meant for. Those are true retail investors.

While accurate statistics vary and are not easy to come by as it relates to the net worth of Canadians, statistics appear to indicate that, based on the income tests set out in the definition of "eligible" investor proposed by the OSC's OM exemption, eligible investors fall within the top 15% of wage earners in Canada.

We believe that this statistic affords some perspective as to whom the OSC is attempting to regulate with the proposed OM Exemption. Should not the top 15% of wage earners in Canada be able to decide for themselves, with minimal oversight from regulators, what to invest in? Our view is yes. Especially as retirees are living longer and the federal and provincial governments are urging Canadians to build their "nest eggs" appropriately in response to the uncertainty surrounding the ability of present day pensions to fund retirement lifestyles.

To be clear, we are in favor of the adoption of an OM Exemption in Ontario. However, we are of the view that the disclosure provided by an OM, the protection afforded by the KYP, KYC and suitability requirements provided for in NI 31-103 and the ongoing disclosure that will be required of entities using the proposed OM Exemption, will be more than adequate to protect "eligible" investors. The other restrictions proposed by the OSC in the OM Exemption (the Related Party Restriction and the $30,000 Restriction as defined below) will only serve to unduly and arbitrarily restrict the top 15% of investors from investing in a manner that they themselves feel is appropriate for them.

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3. Exempt Capital Markets are materially more risky than the Public Capital Markets

We agree that the exempt markets have a level of risk that must be recognized and understood by investors. It is generally stated that this risk primarily arises from the illiquid nature of exempt securities. Exempt market issuers generally are not public entities and therefore the securities issued by them are not freely trading, that is, there are restrictions on when and to whom the securities can be sold by the investor that originally acquired the securities. As a result, the ability of the investor to sell the securities if there is a downturn in the markets or in the fortunes of the particular issuer or because the investor needs the money, is very limited.

However, we feel that it is more appropriate to characterize exempt market risk as constituting a different type of risk rather than a materially higher risk than public markets:

(a) securities of many public entities are not listed. Even though the securities of these unlisted entities are freely trading, there is no market over which they can be traded. In other words they are likely as illiquid as exempt market securities;

(b) securities of many (if not most) listed public entities are very thinly traded, in other words, they have very little liquidity; and

(c) it is generally retail investors that bear the brunt of losses as a result of illiquid or thinly traded public entity stocks (ie, sophisticated investors have better resources and sophistication to determine when to get out of a stock when there is a downturn and better access to facilities to do so quickly).

There have been many "spectacular" disasters in the public markets over the past many years (Nortel and Bre-X to name just two), in addition to down cycles in the public markets (for example, the bursting of the dot-com bubble from 1999 to 2001 and the financial crisis of 2008 and 2009), where billions of dollars have quickly disappeared from the public markets, including in connection with issuers that have widely traded stocks. We suggest that it is retail investors that disproportionately bear the losses that occur in those circumstances compared to institutional and other sophisticated investors. And yet, under Canadian securities laws, because these are publicly listed entities, their securities can be sold to individuals whose income and net worth <u>fall significantly below those of "eligible" investors</u>.

Our view is that exempt markets are no riskier to investors than public markets. As with public markets, the key to protection of investors in the exempt markets is not inflexible arbitrary rules, but flexible principles-based regulation focusing on the suitability of a particular investment for a particular investor.

4. The focus of the OM Exemption and Exempt Capital Markets in general should be on SMEs; Larger companies wishing to raise capital should do so in the Public Capital Markets

Based on OSC Staff Consultation Paper 45-710, OSC Notice 45-712 and the OSC Request for Comment, it appears that the OSC's motivation for proposing to adopt the OM Exemption, and, indeed, the broadening of exempt capital markets in general pursuant to the OSC Request for Comment, is to promote capital raising for SMEs.

We agree that the broadening of the exempt capital markets is crucial for the growth of SMEs across Canada. It appears to us however that the OSC sees the <u>primary purpose</u> for the exempt capital markets to be the provision of early to next stage capital for SMEs and that entities of larger size should look to raise capital in the public markets.

We disagree that entities that are not SME's should, through regulation, be pushed to "go public" and raise their capital in the public markets and, indeed, we do not agree that it should be seen by regulators that it is part of their mandate to do so.

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It should be up to the directors/management/shareholders of each issuer to determine whether they wish for their particular entity to go public. Neither government nor the regulators should fashion regulation in a manner that pushes entities to the public capital markets in order to be able to raise capital for the proper growth of their businesses. Governments and regulators should be agnostic as to how and in which markets public or private companies raise their capital.

Reasons why issuers of any size may not wish to go public can include:

(a) the cost of raising capital in the public markets (especially in an IPO) can be very expensive (ie, multiples of the cost of raising similar amounts of capital in the exempt markets). This cost is borne by the securityholders;

(b) the time frame in which capital can be raised in the public markets (especially in an IPO) can be significantly longer than in which capital can be raised in the exempt markets;

(c) it can be difficult for issuers to attract the attention of registered dealers to sell their product in the public markets, not because the business of the issuer itself may not be profitable or desirable, but because the dealers:

  (i) determine that they cannot gain enough profit from selling the issuer's securities;

  (ii) view the business of the issuer as too risky for the registered dealer; or

  (iii) the business of the issuer or the securities of the issuer are not "plain vanilla common shares" and therefore are not as efficient or easy to sell as certain other issuers or securities;

(d) the ongoing costs and effort of compliance with being a reporting issuer in Canada is significant and continues to increase;

(e) the level of scrutiny by regulators into the businesses of reporting issuers in Canada is significant and continues to increase; and

(f) some management teams/shareholders, even of large companies, simply do not wish to, and choose not to, go public.

Many issuers find it appropriate to go public, and certain industries and businesses find that their business models are conducive to efficient operation in the public markets. However, many do not. Regulators should not place obstacles in the way of such issuers to raise funds in the exempt markets.

5. The Real Estate Industry is materially more risky than other industries that participate in the exempt markets and should be regulated in a more aggressive manner than other industries

Throughout the OSC Request for Comment, the OSC indicates that it has concerns arising from the use of the exempt markets by non-reporting real estate issuers. We note that the OSC:

(a) states that it has "identified certain concerns with the sale of real estate securities by non-reporting issuers in the exempt market" – though it does not state what those concerns are;

(b) states that, "as phase two of the Exempt Market Review", it is proposing to develop tailored disclosure requirements for real estate issuers as it relates to the OM Exemption; and

(c) specifically <u>prohibits</u> the use of the crowdfunding prospectus exemption by real estate issuers.

No suggestion was given in the OSC's exempt market review commentary leading up to the publication of the OSC Request for Comment that the OSC considered the real estate industry to be more risky than other industries or that it was considering prohibiting the real estate industry from participating in a part of the exempt capital markets.

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Our view is that, before the OSC prohibits the use of a prospectus exemption by one particular Canadian industry and indicates that it is going to create special rules for that industry to participate in the exempt markets, it should, at a minimum, publicly identify what those concerns are and, before it presents draft policy in that regard, present independent market evidence demonstrating that the concern is justifiable as compared to other industries and go through a consultation process similar to that in Staff Consultation Paper 45-710.

All industries have risks specific to those industries. We do not believe that the risks specific to the real estate industry are materially worse than risks that are specific to other industries. For example:

(i) the collapse of the "dot-com bubble" or "tech bubble" from 1999 to 2001 resulted in significant losses to investors in the capital markets. Many of the technology entities that raised funds during those times did so in the exempt markets. Many of those entities raised funds (and many are raising funds today) merely on the basis of proprietary ideas/concepts which had/have not been fully developed and/or had/have no short or even medium-term prospect for revenues, let alone profits. In addition, a number of capital raising institutions indicate that a new tech bubble is currently being formed; and

(ii) mining and oil and gas companies regularly raise significant funds, both privately and publicly, for "exploration" plays which are considered to be very high risk investments. In its Exempt Market Review Staff Consultation Paper 45-710 (page 71), the OSC stated that the total capital raised in Ontario in 2011 by non-investment funds in the mining/oil and gas industry totaled approximately \$6.8 billion (25% of the total raised) compared to \$2.2 billion (8%) by the real estate industry. In 2010, these numbers were: mining/oil and gas - \$8 billion (30%) and real estate - \$1.5 billion (5.7%).

Is the OSC considering similar exempt market prohibitions for the high tech or mining/oil and gas industries? If not, why is the real estate industry being singled out when investment in other industries appear to be just as risky?

C. The OSC's Proposed OM Exemption – Significant Concerns with the Related Party Restriction and the \$30,000 Restriction

The OSC Request for Comment indicates that:

(a) registrants that are "related" to an issuer will be prohibited from participating in an OM distribution of the securities of those issuers (**Related Party Restriction**); and

(b) individual investors that qualify as eligible investors (but do not meet the accredited investor definition) will be prohibited from investing more than \$30,000 in investments that utilize the OM Exemption in any 12 rolling month period (**\$30,000 Restriction**). This is not just a restriction on investments in any one entity – this is a restriction on investors themselves that encompasses the entire exempt market in Canada that utilizes the OM Exemption.

In the OSC Request for Comment, the OSC sets out 20 specific questions or requests for comment on the OM Exemption that they wish responders to comment on. We will focus in this letter on our concerns with the Related Party Restrictions and the \$30,000 Restriction and, therefore, the comments in this section relate to those specific questions dealing with those restrictions. We will respond to some of the other questions in Item D. below.

Our specific concerns and comments with respect to the Related Party Restriction and the \$30,000 Restriction are as follows:

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With respect to both the Related Party Restriction and $30,000 Restriction:

1. Existing securities regulation <u>currently provides adequate protection</u> for the concerns the OSC raises in connection with the Related Party Restriction and $30,000 Restriction. The Related Party Restriction and $30,000 Restriction <u>will result in substantially unfair and inappropriate suitability assessments for Canadian eligible investors</u>.

NI 31-103 contains requirements for registrants involved in the sale of securities (including EMDs) to conduct KYP research for each product it sells and KYC research for each client in order to determine whether a particular investment is suitable for the client. If the investment is not suitable, the registrant is required to take steps to indicate to the client that the investment is not suitable for the client. If the client still invests in the product, it does so with the knowledge that the investment is not suitable for it.

Prior to the adoption of NI 31-103, the CSA, including the OSC, specifically "sold" NI 31-103 to the marketplace on the basis that it was "principles-based" regulation and not "rules-based" regulation. The process in the above paragraph was specifically meant to be flexible to allow the registrant to determine what is appropriate or not for a client <u>based on that particular client's circumstances</u>, without having to comply with specific strict rules <u>which may or may not have an appropriate result for a specific client</u>. Principles-based regulation recognizes that a client, with appropriate advice from a registrant, should, depending on his/her financial wherewithal, be able to determine <u>for himself/herself</u> what is appropriate for him/her to invest in. It is clear that a principles-based approach <u>is more fair to an investor</u>.

However, the $30,000 Restriction and the Related Party Restriction are "rules-based" approaches to regulation and are, in the context of the OM Exemption, <u>significant steps backwards</u> from the principles-based approach adopted by the OSC in NI 31-103. Both the $30,000 Restriction and the Related Party Restriction effectively amount to the OSC dictating directly to "eligible investors" that are not accredited investors, what they can and cannot invest in, irrespective of whether such an investment would be suitable for them. So, if an eligible investor that is not an accredited investor determines that he/she wants to invest more than $30,000 in an OM offered product or acquire more than one OM investment that totals more than $30,000 or the registrant advising the client is selling a related party product and is in compliance with current regulations dealing with such circumstance (see Item C.7 below) <u>and</u> he/she and his/her advisor determine reasonably and appropriately (under NI 31-103) that such investments are suitable for him/her, <u>the $30,000 Restriction and/or the Related Party Restriction would still prohibit the investment</u>. This is not appropriate for a number of reasons, including:

(a) it constitutes the OSC adopting additional layers of regulation in circumstances where appropriate regulation is already in place to deal with the specific concern. This adds material cost to the capital market participants, <u>including individual investors</u> and does not add further protection and, in fact, can materially negatively impact investors and other market participants;

(b) it will result in <u>inappropriate and unfair</u> suitability assessments for many eligible investors that are not accredited investors;

(c) as indicated in B.2 above, "eligible investors" fall within the top 15% of investors in Canada from an income point of view. These investors should be able to determine for themselves, with an appropriately prepared offering memorandum and the appropriate assistance of a registrant, what <u>they wish to invest in</u>, especially when governments are urging Canadians to take their retirement savings into their own hands. The Related Party Restriction and $30,000 Restriction will take away material tools available to investors to do this and will send a contradictory message to investors; and

(d) The rules-based regulation proposed by the OSC through the Related Party Restriction and $30,000 Restriction perpetuates the inappropriate and incorrect view that government/regulators know better than individuals what is best for them and must protect individuals from themselves.

We understand that this point has recently been raised with securities commissions and that those

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commissions have responded that NI 31-103 constitutes "registration" regulation while the OM constitutes "issuer" regulation. All experienced participants in the exempt capital marketplace will know that such a response is in no way an appropriate answer to the concerns raised in this Item, as both "registrant" and "issuer" regulation directly impact how issuers raise capital, and the protection of investors, in the exempt capital markets.

As the OSC has not adequately shown, through appropriate studies and research, the "dangers" to the market from the adoption of an OM Exemption that does not contain the Related Party Restriction or $30,000 Restriction, our view is that the adoption of the Related Party Restriction and the $30,000 Restriction will result in the OSC being in non-compliance with its second mandate, the obligation to foster fair and efficient capital markets.

The above items (a) to (d) would not be concerns if the OSC would just allow the principles-based rules set out in NI 31-103 to operate. NI 31-103 has only been in full operation for less than 4 years. That is not adequate time for the market to adjust to it. It is an innovative and effective regulation that responds appropriately to <u>all the needs</u> of the Canadian marketplace. Rather than put in place inflexible rules, the OSC should focus on appropriate guidance to, and work with, the marketplace as it relates to the operation of NI 31-103. Regulators have the power to deal with obvious and blatant breaches of those rules. Issuers and dealers that are complying with the rules should not be punished because others are not in compliance. We request that the OSC let the current system work.

2. The Related Party Restriction and $30,000 Restriction will substantially reduce the capital that could otherwise be available <u>to Canadian exempt market issuers</u> under the OM Exemption

While the OM Exemption will somewhat open up further capital to exempt market issuers, the potential amount of the capital that could be available will be substantially reduced as a result of the Related Party Restriction and the $30,000 Restriction. The OSC has indicated that one of its primary reasons for proposing to adopt the OM Exemption is to facilitate greater access to capital for SMEs. While the requirement to prepare and provide an offering memorandum will be less expensive to an issuer than a prospectus, it will still require resources for the issuer to prepare one properly (which usually requires retaining legal counsel and an appropriate auditing firm). The significantly reduced amount of capital that will be available under the OM Exemption because of the adoption of the Related Party Restriction and the $30,000 Restriction, will result in a competition for those available funds. Those issuers that have more resources will be able to prepare "better" offering memoranda and be in a better position to attract investors, to access those funds and thereby "crowd out" those issuers that have less resources. This will result in those issuers that need the funds the most to be in a worse position, competitively, to attract those funds.

As a result, we are of the view that the Related Party Restriction and the $30,000 Restriction will significantly restrict the usefulness of the OM Exemption for SMEs and, as a result, will not have the impact for SMEs that the OSC is proposing.

3. The Related Party Restriction and $30,000 Restriction will substantially reduce the choices that would otherwise be available <u>to Canadian investors</u> under the OM exemption and thereby impact their ability to diversify their portfolios in an appropriate manner

Appropriate diversification of an investment portfolio is the goal of most Canadian investors. For certain investors, investment in exempt market products, including alternative investments, is a suitable and appropriate way for them to diversify their portfolios. The Related Party Restriction and the $30,000 Restriction will reduce the tools available for many investors to appropriately do that.

By not adopting the Related Party Restriction and the $30,000 Restriction in the OM Exemption, the OSC and the Ontario government could increase availability of different investment products for Canadian eligible investors with little or no increase to the risk in the Canadian capital markets.

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4. **The Related Party Restriction and $30,000 Restriction will result in a material competitive disadvantage for EMDs compared to other participants in the Canadian capital markets**

The main participants in the Canadian capital markets, being securities dealers (**SD**s), mutual fund dealers (**MD**s) and insurance dealers (**ID**s) compete for the same groups of investors, including the group of investors that EMDs can sell to. However, EMDs can only sell to those investors that can avail themselves of prospectus exemptions. This primarily means that EMDs can only sell to those investors who qualify as "accredited investors" or "eligible investors".

While the Related Party Restriction and the $30,000 Restriction will have an impact on SDs, MFDs and EMDs, the SDs and MFDs can always still sell prospectus qualified securities and mutual funds to (i) persons that are not eligible investors or accredited investors, <u>and</u> (i) to eligible investors and accredited investors. In other words, SDs and MFDs (as well as IDs selling investment products) can sell their specific types of products to investors who are the sole target group of EMDs.

However, the converse is not true. The only groups that EMDs can sell to are, realistically, eligible investors and accredited investors. The Related Party Restriction and the $30,000 Restriction will substantially reduce the pool of capital that would have otherwise been available to EMDs in Ontario under the OM Exemption and EMDs will be required to compete with more established and generally better funded groups such as SDs, MFDs and IDs, who will, because of their operations, usually have a larger (though not necessarily better) shelf of products available.

This will create a significant competitive disadvantage for EMDs compared to SDs, MFDs and IDs. We believe this is unfair to EMDs and is unwarranted given the other points made elsewhere in this letter (ie, adequate rules are already in place to address regulators' concerns with the OM Exemption, etc).

This is compounded by the fact that the EMD industry is only a few years old and most EMDs are smaller, less financially strong organizations compared the other categories of registered dealers in investment products.

If the OSC wants to create an effective and protective EMD marketplace, it needs to put the EMDs on a more level playing field from an economic point of view. Implementing the Related Party Restriction and the $30,000 Restriction will negatively impact EMDs from this standpoint. See Item C.7 below.

5. **The Related Party Restriction and $30,000 Restriction could (i) reduce the number of EMDs in the marketplace and reduce competition for the stronger EMDs and choice for investors, and (ii) make it harder for less well financed EMDs to afford appropriate compliance systems and personnel**

A further impact of the competitive disadvantage to EMDs as compared to other capital raising participants, is that smaller, less financially strong EMDs will have a harder time competing against larger and financially stronger EMDs for both clients and dealing representatives. This may result in many such EMDs having to shut down. This will lessen competition for the larger EMDs and lessen choice for investors in the EMD marketplace. This result is not efficient for the marketplace or for investors nor should lessening competition in the capital markets be one of the roles of the regulators.

Even if some of these smaller, less well financed EMDs are able to continue operating, they could have less resources available for systems such as compliance. While compliance systems are crucial for the protection of investors, those systems, including the cost of experienced compliance personnel, are costly. The less resources that an EMD has available to it could result in that EMD not having as robust a compliance system as better financed EMDs and afford less protection for their clients.

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6. **The adoption of the Related Party Restriction and $30,000 Restriction by the OSC will create further disharmony in the Canadian securities regulatory system**

As we indicate in Item C.7 below, an offering memorandum exemption has been available in all other provinces and territories since at least 2005, with some jurisdictions (British Columbia and Alberta) adopting an offering memorandum exemption in 2002. Other than New Brunswick, none of those jurisdictions are proposing to implement a Related Party Restriction. In the OSC Request for Comment, the OSC states that it is basing the OM Exemption on the offering memorandum exemption existing in other provinces "in order to facilitate harmonization". We do not view the adoption of material restrictions such as the Related Party Restriction and the $30,000 Restriction by the OSC as "facilitating harmonization" with the other provinces as it relates to the OM Exemption and we do not believe that the OSC should suggest that harmonization is being achieved through this. This will result in further dis-harmonization in the exempt markets among the provinces.

With respect to the Related Party Restriction:

7. **Related Party Sales are common in the Canadian Capital Markets and have been adequately dealt with in similar circumstances for "related registrants" in other categories of registration without outright prohibitions**

Related Party Sales (defined below) have long been an accepted part of the securities industry in Canada. The securities dealer (**SDs**) arms of the biggest corporations in Canada (including banks) regularly sell their own investment products on a public and exempt market basis. Most large mutual fund dealers (**MFDs**) in Canada are owned by mutual fund manufacturers and sell only their own related product. Many other MFDs sell their own and other manufacturers' products. In addition, while not strictly part of the mainstream securities industry, many large insurance dealers ("**IDs**") in Canada sell their own manufactured investment products.

The current securities rules applicable to SDs, MFDs and IDs engaging in sales of securities of related issuers (**Related Party Sales**) permit those sales to occur provided their processes include one or more of (i) disclosure of the conflict, (ii) consent of the client, (iii) concurrent sale of a portion of the offering by an unrelated registered dealer and/or (iv) independent review of the related issuer product. There is no outright prohibition placed on Related Party Sales by those groups.

It is incongruent and unfair that Related Party Sales by SDs, MFDs and IDs (being a significant portion of sales of investment product on an annual basis) have been allowed for many years involving investors who are much more at risk (ie, true retail investors who do not reach the category of "eligible investors") <u>and yet</u> Related Party Sales of securities under the OM Exemption (to eligible investors – see Item B.2 above), no matter the category of registration of the dealer involved, will be the subject of an outright prohibition.

Any one or more of the safeguards referred to in items (i) to (iv) above have been determined by securities commissions across Canada, including the OSC, to be adequate to mitigate or manage the conflicts arising from Related Party Sales in all other parts of the Canadian public and exempt markets <u>and can be used in a real and meaningful way</u> to mitigate or manage the conflicts arising from Related Party Sales under the OM Exemption.

Our view is that it is inappropriate for the OSC to prohibit Related Party Sales when there is a number of appropriate examples of existing rules for other categories of registrations dealing with the mitigation and management of conflicts of interest in Related Party Sales without the use of an absolute prohibition. We believe that the second mandate of the OSC (foster fair and efficient capital markets) requires it to implement any one or more of these rules first before it determines that an outright prohibition is required.

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Notwithstanding that the other jurisdictions are aware that the OSC is adopting the Related Party Restriction and notwithstanding that the CSA Request for Comment was issued on the same day as the OSC Request for Comment, only the New Brunswick Securities Commission has indicated that it is also proposing to adopt the Related Party Restriction. Clearly the other jurisdictions (constituting the majority of exempt market sales in Canada) do not see a significant concern with the sale of securities under the offering memorandum exemption by related registered dealers. If this restriction is not deemed necessary in these other jurisdictions (which include Alberta, British Columbia and Quebec, being all of the other significant capital raising jurisdictions in Canada), we question why it is deemed necessary in Ontario, especially when such a restriction could have a materially negative impact on capital raising by various legitimate groups in Ontario (see Items C.8 and 9 below).

8. With the adoption of NI 33-301 in late 2010, the CSA required "multiple issuer groups" to form and register EMDs to undertake Related Party Sales of issuers related to those EMDs. It is now inappropriate for the OSC to prohibit those EMDs, in the circumstances of the OM Exemption, from carrying out the activities for which they were required to be formed and registered.

We note that the OSC states as reasoning for the Related Party Restriction: "[w]e have significant investor protection concerns about the activities of some EMDs that distribute securities of 'related' issuers" and "[a]s the [OM] exemption will expand the class of investors with whom an EMD may deal to include retail investors, we are concerned that these issues may be exacerbated if the EMD is related to the issuer. Accordingly, we have proposed that the exemption not be available for a distribution by a registrant of securities of a related issuer."

The OSC has indicated in the past its displeasure with the EMD category of registration. The EMD category was created by the CSA (and the OSC) when NI 31-103 was adopted and the EMD category has only been mandated and full in operation for less than 4 years. As we have discussed earlier in this letter, NI 31-103 created a "principles-based" registration regime. This "style" of regulation (which Walton supports) is one that requires more cooperation among the various participants in the registration marketplace and necessarily will involve a longer period of time for it to achieve the required results. As stated in the article "Principles-Based Securities Regulation" by Christie Ford, Assistant Professor at the University of British Columbia Faculty of Law:

> "…principles-based regulation also requires a relationship between regulator and regulatee that is generally trusting and collaborative, not adversarial or cat-and-mouse."

and

> "The transition to a principles-based approach could be challenging for regulated entities and public companies. As the FSA recognized in an early document, 'Changes in the manner of expression of requirements may impose a burden on businesses … substantive changes … need to be accompanied by reasonable lead times for adjustments to systems and procedures.'"

This was all part of the discussion that occurred among the regulators and the market participants in the time leading up to the adoption of NI 31-103 and was part of the expectation of the participants when NI 31-103 was adopted.

In addition, one of the reasons stated by the CSA for the adoption of NI 31-103 was the regulation of what they referred to as "serial issuers", ie, corporate groups that created and marketed multiple issuers. This resulted in these groups being required to create related EMDs in order to sell the securities of their issuers. We believe that it is now inappropriate for the OSC to prohibit these types of EMDs from, in the circumstances of the OM Exemption, carrying out the activities for which they were specifically required to be formed and registered, especially when:

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(a) as indicated above and in Item C.1, the EMD category of registration has not been given adequate time to appropriately adjust to the "principles based" regulation set out in NI 31-103; and

(b) as indicated in Item C.7 above, there is more than adequate examples of existing rules for other categories of registrations dealing with the mitigation and management of conflicts of interest arising from Related Party Sales without the use of an absolute prohibition.

9. It is efficient and effective (including for investors) for "Multiple issuer groups" to sell their own securities and they should not be prevented from doing so provided they adopt adequate rules and processes to mitigate the applicable conflicts of interest.

The OSC states, as an argument for the Related Party Restriction, "[o]ne of the purposes of the [OM] exemption is to enable capital raising by start-ups and SMEs. It seems unlikely that a start-up or SME would find it worthwhile to establish a related registrant to sell its securities" (emphasis is ours). This statement is surprising and unreasonably dismissive of the potential impact of the Related Party Restriction because it ignores an important and growing segment of the exempt capital raising industry. That segment is multiple exempt issuer groups, such as Walton, where the group "manufactures" and sells (much like mutual fund manufacturers) securities of a number of issuers on an exempt market basis rather than public market basis. Many of these groups participate in the real estate, infrastructure, oil and gas and mining (particularly flow-through structures) and mortgage industries.

For example, Walton creates and markets real estate project investment vehicles (limited partnerships or RRSP eligible corporations) which carry out short to medium term specific real estate investment projects. Other groups create and market multiple entities that build infrastructure projects, such as individual hotels/motels or commercial/industrial buildings. Other groups create and market multiple investment entities that invest in a set amount of oil and gas or mining flow through securities over a defined period of time. Other groups create and market multiple entities that invest in set amounts of mortgages.

Since the 2008/2009 financial crisis, more and more investors have sought out investments of this type, which are generally considered to be alternative investments (that is, alternative to the types of investments generally available in public or even private markets). Some reasons that investors find these investments attractive is that the investments:

(a) have a defined investment objective, such as to build and sell a particular hotel or building, buy and implement zoning changes on a particular piece of land and sell it to a developer, or buy, subdivide and place infrastructure on a piece of land and then sell lots to builders, etc. Many investors prefer these types of shorter term, defined projects and invest in them to diversify their portfolios;

(b) may, in certain circumstances, have low or no correlation with the public markets, that is, they are not necessarily impacted by changes in the economy in the same way that the public markets are and therefore they are useful for diversification of portfolios;

(c) are generally not available in public companies as many of such projects tend to be funded by institutional investors rather than through public vehicles. Recent articles indicate that institutional investors are specifically investing larger portions of their funds in alternative investments; and

(d) if created by established groups, can provide greater comfort to investors as to the potential success of the investments. Returns can never be guaranteed, but investors do have more confidence in multiple issuer groups that have established positive track records than in an entity which is completing such a project for the first time and on a one-off basis only.

Because of the nature of these individual investment structures (shorter term, defined project), their returns on investment are very susceptible to increases in costs. That is why it is generally not efficient for these structures to raise their funds through an IPO which is very costly. In addition, the nature of these

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structures do not lend themselves to effective trading on stock exchanges. As a result, many, if not most, of these structures, raise their capital in the private markets.

Each of the investment structures created by these multiple issuer groups are "start-ups" and most of them are "SMEs" and therefore fit within the purpose of the adoption of the OM Exemption as stated by the OSC.

A number of these structures, like Walton, have found it efficient to form their own EMDs to sell these products. Indeed, as indicated in Item C.8 above, this was one of the stated reasons for the implementation of NI 31-103 – to cause the sales entities in these multiple issuer groups to be appropriately regulated under law. In Walton's case, it also engages third party dealers, including EMDs, to sell its products, but a substantial portion of its sales come from WCMI. WCMI only sells Walton product.

The Related Party Restriction will prevent such groups from selling their own products. This restriction will have a significantly negative and material impact on this particular segment of the exempt market.

Regarding the concerns the OSC may have with Related Party Sales, we point to the arguments made in Items C.7 and 8 above. For example, regarding Item C.7, in response to recent concerns regarding conflicts of interest pertaining to the related party nature of WCMI and Walton, WCMI appointed an "Independent Compliance Review Committee" (**ICRC**) comprising three individuals who are independent of Walton and who collectively have finance, real estate and securities law expertise. WCMI does not sell any Walton product unless this committee reviews and approves the product for sale to investors. The standard of review for the ICRC in relation to a product includes whether the product has a reasonable prospect of meeting its investment objectives and whether the product has a reasonable prospect of being a suitable investment for some clients, including both retail and institutional clients, as applicable. In making that determination, the ICRC reviews and assesses the information contained within the offering memorandum and information sourced by Walton in the drafting of the offering memorandum and the assembly of the financial modeling for the product. In addition, this ICRC also has a mandate to (i) provide governance oversight in connection with WCMI's compliance procedures and systems in accordance with NI 31-103 and other securities legislation, and (ii) provide oversight over proposed material related party transactions and arrangements between WCMI and entities related to WCMI. WCMI also provides detailed disclosure to clients with respect to the related party nature of its sales of Walton product.

We do not understand why the presence of processes and procedures as described above or other methods of mitigating conflicts of interest arising from Related Party Sales as referenced in Item C.7 above are not sufficient to allow multiple issuer groups to sell their own product, especially when Related Party Sales are permitted in other parts of the capital markets. An outright prohibition of such sales will only serve to materially negatively impact the financing of these issuers and the choice available to investors.

10. **Issuers that sell their securities infrequently ("Infrequent Issuers") and do not trip the "business trigger" under NI 31-103 can sell <u>their own</u> securities under the OM Exemption. The risks that the Securities Commissions are protecting investors from with the Related Party Restriction are applicable to those sales as well, yet Infrequent Issuers are permitted to sell their own securities to eligible investors. This creates a further unlevel playing field for EMDs.**

Under NI 31-103, only entities <u>that are in the business of selling exempt market securities</u> are required to be registered as a dealer. The purpose of this "business trigger" is to ensure that entities that <u>trade in securities as a business</u> are registered as a dealer and must comply with the rules applicable to dealers for the protection of investors who acquire securities from them.

However, issuers that sell their securities to others but do not do so as a business are not required to register under NI 31-103. An example is an oil and gas company that wishes to sell some of its securities

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to raise funds to drill a well or to fund some other program. Its business is as an oil and gas company not as a securities dealer. Under Canadian securities rules (including under the proposed rules in Ontario), such a company can sell its securities under an offering memorandum to eligible investors without having to hire a registered dealer to do so. Many Infrequent Issuers do raise funds for themselves in this manner.

However, the risks that caused the OSC to propose the Related Party Restriction in connection with the proposed OM Exemption are just as applicable to Infrequent Issuers and likely more so because they are selling their own securities without being subject to the rules that EMDs are subject to.

We find it inappropriate that these issuers are permitted to sell their own product without having to comply with the training, insurance, KYP, KYC, suitability and other requirements set out in NI 31-103 and yet, EMDs and other registrants that are required to comply with these requirements, are prohibited from selling securities of related issuers under the OM Exemption. This also creates a further unlevel playing field for EMDs.

With respect to the $30,000 Restriction:

11. **The $30,000 Restriction is an arbitrary number. Securities commissions should be required to undertake further research in support of the restriction before they place a material restriction on investing that can have a materially negative impact on markets and the economy.**

The OSC provides no background as to how the $30,000 amount was chosen. The only substantive comment the OSC makes is that "[i]n our view, limits on both eligible and non-eligible investors are appropriate to limit the amount of money that retail investors invest in the exempt market" (emphasis is ours). In the CSA Request for Comment, the CSA (other than Ontario) states that they chose the $30,000 amount because, based on the Alberta Securities Commission's (**ASC**) records over a two year period, the median total annual amount of investments made by eligible investors under the OM Exemption in Alberta was "less than $30,000". The OSC does not indicate whether that was the reason for choosing the $30,000 amount.

The OSC's dual mandate is the protection of investors and fostering fair and efficient capital markets. Our view is that, if the OSC wishes to adopt such a restriction that could materially negatively impact the use of the OM exemption, in order for it to reasonably demonstrate that it has exercised its regulatory powers and responsibilities appropriately, it needs to go beyond simply "its view" and should more appropriately demonstrate (through studies and other much more detailed statistical information beyond that stated in the CSA Request for Comment) why such a restriction is required and, if so, why $30,000 is the appropriate amount. Otherwise, such restriction and amount can only be seen as an arbitrary exercise of the regulatory powers of the OSC. The participants in the capital markets are entitled to such studies in order for them to appropriately respond to the OSC's proposals.

For example, in Annex B to the CSA Request for Comment, it is stated that the average investment size for investors in Alberta in 2011 and 2012 was over $45,000. Why choose median over average? Also, one specific clarification needed is whether, if indeed the OSC relied on the ASC statistics referred to above, the median calculation referred to above is in connection with all investments by an investor irrespective of the number of entities it invested in, or is it only on an entity by entity basis. Without commenting generally on the appropriateness of the methodology used by the ASC, if it is the latter, how could that be seen as an appropriate number as it would not take into account all investments by the investor in all issuers under the OM exemption each year? The actual median number using the former would always be higher and would be a more accurate representation of how much individuals invest in the exempt market under the OM exemption. This is just one item of many that the OSC would need to research to appropriately demonstrate why this restriction is necessary and why $30,000 would be an appropriate amount.

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12. The $30,000 Restriction will create a disincentive for dealers to sell OM exempt product <u>which will lessen the availability of capital for issuers and choice for investors</u> and could result in OMs being sold by issuers <u>without the benefit of registered dealers thereby adding investor risk to the capital markets</u>.

The OSC states that one of the main reasons for its adoption of an OM Exemption is to facilitate capital raising for SMEs. As indicated in Item B.4. above, it can practically be difficult for new and smaller issuers to attract the attention of registered dealers to sell their product. This may not be because the business of the issuer itself may not be profitable or desirable, but because the dealers have determined that they cannot make enough profit from selling the issuer's securities.

The adoption of the $30,000 Restriction will make it even more difficult for SMEs to attract the attention of registered dealers to sell their product as the dealer's ability to profit will be lessened (because of the limit on purchases that clients can make in the OM exempt market as a whole) and may not adequately offset the costs and time involved in the due diligence required to meet their KYP obligations before they sell the product.

This will result in some issuers not being able to raise sufficient capital to fund their businesses through the OM Exemption and therefore abandon or not undertake an offering. This, in turn, will artificially lessen investment opportunity for investors.

This could also result in issuers attempting to sell their own product through an OM offering (assuming they don't trip the "business trigger" under NI 31-103), without the use of a registered dealer, which is a result that actually <u>adds investor risk</u> to the marketplace. While NI 31-103 does contemplate the sale of exempt securities by issuers without the use of a registered dealer provided the "business trigger" is not tripped, we suggest that the OSC should not be putting rules in place that results in the promotion of sales without the use of a registered dealer. This would not be a concern if the $30,000 Restriction is not adopted. We suggest that the OSC consider the alternatives in this circumstance and consider which is better for the marketplace: (i) no limit but sales through a registered dealer – which we indicate elsewhere will add very little or no risk to the marketplace, or (ii) a limit which will promote sales to eligible investors without a registered dealer?

13. The $30,000 Restriction <u>could lead to inappropriate behavior by some EMDs and Dealing Representatives</u> in relation to commissions and suitability for clients.

The OM Exemption will open up, for EMDs and other registered dealers, a larger market of potential investors (eligible investors that are not accredited investors). However, the actual amount that each such investor can invest in the OM market in any 12 rolling month period will be restricted to $30,000. This will naturally restrict the amount of commissions that a dealing representative in an EMD can earn from any one such client. This could result in some less experienced or less compliance minded dealing representatives to influence their clients to invest in an OM product that has a greater benefit (ie, commissions) to that dealing representative but may be less suitable for the client (but still suitable) than another product that has a lower commission.

While blatant examples of this behavior should be able to be caught by the compliance personnel of EMDs, it may be difficult for compliance personnel to notice such behavior in more subtle situations, especially if the compliance resources of the EMD are already strained.

14. The $30,000 Restriction creates a significant practical problem for some eligible investors as to which OM exempt product they should invest in and <u>could result in such investors investing in less suitable product</u>.

The $30,000 Restriction prohibits eligible investors that are not accredited investors from investing in more than $30,000 under the OM Exemption in any 12 rolling month period. The practical result of the

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12 rolling month requirement is that investors that wish to invest the full $30,000 amount in any such 12 month period in OM offerings may:

(a) place the full amount in a product that it finds suitable and desirable and then miss out on a better opportunity that may come out a number of months later but which is no longer available after the end of the 12 rolling month period; or

(b) place less than the full $30,000 in a more suitable and desirable product in the beginning of the 12 month period because the investor hopes to find another suitable product later on which never materializes.

This could actually result in investors investing in less suitable product than they would have if they could invest more than $30,000. This will not lead to fair and efficient markets and it is, we submit, not in the mandate of the OSC to implement regulation that could harm investors in this manner.

15. The $30,000 Restriction will favor exempt market issuers that issue RRSP eligible securities or securities with other tax incentives over exempt market issuers that do not issue such securities. It will also favor exempt market issuers that issue such securities in the first 60 days of the calendar year over those that do not.

Many investors prefer to invest a portion of their annual investment cash in RRSP eligible securities and/or in other securities that issue securities with other tax incentives (ie, flow-through securities). The $30,000 Restriction and the fact that most tax beneficial investments occur in the first 60 days of the calendar year will result in a "rush for capital" in the first 60 days of the calendar year by exempt market issuers that issue such securities under the OM Exemption.

This will mean that exempt issuers that do not issue securities with tax incentives may also have to complete their OM offerings during that time period. They will have to compete with such tax beneficial issuers for a share of their capital. This could put them at a competitive disadvantage for that capital.

This will also prejudice issuers that issue securities on a regular basis over the course of the year or those that simply need to raise capital at a time other than the first 60 days of the calendar year.

This will not lead to fair and efficient capital markets. It is not in the mandate of, and it is inappropriate for, the OSC to implement regulation that favors capital raising by one type of exempt market issuer over another.

D. Other Comments on the Proposed OM Exemption

Below are responses to some of the specific requests for comment contained in the OM Prospectus Exemption section of the OSC Request for Comment. The numbering below corresponds to the number in the OSC Request for Comment, though some portions of the questions have been removed for brevity.

1) What else could we do to make the OM Prospectus Exemption a useful financing tool for start-ups and SMEs?

For all of the reasons indicated above dealing with the restrictions that they will place on the ability of start-ups and SMEs to raise capital in the exempt market place, do not include the $30,000 Restriction or the Related Party Restriction when the OM Exemption is adopted.

2) Should we impose a cap or limit on the amount that a non-reporting issuer can raise under the exemption?

No. This would create an inflexible rule that would be inconsistent with the rules currently in place. As indicated above, clearly Canadian issuers are moving more and more to the exempt markets to raise their

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capital. We have listed above potential reasons as to why issuers are doing that. It is clear that the exempt markets are crucial to the health and growth of the Canadian economy. We do not believe it to be in the mandate of any securities regulator to take steps to restrict the growth of any legitimate market in Canada. The rules currently in place (or proposed to be put in place) relating to OM disclosure, ongoing disclosure requirements for non-reporting issuers to provide certain disclosure and the requirements for registered dealers to assess suitability of investments are more than adequate to protect investors and the markets.

3) Should we vary the requirements of the OM Prospectus Exemption to be different (for example, disclosure requirements) depending on the issuer's industry, such as real estate or mining?

No. The current form of OM, with its certificate requirement to disclose all material information with respect to the issuer and its securities, is sufficient and flexible. If the information is material, it is already required to be disclosed. Adding further form requirements would only serve to (i) make OMs longer, and (ii) create inflexible rules that might cause disclosure to be made that is immaterial, confusing or possibly misleading.

4) We have identified certain concerns with the sale of real estate securities by non-reporting issuers in the exempt market. As phase two of the Exempt Market Review, we propose to develop tailored disclosure requirements for these types of issuers. Is this timing appropriate or should we consider including tailored disclosure requirements concurrently with the introduction of the OM Prospectus Exemption in Ontario?

Our view is that it is inappropriate for the OSC to focus on the real estate industry when other industries carry just as much risk. This is especially so when the OSC has declined to indicate what its concerns are with the real estate industry. See Item A.5. above. This also applies to the OSC's suggestion regarding creation of a different set of disclosure rules for real estate issuers. See 3) above. Additionally, our view is that the OSC should not create any such regulation on a piece-meal basis. It should present all of its proposed rules at once (ie, the OSC Request for Comment should have been accompanied with the proposed form requirements). How can market participants comment appropriately on these rules when they have not yet been made aware of what all the rules are?

7) Should there be a limit on the offering period? How long does an OM distribution need to stay open? Is there a risk that "stale-dated" disclosure will be provided to investors?

No, there should not be such a limit. We do not understand what regulatory purpose would be served by putting limits on the period of time an OM can remain open. The materiality certificate will require amendments to be made to the OM if any of the information contained in the OM becomes materially incorrect. Adding a time limitation would be duplicative and would only limit issuers unnecessarily.

8) Do you agree with our proposal to prohibit registrants that are "related" to the issuer (as defined in National Instrument 33-105 *Underwriting Conflicts*) from participating in an OM distribution? We have significant investor protection concerns about the activities of some EMDs that distribute securities of "related" issuers. How would this restriction affect the ability of start-ups and SMEs to raise capital?

No. This would significantly restrict the ability of some start-ups and SMEs to raise capital and would restrict investors unnecessarily. See our commentary in Items B and C above.

9) Concerns have been raised about the role of unregistered finders in identifying investors of securities. Should we prohibit the payment of a commission or finder's fee to any person, other than a registered dealer, in connection with a distribution, as certain other jurisdictions have done? What role do finders play in the exempt market? What purposes do these commissions or fees serve and what are the risks associated with permitting them? If we restrict these commissions or fees, what impact would that have on capital raising?

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This should not be restricted. Finders play an important role in the access of capital, especially in the exempt markets. Adequate rules are already in place to deal with the concerns set out above provided they are enforced properly. In our view, the concern lies in inadequate enforcement. Issuers and dealers that are following the rules should not be punished because others are not.

10) We have proposed changing the $400,000 net asset test for individual eligible investors so that the value of the individual's primary residence is excluded, and the threshold is reduced to $250,000. We have concerns that permitting individuals to include the value of their primary residence in determining net assets may result in investors qualifying as eligible investors based on the relatively illiquid value of their home. This may put these investors at risk, particularly if they do not have other assets. Do you agree with excluding the value of the investor's primary residence from the net asset test? Do you agree with lowering the threshold as proposed?

No. The odd result of this is that persons who do not live in a house that they own and have put their investments in other items (which may be just as illiquid as a primary residence, like other houses which they do not live in, land, art, cars, jewelry, etc) can count these assets towards the $250,000 net asset test and invest in these types of securities, whereas those individuals who have decided to invest in a primary residence, may not be able to do so. We cannot see how that is a just or appropriate result.

12) Do you support the proposed investment limits on the amounts that individual investors can invest under the OM Prospectus Exemption? In our view, limits on both eligible and non-eligible investors are appropriate to limit the amount of money that retail investors invest in the exempt market. Are the proposed investment limits appropriate?

No. See our commentary in Items B and C above.

13) Current OM disclosure requirements do not contain specific requirements for blind pool issuers. Would blind pool issuers use the OM Prospectus Exemption? Would disclosure specific to a blind pool offering be useful to investors?

Blind pool issuers do use the OM prospectus exemption. Our initial reaction is that no specific disclosure requirements are needed for blind pool issuers. As indicated above, the current form of OM, with its certificate requirement to disclose all material information with respect to the issuer and its securities, is sufficient <u>and flexible</u>. If the information is material, it is already required to be disclosed. Adding further form requirements would only serve to (i) make OMs longer, and (ii) create inflexible rules that might cause disclosure to be made that is immaterial, confusing or possibly misleading.

14) We are not considering any significant changes to the OM form at this time. However, we are aware that many OMs are lengthy, prospectus-like documents. Are there other tools we could use at this time (short of redesigning the form) to encourage OMs to be drafted in a manner that is clear and concise?

OMs are long for two reasons (i) because the form requirements for OMs are inflexible and arbitrary – especially as it requires that disclosure follow the form in the order that is set out in the form, and (ii) because of the materiality certificate. The form should be redrafted in a manner that promotes flexibility in disclosure provided the materiality requirement is satisfied. This may allow for more concise disclosure. However, the requirements of materiality (which are crucial for investors) do result in longer disclosure for non-commodity type businesses. Liability for misrepresentation lies with the issuer, directors and officers of the issuer and the promoter. The regulators are in no position to arbitrarily shorten OMs when doing so may put these groups at risk personally.

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E. <u>Other Comments on other Parts of the OSC Request for Comment</u>

Crowdfunding:

While we anticipate that the proposed crowdfunding prospectus exemption will likely not play a role in Walton's capital raising efforts, we disagree with the proposal to exclude real estate issuers that are not reporting issuers from the definition of eligible crowdfunding issuers. The reasons for our opposition are the same as those set forth in Item B.5 above. Again, all industries have risks specific to those industries and we do not believe that the risks specific to the real estate industry are materially worse than risks that are specific to other industries.

Proposed Annual Audited Financial Statement Obligation for OM Issuers:

We are concerned with the requirement to provide annual audited financial statements within 120 days from the end of the issuer's financial year end. We recognize that 120 days from the end of the issuer's financial year end is the deadline required for "venture issuers" under securities legislation but note that many provincial corporate statutes, including the *Business Corporations Act* (Alberta) only require corporations to table at their annual shareholder meetings annual financial statements for a period that ends not more than six months (180 days) after the corporation's year end.

We believe it is not appropriate to elevate users of the OM Exemption to the filing requirements of venture issuers in this regard and propose that the 180 days provided in the corporate statutes is a more suitable deadline.

Also, given the deadlines for the preparation of audited financial statements for public entities, it may make sense to have a later deadline for non-reporting OM issuers, to stagger the timing for the resources needed from auditors to prepare audits for the financial statements for those entities.

Proposed Requirement for Notice of the Occurrence of Certain Events:

We are not opposed to a requirement to give notice under the OM Exemption of the occurrence of the events set forth in proposed Section 2.9(17.9) but request that the OSC provide guidance on how such notice should be made available and its form and level of detail.

F. <u>Conclusion</u>

As indicated above, we applaud the proposed adoption by the OSC of an offering memorandum exemption. However, the Related Party Restriction and the $30,000 Restriction that the OSC proposes to place on the proposed OM Exemption will, among other things:

(a) add further layers of arbitrary regulation when the current regulation is adequate to deal with the regulatory concerns;

(b) significantly limit its effectiveness as a capital raising tool for start-ups and SMEs;

(c) significantly limit the effectiveness of the principles-based regulation previously provided in NI 31-103 is it relates to the exempt capital markets;

(d) limit and prevent investors from investing in products that may be suitable for them or that may result in an appropriate diversification of their portfolios;

(e) reduce the number of EMDs in the marketplace and reduce competition for the stronger EMDs and choice for investors;

(f) make it harder for less well financed EMDs to afford appropriate compliance systems and personnel;

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(g) create a competitive disadvantage for EMDs;

(h) favour certain exempt issuers over others; and

(i) create further disharmony in the Canadian exempt markets.

A significant opportunity is available to the Province of Ontario to open up its exempt capital markets in a significant manner with little or no increased risk to investors. This can be achieved by:

(i) the adoption of the proposed OM Exemption without the adoption of the Related Party Restriction and the $30,000 Restriction; and

(ii) the continued appropriate application of the principles-based rules contained in 31-103.

As we discussed above, both NI 45-106 and NI 31-103 contain adequate regulation to deal with the concerns that the OSC may have regarding the OM Exemption. Appropriate use of, and enforcement under, those rules will allow the OSC, in the context of the OM Exemption, to adequately protect investors and foster fair and efficient capital markets without having to resort to the implementation of the Related Party Restriction and the $30,000 Restriction.

We would be happy to discuss our comments with you. Please do not hesitate to contact us if you have any questions.

Yours truly,

WALTON INTERNATIONAL GROUP INC.

Mark McKenna
President

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