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BY E-MAIL

Alberta Securities Commission
British Columbia Securities Commission
Manitoba Securities Commission
New Brunswick Securities Commission
Securities Commission of Newfoundland and Labrador
Registrar of Securities, Department of Justice, Government of the Northwest Territories
Nova Scotia Securities Commission
Registrar of Securities, Legal Registries Division, Department of Justice, Government of Nunavut
Ontario Securities Commission
Prince Edward Island Securities Office
Autorité des marchés financiers
Saskatchewan Financial Services Commission
Registrar of Securities, Government of Yukon

Dear Sirs/Mesdames:

Proposed National Instrument 45-106 - *Prospectus and Registration Exemptions*

We are writing in response to the Canadian Securities Administrators' ("CSA") Request for Comment in respect of Proposed National Instrument 45-106 – *Prospectus and Registration Exemption*s ("NI 45-106" or the "Proposed Rule") published December 17, 2004.

We strongly support the policy of harmonizing securities laws across Canada to make it easier and less costly for investors and issuers of securities to operate in an effectively regulated and competitive marketplace. However, we are concerned that the large number of jurisdiction-specific exceptions from the harmonization efforts provides little disincentive for individual jurisdictions to subsequently diverge from the "harmonized" rule. We are of the view that the fewer jurisdictional exceptions in the initial version of the Proposed Rule, the less likely jurisdictions will be to introduce further individual exemptions.

We note that for the most part our comparisons to current Canadian legislation use the current law of Ontario as a base.

Part 1: Definitions and Interpretation

(a) *Canadian financial institution*

We submit that the proposed new definition of a *Canadian financial institution* should be revised to require that a financial institution must be authorized to carry on business as a specified form of entity in Canada in order to benefit from treatment as an *accredited investor*. The analogous exemptions in Ontario Securities Commission ("OSC") Rule 45-501 – *Exempt Distributions* ("Rule 45-501") specifically links the legislation under which the accredited investor must be qualified to carry on business in Canada to the activity performed by the *accredited investor*. In order to avoid a potential interpretation of the definition as an entity merely authorized to carry on business in a jurisdiction of Canada (which would presumably include authorized to carry on business under corporate legislation), we submit that the part (c) of the definition of *Canadian financial institution* be revised to ensure that, for example, a trust company must be qualified to do business as a trust company rather than simply be authorized by an enactment to carry on business.

(b) *Accredited investor*

We wish to comment on certain aspects of the proposed definition of *accredited investor*. Part (e) of that definition provides that, except for a former limited market dealer, any individual who was once registered in a jurisdiction of Canada as a representative of a registered adviser is treated as an *accredited investor*. This provision is consistent with the current position under Rule 45-501. In circumstances where an individual's registration is terminated because of wrong-doing, in our view securities regulation should not afford such individual continued treatment as an *accredited investor*. Although it is arguable that securities regulation should not be concerned with protecting such an individual in his or her investment activities, by qualifying as an *accredited investor* such an individual will continue to enjoy access to investment prospects that are not available to the general public. We recommend that the definition should exclude from treatment as an *accredited investor* any individual whose registration as a representative of an adviser was terminated because of wrong-doing.

We support the expansion provided in part (l) of the definition of *accredited investor*. Compared to the current asset test applicable to an individual investor, the revised definition allows an individual who has substantial net assets (in excess of $5 million), but whose assets are not largely comprised of financial assets, to qualify as an *accredited investor*.

With respect to charities registered under the *Income Tax Act* (Canada), part (r) of the definition of *accredited investor* introduces a new requirement that such charities obtain advice. Under the current definition in Rule 45-501, any registered charity qualifies as an *accredited investor*. The new definition would require such charities to obtain advice from an eligibility adviser or adviser registered under the law of the jurisdiction of the charity. We are unaware of general abuse under the current regime and submit that securities regulation should emphasize the responsibility of charity trustees and other administrators

to take appropriate steps to manage charity funds, rather than requiring issuers to enquire about the quality of advice given to a registered charity before accepting an investment from such an entity. Therefore, we submit that it would be appropriate to maintain the current status and provide that registered charities are, *per se*, *accredited investors*.

(c) *Person*

Although the proposed definition of *person* comprises a helpful addition to the regulations, this definition should be broadened. As proposed, the definition would lead to uncertainty as to the forms of corporate organizations that qualify as *persons*. In that regard, we recommend replacing parts (b) and (c) of the definition with the following:

> "(b) a corporation, limited or unlimited liability company, other form of corporate organization, partnership, limited partnership, limited liability partnership, trust, fund, any organization analogous to the foregoing, any association, syndicate, organization or other organized group of *persons*, whether incorporated or not, and"

Part 2: Prospectus and Registration Exemptions

(a) Division 1: Capital Raising Exemptions

(i) Section 2.1: The rights offering exemption

We submit the meaning of Section 2.1 of NI 45-106 is currently unclear. One possible interpretation is that the proposed provision would extend the exemption to a trade by an issuer in any right to purchase securities of its own issue. Currently, the exemption only applies to a trade by an issuer in a right it has granted to purchase additional securities of its own issue. The proposed rule may be interpreted as applying to any trade by the issuer in any right to purchase its securities, even if that right did not originate with the issuer. We are concerned that under this provision of the Proposed Rule an issuer could rely on the exemption when trading in puts, calls, futures and other derivative rights relating to the purchase of that issuer's securities, even if those rights were not originally granted by the issuer. It is our view that rights offering exemptions are appropriately limited to trades in rights granted by an issuer to purchase additional securities of the issuer and that, therefore, the ambit of the proposed exemption be limited to rights that have originated with the issuer.

(ii) Section 2.3: The accredited investor exemption

Please refer to our comments with respect to Part 1 of NI 45-106. As noted in the request for comments, the proposed rule would also extend the *accredited investor* exemption to trades in investment funds by fully managed accounts where those accounts are managed by a registered adviser or similar specialist. We support this extension because it places the focus of regulation on the area where it is most appropriate and likely to be most effective, the regulation of advisers of fully managed accounts. We note that the Proposed

Rule would remain more restrictive in Ontario than in other jurisdictions. In Ontario, a trade by a fully managed account in securities of investment funds will only be exempt if it is made by an adviser that is registered or qualified to act in that capacity by the laws of any Canadian jurisdiction. In other Canadian jurisdictions, a fully managed account with an adviser so registered or authorized under a foreign law would also benefit from the exemption. While we appreciate the rationale of limiting this exemption to those fully managed accounts with advisors qualified in a Canadian jurisdiction, we submit that in the absence of evidence of its abuse, the OSC should reconsider this "Ontario exception" in the interests of harmonization with the other Canadian jurisdictions.

(iii) Section 2.4: The private issuer exemption

Section 2.4 of NI 45-106 restores the exemption for trades in the securities of a *private issuer* by specified categories of investors. We strongly support the reinstatement of this exemption.

(iv) Sections 2.5, 2.6 and 2.7: Family, friends and business associates exemption

While we appreciate the potential problems associated with extending exemptions from the prospectus and registration requirements to *close personal friends* and *close business associates* and prefer the exemption set out in Section 2.7(1) of the Proposed Rule, we submit that in the interests of harmonization the OSC reconsider adopting the broader provisions in section 2.5 of the Proposed Rule. The rationale for both of these exemptions is primarily based on the investor's greater comfort with the issuer as a result of a personal relationship with a principal of the issuer. It will always be difficult to establish that these relationships are sufficient to instil such comfort and to establish who should qualify as a *close personal friend* or a *close business associate.* However, it should be acknowledged that, at least in the case of the private company exemption found in the Proposed Rule (or the current closely held issuer exemption), these investors would be permitted to invest in such issuers with no more protection than that afforded by this "friends and associates" exemption in the Proposed Rule. We believe it may be useful to highlight to the investor that the exemption is premised solely on the relationship of the investor with the issuer's principal. One means to do so is to require the purchaser execute a certificate to the effect that the investor is a close personal friend or a close business associate of the director, executive officer, founder or control person, as the case may be, and *has known such person for a sufficient period of time to assess their capabilities and trustworthiness*. Such an additional document may help to focus the investor's awareness that the prospectus-exempt trade is reliant on the relationship between the parties.

(v) Section 2.8: Offering memorandum exemption

We support the view that the offering memorandum exemption set out in NI 45-106 should not be available under Ontario securities law. Given the extensive prescribed disclosure for an offering memorandum used in connection with this exemption under NI 45-106, we believe that it merely serves to create a simplified prospectus regime alongside the current

prospectus regime. As such, this exemption introduces additional unnecessary complexity and, given the differences in application between the other jurisdictions, confusion into the securities laws of Canada. In our view, this is inconsistent with the goal of creating a harmonized securities regime. We support the OSC's resistance to introducing this exemption in Ontario.

(vi) Section 2.10: Prescribed minimum amount exemption

We support the reintroduction of a prescribed minimum amount exemption. We submit that this is a useful addition to the securities regime as it facilitates private placements by providing a "bright line test", however, we note that the exemption, as written, differs slightly from the former exemption in Section 72(1)(d) of the *Securities Act* (Ontario) (the "OSA"). Accordingly, we submit that it would be prudent to clarify the Proposed Rule by incorporating into the exemption the concept of "aggregate acquisition cost" rather than rely on the explanation in the companion policy.

(b) Division 2: Transaction Exemptions

(i) Section 2.16: Take-over bid or issuer bid

We are concerned that the language in Section 2.16, "…a trade in a security under a take-over bid…", may be interpreted as being limited to trades by shareholders of the offeree issuer to the offeror. To clarify that this exemption is available in connection with share consideration provided by an offeror, we submit that the language should be amended to read "…a trade in a security in connection with a take-over bid…".

(c) Division 4: Employee, Executive Officer, Director and Consultant Exemptions

(i) Section 2.22: Definitions

We note that the new exemptions set out in NI 45-106 differ from existing exemptions in Multilateral Instrument 45-105 – *Trades to Employees, Senior Officers, Directors and Consultants* in the substitution of the concept of *executive officer* for *senior officer*. The definition of executive officer appears to be considerably broader than the definition of senior officer, and includes any individual who performs a policy-making function in respect of the issuer. We submit that in order to avoid confusion it may be prudent to clarify that this portion of the definition only pertains to the principal or core business of the issuer.

(d) Division 5: Miscellaneous Exemptions

(i) Section 2.30: Incorporation or organization

We agree that, due to the availability of other exemptions, the exemption contemplated by proposed Section 2.30 is unnecessary and need not be included in the final instrument.

If, notwithstanding the foregoing, this provision is included in the final instrument, we have one comment with respect to its wording. In contrast with OSA Section 72(1)(o), the current draft of Section 2.30 fails to provide a prospectus exemption for a trade by an issuer in a security of its own issue if the statute under which the issuer is incorporated requires the trade to be for a greater consideration or to a larger number of incorporators or organizers than are contemplated by subsection (1). This could be rectified by amending subsection (3) to provide that "the prospectus requirement does not apply to a distribution of a security in the circumstances referred to in subsections (1) and (2)".

(ii) Section 2.43: Conversion, exchange or exercise

According to the summary in respect of NI 45-106, the requirement to give prior written notice to the securities commission under proposed Section 2.43 appears intended to capture only trades in a security where the issuer is trading in a security of *another* issuer that is a reporting issuer. However, as drafted, the wording of Section 2.43(1)(b) in conjunction with Section 2.43(2) could be misconstrued as requiring an issuer to provide such notice to regulators in the case of trades of both securities of another issuer that is a reporting issuer and securities of its own issue where the issuer is, itself, a reporting issuer. We would therefore recommend clarifying the wording in this provision by inserting language in Section 2.43(1)(b) similar to that found in OSA Section 72(1)(h) so that the provision reads:

> subject to subsection (2), the issuer trades a security of a reporting issuer held by it to an existing security holder in accordance with the terms and conditions of a security previously issued by that issuer.

Part 4: Control Block Distributions

(a) Section 4.1: Control block distributions

The exemption regarding control block distributions found in Section 4.1 essentially provides for the same exemption as is currently available under National Instrument 62-101 – *Control Block Distribution Issues*. However, we would suggest replacing the proposed language under Subsection 4.1(3)(a)(i) with "has filed the reports required under the early warning requirements or files the reports required under Part 4 of NI 62-103," in order to clarify that an eligible institutional investor can avail itself of the exemption even if it does not itself participate in the alternative monthly reporting regime. Additionally, we note the typographical error in Subsection 4.1(4), which should be corrected by deleting "of" and replacing it with "in".

(b) Section 4.2: Trades by a control person after a take-over bid

We have no substantive comments with respect to the exemption in Section 4.2 for trades by a control person after a take-over bid but note that it now applies to a "take-over bid", instead of the present availability under Section 2.4 of Rule 45-501 to a "formal bid".

However, the present requirements of the exemption suggest that it will continue to apply only to formal bids and further clarification is unnecessary.

Part 5: Offerings by TSX Venture Exchange Offering Document

We agree that the exemption under Section 5.2 is not necessary for the Ontario market.

Please do not hesitate to contact me (416-863-5537) if you wish to discuss our comments further.

Yours very truly,

(signed) Robert S. Murphy

Robert S. Murphy