



March 8, 2013

John Stevenson
Secretary, Ontario Securities Commission
20 Queen Street West
19th floor, Box 55
Toronto, Ontario M5H 3S8

Sent via Email: jstevenson@osc.gov.on.ca

Dear Sir:

Re: OSC Staff Consultation Paper 45-710

About the National Exempt Market Association (NEMA)

Originally founded in 2011 as the Western Exempt Market Association, we are an organization dedicated to the growth of the exempt market's public profile and the improvement of its reputation. Through our members, NEMA has firsthand insight and knowledge of the operation and corresponding needs of the retail based exempt market in Canada.

Like yourselves, NEMA seeks a proper balance between protection of investors and accessibility of capital for the business community. NEMA advocates for securities regulation that works in practice, not in theory, for the benefit of investors, industry, and the Canadian economy.

With this in mind, NEMA is pleased to present the following commentary on the Ontario Securities Commission (OSC) Exempt Market Review; Considerations for New Capital Raising Prospectus Exemptions (the 'Consultation Paper').

Process of Compiling this Report

Since the consultation paper was published on December 14, 2012, NEMA has been active in soliciting member and stakeholder feedback. In addition to a vast amount of email correspondence, NEMA participated in one-on-one conversations with over two hundred stakeholders in Ontario. We also held five of our own industry roundtable sessions in Toronto and attended the January 30 OSC consultation session. This report is a qualitative compilation of these efforts.

Executive Summary

An offering memorandum (OM) exemption is an effective tool for business, financial professionals, and investors alike. It allows businesses to raise capital without the high costs of a prospectus. It allows

advisors to gain a better understanding of a product they are selling, and it provides investors with a simple to read comprehensible document while still providing them with many of the same rights as afforded by a prospectus. It is for these reasons that its use is permitted by every other provincial securities commission or regulatory authority.

Answers to OSC Exempt Market Review Questions

Please note that this response addresses only those specific questions in the consultation paper that our members have indicated to be of the greatest importance.

Should an Offering Memorandum exemption be adopted in Ontario? If so, why?

Yes, our members unanimously agree that an OM exemption should be adopted in Ontario. We have segmented this section into five sections justifying this response:

(1) It enhances the ability to raise capital for Small & Medium Enterprises (SMEs)

SMEs are essential to the Canadian economy. Small (less than 100 employees) and Mid-Size (100-499 employees) businesses make up 98.1% of Canadian companies. In 2011, SMEs contributed to 63.7% of Canadian private sector employment. In addition, that same year, SMEs created 79,000 new jobs in Canada.¹ According to the Business Development Bank of Canada (BDC) Viewpoints study in 2011, ‘problems accessing additional financing’ was the second greatest challenge (32%) to SMEs with ‘the economic situation’ (40%) being the greatest challenge.²

SMEs are decreasing in numbers and say acquiring capital is their biggest challenge. A particularly concerning trend, especially for Ontario, is the decrease in privately owned mid-size firms. Mid-size firms contribute 12% to GDP and 16% to employment, even though they represent only 1% of firms in Canada. Nationally, firms of this size decreased by 17% from 2006 to 2010. In Ontario, the trend is more severe with a 25% decrease for the same period. Of these firms, 83% of them are privately owned. In the BDC’s study *What Happened to Mid-sized Firms?*³ mid-size businesses state ‘availability of financing’ as their key challenge (40%).

Entrepreneurs would invest more in their businesses, if they could access the capital. Another BDC study⁴ surveyed over 500 principals of Canadian SMEs about business investment spending. Over half of respondents stated that they plan to participate in business investment, and 60% stated that they would like to invest more or earlier, but access to credit was an inhibiting factor. The stated obstacles to investment were ‘insufficient working capital’ at 50%, and ‘limited access to credit’ at 30%.

Small business financing has never been harder to come by. In our current economic climate, banks are much more inclined to finance ongoing businesses with proven cash flows than they are new ventures. Banks fulfill a key role in our economy but financing new ventures and SMEs is no longer one of them.

¹ SMEs at a Glance BDC, http://www.bdc.ca/EN/Documents/SBW/BDC_SBW_Fiche_Info_SMEsAtAGlance_EN_2012.pdf

² BDC Viewpoints Study Oct 2011

³ BDC Study “What happened to Canada’s Mid-sized Firms?”

http://www.bdc.ca/EN/Documents/marketing/ViewPoint/BDC_study_mid_sized_firms.pdf

⁴ *Investments BDC Viewpoint Study* October 2012 http://www.bdc.ca/EN/Documents/other/BDC-InvestmentReport_EN_v2.pdf

By restricting capital to SMEs through a policy that differs from other provinces, the Ontario economy is being stifled, and Canada is becoming less competitive as job growth has to be through SMES, as Canada's labor market is currently globally uncompetitive for multinational corporations.⁵

The OM exemption would give Ontario SMEs a much needed option to infuse their business with capital. To prepare an OM costs as little as \$25,000 as opposed to preparation of a prospectus which can start at \$200,000 or more.⁶ In addition, preparation of an OM is much quicker, taking as little as four weeks, whereas a prospectus can take upwards of six months to complete. Creating the policy change of allowing the OM exemption in Ontario would assist SMEs who are requesting the government to help them to access capital, without the high costs of a prospectus. Provided there are sufficient investor protection mechanisms in place, which there are in an OM (as detailed later in this paper), it would be unfounded to continue to deny Ontario SMEs this alternative access to capital as it is efficient from both a cost and time perspective.

(2) An OM provides retail investors with greater access to investment opportunities already afforded to select groups in Ontario, and the rest of the Canadian population

Providing access to exempt market securities to retail investors would allow them to diversify a portion of their funds away from market volatility.

The lack of the OM exemption has effectively left only two available prospectus exemptions for individual investors in Ontario. The existence of only the accredited investor (AI) and minimum amount (MA) exemptions have created a lack of individual investor access to opportunities that institutional investors like pension funds enjoy. Only 1.14% of Ontario residents in 2010 met the income threshold for the AI exemption.⁷ A less common exemption utilized is the MA exemption,⁸ an exemption that puts retail investors at a huge risk of specialization of their portfolio, leading to over exposure in one asset. Therefore, only a small segment of Ontario investors have access to private securities and alternative investments, constricting their investment options and ability to diversify in non-market correlated assets.

This current arrangement provides for an unfair benefit to individuals who hold a portion of the \$1.31 trillion in pension plans in Canada, as they are able to benefit from diversification into non-market correlated alternative assets.⁹ Whereas individuals who have collectively invested \$1.02 trillion¹⁰ into RRSPs, DPSPs, TFSA's, RDSPs, and RRIFs for their retirement cannot generally access these alternatives in Ontario. The majority of exempt market securities are not as liquid as mutual funds and stocks, but retirement plans are not meant to be for short term investing. Pension plan members cannot access their funds unless they retire (or leave their employer in restricted cases). As RRSPs were created to motivate individual retirement savings for those who do not enjoy the benefit of pension plans, policy should support RRSP holders accessing a similar range of products for their portfolios.

⁵ *Top Ten Barriers to Competitiveness*. The Canadian Chamber of Commerce. 2011.
<http://www.chamber.ca/images/uploads/Top10/Top10Barriers.pdf>

⁶ Based on NEMA member law firms pricing 2013

⁷ OSC Staff Consultation Paper 45-710, Appendix D Income Data, p. 75

⁸ OSC Staff Consultation Paper 45-710, Appendix C Exempt Market Activity in Ontario, p. 71

⁹ Investor Economics, Household Balance Sheet. December 2011.

¹⁰ Investor Economics, Household Balance Sheet. December 2011.

(3) There has been significant growth in the exempt market, particularly with ‘smart money’

In addition to those that are accredited, Ontario residents fortunate enough to have a defined benefit plan have exposure to exempt market securities. In Ontario, 1.028 million public employees, including OSC staff, have public sector defined benefit plans.¹¹ All major defined benefit pension plan programs have incorporated private assets into their portfolios to mitigate market risk since the global financial crisis in 2008. Below is a chart of major pension plans and their current holdings, as well as their returns based on their 2011 annual reviews. Exempt market assets can be denoted under different equity classes, so all relevant asset classes are displayed.

Table 1: Canadian Pension Plans and their investments in the Exempt Market:

Name	Asset Class	Holdings	2011 Returns
Canadian Pension Plan ¹²	Real Assets	17.10%	13.90%
	Private Equity	15.30%	16.90%
Healthcare of Ontario Pension Plan ¹³	Private Equity	4.90%	10.31%
	Real Estate	11.50%	17.84%
Local Authorities Pension Plan ¹⁴	Private Equity	7.50%	8.20%
	Alternatives	32.00%	16.60%
OMERS Administration Corporation ¹⁵	Private Equity	13.90%	7.23%
	Real Estate	13.20%	8.40%
OP Trust ¹⁶	Private Equity	4.00%	29.60%
	Real Estate	15.00%	14.80%
Ontario Teachers Pension Plan ¹⁷	Private Equity	10.00%	16.80%

¹¹ Statistics Canada 2011 Registered Pension plan members, Ontario <http://www.statcan.gc.ca/tables-tableaux/sum-som/l01/cst01/famil119g-eng.htm>

¹² http://www.cppib.ca/Investments/Real_Assets/

¹³ 2011 Annual Report http://hoopp.com/uploadedFiles/Home/Finance_and_Governance/Annual_Report/2011_AnnualReport.pdf

¹⁴ 2011 Annual Report

http://www.lapp.ca/about/publications/annual_reports/LAPP_Annual_Report_2011.pdfhttp://www.lapp.ca/about/publications/annual_reports/LAPP_Annual_Report_2011.pdf

¹⁵ 2011 Annual Report http://www.omers.com/pdf/OMERS_Annual_Report_2011.pdf

¹⁶ 2011 Annual Report http://www.optrust.com/AnnualReports/AR2011/OPTrust_AR_2011.pdf

¹⁷ 2011 Annual Report <http://www.otpp.com/investments/asset-groups;jsessionid=bXSR975wukZfx2I54MHaQU+9.undefi>

Corresponding excerpts justifying investment in private securities

Ontario Teacher's Pension Plan

“We use alternative investments to capitalize on market inefficiencies and earn returns that are uncorrelated to other asset classes — thereby delivering true diversification.”¹⁸

OP Trust

“These changes, which will continue to be implemented over the next several years, subject to findings of a 2012 asset/liability study, include:

- reducing the Plan's exposure to public equities to 25% of the Fund, compared to 41.3% under the previous policy target
- increasing the target allocation for private equity to 15%, up from the previous target of 10%
- increasing the target real estate allocation to 15%, an increase of 5% from the previous target”¹⁹

OMERS

“Our substantial private market investments in infrastructure, real estate and private equity earned 8.20% or total investment income of \$1.8 billion. Our strategy to shift capital from public to private markets is working in accordance with our Strategic Plan's goal to achieve diversification in this asset mix.”²⁰

With pension funds and institutional money creating diversification and neutralizing market risk with non-correlated assets of private securities, it is only fair that individual retail investors working in the private sector are afforded the same opportunities.

(4) It decreases capital raising costs without compromising investor protection

The OM can be a tool for investor protection, much like a prospectus. The purpose of a prospectus is to protect the investor by giving them all the pertinent information to make an informed investment decision and an OM serves the same purpose.

Both individuals and institutions are actively seeking out diversification with alternative investments. In 2011, the estimated size of the exempt market in Canada was \$150 billion dollars.²¹ Adoption of the OM exemption in Ontario would be a positive action in supporting investors with an easy to read document while still providing them with many of the same rights afforded by a prospectus, as detailed in the following tables.

¹⁸ Ontario Teachers Pension Plan <http://www.otpp.com/investments/asset-groups/fixed-income-alternatives>

¹⁹ http://www.optrust.com/AnnualReports/AR2011/OPTrust_AR_2011.pdf p. 13

²⁰ Michael Nobrega, President & CEO OMERS 2011 Annual Report p. 8 http://www.omers.com/pdf/OMERS_Annual_Report_2011.pdf

²¹ Data taken from the CSA 2012 Enforcement report

Table 2: Summary of Disclosure Requirements in a Prospectus versus Offering Memorandum

Information included	Prospectus	Offering Memorandum
The history of the issuer and a description of operations	Yes	Yes
A description of the issuer's business and investment plans	Yes	Yes
A description of the intended use of the money raised from selling the securities	Yes	Yes
Information about the issuer's management and its principle shareholders	Yes	Yes
A summary of major risk factors affecting the issuer	Yes	Yes
A description of the legal rights of investors if the document contains a misrepresentation	Yes	Yes
A listing of the assets the issuer holds	Yes	Yes
A listing of the debt the issuer holds	Yes	Yes
A listing of other securities that have already been issued	Yes	Yes
Audited Financial statements	Yes	Yes

Even though OMs do not offer the same detail of disclosure as a prospectus (which often makes them too complex for average investors), the above table indicates that generally the same type of information is given in both.

Table 3: Summary of Structural Differences in a Prospectus versus Offering Memorandum

Features	Prospectus	Offering Memorandum
Ability to list on a public exchange	Yes	No
Tradable (OTC or an Exchange)	Yes	No
Continuous filings on SEDAR	Yes	No
Investor right to sue for material misrepresentation	Yes	Yes
Files with the Regulator	Pre distribution	Post distribution
Reviewed by the Regulator	Yes	No
Is there a market where the issuer's securities can be sold	Yes	No
Guarantees Investors will not lose all of their money	No	No

Unfortunately, neither an OM or prospectus can guarantee the absence of fraudulent activity or investor loss, however, both are tools to present investors with necessary information before they make an investment decision.

It should also be noted that regulators in both New Brunswick and Saskatchewan offer a voluntary pre-offering review for OMs.²² This review is to ensure the OM has adequate disclosure based on 45-106F2 requirements, and does not imply certification or approval by the commissions. The OSC could look at instating a similar program to add an extra level of investor protection. This program ideally could operate on a user fee basis with a 20 business days service standard for completion, as the New Brunswick Securities Commission is adopting.²³

²² New Brunswick and Saskatchewan offerings can be pre-filed as per staff notices 45-701 and 45-704 respectively

²³ NBSC staff notice 45-106 and NEMA personal communication with NBSC March 6 2013.

(5) NI 31-103 has created a better alignment of interest of issuers and investors

While it cannot be denied that in the past retail investors have lost money through investments in the exempt market, it has become clear that the losses that occurred were often due to registration exemption issues, not prospectus exemption issues. A vast majority of the losses occurred because the people that were selling the underlying securities were not registered and therefore did not concern themselves with things like suitability advice, knowing their client, or even having a real understanding of the product they were selling. The CSA noted that the lack of proper advice and care was a registration exemption issue not a prospectus exemption issue directly. Therefore, the necessary changes were made by implementing 31-103,²⁴ not modifying a fundamental prospectus exemption.

Additionally, there is a distinction between Exempt Market Dealers (EMDs) that sell related and unrelated issuers. When exempt market products are sold with an unrelated issuer and dealer, it is an arms-length transaction. This ‘retail’ model of the exempt market is more mature in Western Canada but could develop in, and greatly benefit, Ontario if the OM exemption is adopted. In this case, an EMD negotiates the best deal they can for investors, and seeks investor alignment in issuer/managerial compensation. This model is far less prone to potential conflicts of interest than is seen in related party offerings. EMDs serve all retail investors in other markets, whereas they only serve the top “1%” in Ontario. These EMDs offer similar, sometimes even identical, products as investment firms registered in other categories and have similar requirements in regards to suitability, know your client (KYC), know your product (KYP), and disclosure best practices.

Should there be any monetary limits on (the OM) exemption?

NEMA recommends that there should be no limits on the OM exemption in regards to the amount capital that is permissible to be raised by an issuer. The market should determine the best ranges of capital raising for the OM exemption, not the regulators. Our members unanimously stated that a \$1,500,000 per year maximum is too low and that the OM exemption would not be utilized in Ontario under these constraints. All members also unanimously stated that the \$2500 investor maximum per offering is completely unworkable. The majority of our members expressed that adoption of limits for investors similar to those found in the ‘Alberta model’ would be the most practical.

The proposed limits expressed in the consultation paper are completely impractical for EMDs, issuers, and investors alike. None of the industry participants we spoke with would engage this market based on the proposed limits. It was expressed to NEMA that these limits are only workable for the proposed crowdfunding model. The following is a summary of member feedback as to why the limits are impractical for SMEs, EMDs, and Investors alike.

²⁴ National Instrument 31-103 <http://www.albertasecurities.com/securitieslaw/pages/viewdocument.aspx?projectid=e8dbe910-53b1-47d0-9135-42618569788e>

Proposed Limits are Impractical for SMEs

One of the OSC's core mandates is "fostering fair and efficient capital markets and confidence in capital markets."²⁵ Restricting an investor to \$2,500 does not provide confidence but rather fear of deal risk and requiring an issuer to sign up a minimum of 600 investors per annum (3/business day) to get \$1,500,000 could hardly be described as efficient.

Additionally, the financial costs of an OM are too high under the proposed limits. Firstly, \$1,500,000 is generally not a significant enough capital raise for SMEs to create economies of scale to absorb the costs associated with the preparation of an OM. Secondly, that problem would be compounded when an issuer has to cover the costs (legal, printing, filing, reporting, etc.) associated with hundreds of investors due to the small proposed investor limit. The resource cost in investor service, and administration, makes these limits far too costly for the SME to benefit the business they are operating.

Proposed Limits are Impractical for EMDs

The proposed limits are not conducive for the EMD model currently in operation in all other provinces (otherwise known as the retail exempt market). The dealing representatives (DRs) who advise their clients under an EMD have their subscriptions (trades) approved by the EMDs Chief Compliance Officer. These recommendations are made with the same principles of asset allocation, diversification, suitability, know your client (KYC) and know your product (KYP) used in other registrant categories to determine appropriate investment amounts for each client.

Under the proposed limits, the projected revenue would not be sufficient to motivate EMDs and their DRs to sell under the OM exemption. If commissions are estimated at 6% to the DR, and 2% to the EMD, a DR would earn \$150 and an EMD would earn \$50 for a \$2,500 subscription. The ongoing administrative costs (and potential liability) of maintaining this type of client far outstrips the potential revenue.²⁶ Small investors are already too risky and costly for many firms to service and implementing small thresholds such as these would not increase their choices.

In addition, a \$1,500,000 maximum offering would not generally create enough economies of scale to cover the costs for an EMD to warrant doing due diligence, product training, and market implementation on a product. This makes this exemption of little use for the SMEs for whom it is intended, as there is no EMD we know of that would be willing to sell the OSC's proposed form of offering. Also, the cost in an increasing frequency of subscriptions based on decreasing subscription amounts would increase the cost of compliance for these firms, which is not ideal for the EMD.

Proposed Limits are Impractical for Investors

One of the greatest risks to any offering is under capitalization. By restricting an issuer to \$2500 per investor under this exemption, you would be forcing them to obtain subscriptions from a huge number of investors, perhaps an impossibly high number. Placing these restrictions on an offering immensely

²⁵ OSC Homepage http://www.osc.gov.on.ca/en/About_about_index.htm

²⁶ Based on interviews NEMA had with Canadian retail EMDs

increases the risk of under capitalization, which violates a fundamental goal of the OSC, protecting investors.²⁷

If the proposed limits in the consultation paper for the OM exemption were brought in, a retail investor would have the reckless situation of choosing between over diversification in many products (four per year) at \$2500, or to specialize into one product at a minimum of \$150,000. Ironically, the best limit per product for most clients would be somewhere in between the \$2500 and \$150,000 range, where investment is not permitted under these proposals. The composition of a client's portfolio should be based on individual circumstances, financial goals and portfolio diversification and asset allocation principles. It should not be determined by maneuvering around arbitrary limits set by a regulator as this has the potential to put clients in danger of over diversification or specialization of their life savings. In addition, with an amount so nominal as a \$2500 maximum, the client is less likely to read the OM or make any efforts to understand a prospective investment.

Adopting the OM exemption would help in the advancement of a fundamental investor right, the right to do as one chooses with their own money. Investors can do this in other facets of their finances already. Any Ontario resident can invest \$10,000 on a penny stock through a discount broker with the click of a mouse, even though they are provided with no disclosure documents and no suitability advice. Furthermore, any Ontario resident can put as much money as they choose on a hand at blackjack. If investors have these freedoms, it seems illogical to restrict Ontario residents to investing a maximum of \$2,500 in legitimate private business after being given access to disclosure, purchaser's rights, and even suitability advice.

Alternative Recommendations to the Proposed Limits

Based on the previous consultations with the OSC, NEMA has concluded that the OSC is not amenable to considering the unlimited BC model mentioned in the consultation paper, as it has been indicated informally that it is too unrestrictive. NEMA recommends adopting the 'Alberta model,' but if that too is not acceptable to the OSC, then NEMA suggests entertaining adopting an eligible investor regime with a capitalization limit. Our collective alternate recommendations are as follows:

- 1. Using Modified Eligible Investor Criteria:** It would protect small investors by limiting them to \$10,000. In addition, it could protect 'eligible investors' by not allowing them to invest over a prescribed limit (\$50,000 to \$100,000). Further, The OSC could exclude the principle residence in its calculations of eligible investors provided it lowered the net worth requirement to less than \$400,000.
- 2. An Increase in the proposed limit on how much the Issuer can raise per annum:** While our members universally said that the market should dictate upper limits on the OM exemptions, it was also communicated that the limit needs to be increased to \$20 million at the very minimum to not interfere with business processes and investor yield.

²⁷ OSC Homepage http://www.osc.gov.on.ca/en/About_about_index.htm

3. **Distinguishing between ‘related party’ and arm’s length transactions:** NEMA recommends that if investor and issuer restrictions are implemented, the OSC could isolate those restrictions to ‘related party’ offerings and not to those in which the EMD has no relationship with the issuer.
4. **Use Resources to Educate Registrants on Proper Procedures:** The greatest frustration our members communicate to us is not knowing if they are properly following the rules. We receive constant feedback from members that regulators are ambiguous and inconsistent in their responses to registrants and their councils. Our members want to operate in a compliant manor, but feel frustrated in their efforts. NEMA recommends proactive campaigns and resources like those offered by the NBSC²⁸ as a best practices standard.
5. **Use Resources to Enforce Rules and Punish Fraudulent Participants** The OSC currently has approximately 500 employees with 132 dedicated to enforcement.²⁹ Some of these human resources could be used to pre-approve OMs, and to properly investigate and penalize fraudulent behavior by those that misuse this exemption.

If there should be monetary limits on the OM exemption, should they be in addition to any limits imposed under any crowdfunding exemption?

The OM exemption and crowdfunding should not be looked at in the same light in any facet. The OM limits need to be significantly greater than what would be workable under the crowdfunding model for the reasons described in the previous section relating to costs, disclosure provided, and investor rights. NEMA’s research did not focus on crowdfunding as it is not a focus of our membership base at this time.

While NEMA supports the OSC envisioning the future of the capital markets, and how the technological revolution is changing the investor experience, it should not be at the cost of the present. The OM exemption is well established and utilized in other Canadian jurisdictions and there is significant research available into its benefits and shortcomings. Crowdfunding is a new concept with its merits and faults currently undocumented. While NEMA supports the idea of vast prospectus exemptions (with investor protection mechanisms in place) it is recommended that the OSC first look at what exemptions are already working in other CSA member jurisdictions to facilitate efficient capital markets and invigorate Ontario SMEs, and then look to international jurisdictions for new ideas.

Should a purchaser be required to receive investment advice from an adviser in order to rely on [the OM] exemption?

Yes, as long as EMDs and DRs are included in the definition. The majority of NEMA’s members that are DRs are either concurrently registered in other categories or have been in the past.

As mentioned in a previous section, with the involvement of a registrant, along with the providing of disclosure, the advisory process is not materially different from investing in the public markets. The same principles of KYC, KYP, suitability, diversification and asset allocation apply in the exempt market. The exempt market is now comprised of many registered advisors who feel they have a duty to act in their

²⁸ NBSC has resources are available including an OM template and education opportunities <http://www.nbsc-cvmb.ca/nbsc/content.jsp?id=1241&pid=1239>

²⁹ Personal communication with the OSC and NEMA, March 5, 2013.

clients' best interests, as is the case in the public markets, a position that NEMA has supported mandating to the CSA.³⁰ There are two primary concerns that securities regulators should have concerning all investments, those being proper disclosure and suitability, both of which are now covered in the balance of Canada's exempt market since implementation of National Instrument 31-103.

Should there be mandatory disclosure required in an OM? If so, what level of disclosure should be required?

Yes, adoption of the current 45-106F2 form used by all other jurisdictions would be prudent and assist with harmonization efforts with other provincial regulators.

NEMA has two other recommendations for mandatory disclosure in an OM. First, implementing an ongoing disclosure regime for private issuers of a certain size, particularly mandating annual audited financial statements should be given consideration. While it would have to be scaled to ensure it met the tests of a cost/benefit analysis, it would mitigate chances of fraud, which seems to be one of the OSC's primary concerns. Second, the OSC could consider removing the audited financial statement requirement for brand new issuers' OMs as it is an unnecessary cost associated with OMs with negligible benefits.

Should we require registrant involvement as a condition of (the OM) exemption? If so, what category of registration should be required?

Yes, as long as EMDs and DRs are included. To suggest that an EMD could not sell an exempt market security under any prospectus exemption is illogical.

The OSC's concerns about the findings during their compliance sweeps of EMDs provide no justification to prevent the opening of a retail exempt market through the OM exemption. To better gauge how this exemption affects EMDs, it would be most logical to look at compliance sweeps from other jurisdictions, as they already have the OM exemption and the retail exempt market.

In the OSC's ongoing discussions with fellow regulators about the OM exemption, NEMA recommends gathering data on compliance issues related to the OM exemption when an EMD is involved and where the underlying issuer is not a related party. It is highly probable that there will be very little deficiencies found now, as these issues were addressed with adoption of NI 31-103 and precedents set through enforcement.

Would a sophistication based exemption be useful for issuers, particularly SMEs, in raising capital?

Yes. Any additional exemptions will have some use for issuers. This exemption would be particularly relevant for start-ups as the costs associated with preparing the underlying legal documentation should be minimal.

³⁰ NEMA Response to the CSA consultation paper 33-403 on Best Interest Standards for Advisors and Dealers
<http://www.osc.gov.on.ca/en/38075.htm>

What educational qualifications should be met? Should we broaden the relevant educational qualifications?

In order for this exemption to be impactful, the relevant education qualifications should be broadened. NEMA recommends including the following designations;

- Chartered Accountant (CA)
- Chartered Financial Analyst (CFA)
- Certified Financial Manager (CFM)
- Certified Financial Planner (CFP)
- Certified General Accountant (CGA)
- Chartered Financial Consultant (CH.F.C.)
- Certified Management Accountant (CMA)
- Chartered Professional Accountant (CPA)
- Financial Management Advisor (FMA)
- Bachelor of Laws (LLB)
- Professional Engineer (PEng)
- Personal Financial Planner (PFP)
- Registered Financial Planner (RFP)

Other Recommendations

Managing Enforcement Other jurisdictions understand that the solution to improper practices with any exemption lie within their enforcement divisions. NEMA encourages the OSC to take the same approach and adopt this exemption based on the assumption that it will be utilized properly, and not paint the majority of EMDs that operate compliantly with the same brush as those that do not. If the OM exemption is adopted, the OSC could allocate enforcement efforts currently dedicated to reviewing investors accredited status towards compliance reviews of issuers who use the OM exemption.

Entertain Foreign Investment Opportunities It is understood that the rationale of mandating that exempt market funds are spent in Canada will help stimulate economic growth and employment. However, it ignores investment demands and diversification opportunities

Allow Retail Investors Access to Tax efficient Structures: Precluding certain tax efficient securities from being sold under the OM exemption, such as Limited Partnership (LP) or Mutual Fund Trust (MFT) units is ill advised. It is the DRs job to understand the securities and communicate this information to the investor. Factually, LP and MFT units are regularly sold to retail clients in other jurisdictions and are quickly becoming as well understood as the proposed allowable securities.

Concluding Remarks

Since implementation of National Instrument 31-103, the exempt market has become not so different than other parts of the investment industry. No matter how much regulation is in place, there will be success stories and there will be failures. NEMA recommends the OSC further empower the citizens of Ontario to make their own investment decisions and allow business to access capital in an efficient manner. In addition, the OSC should allow EMDs and DRs to do the job they have been permitted to do by merits of their registration and create suitable matches between the two.

Happy investors do not call securities regulators, angry ones do. It's logical to assume then that OSC staff and commission members are more in touch with the failures that occur in the capital markets than its successes. Given this perspective, there is a natural inclination for regulators to put the protection of investors ahead of the needs of the business community. While NEMA believes in investor protection mechanisms, the OSC over time has allowed the pendulum to shift and remain too far towards protecting investors at the cost of the efficiency of their capital markets (and ultimately investor choices as a byproduct). No matter what the regulation, no amount of rules will prevent some people from making poor investment decisions and that is why diversification and advisor engagement is crucial. There will always be business failures and fraud, in both public and private markets. That should not disallow SMEs to raise capital efficiently nor should it disallow the majority of investors to access exempt market securities.

NEMA is optimistic that commission members will give due consideration to the case presented by their staff, the exempt market industry, the trends of institutional investors, and the Ontario business community. NEMA is of the opinion that a strong business case has been made, and evidence suggests that it would be prudent for the OSC to adopt multiple additional prospectus exemptions, particularly the OM exemption and harmonize their policy with the rest of the country.

We also offer the OSC our support in any way it is needed as they contemplate these beneficial changes to their exempt market.

Regards,



Craig Skauge

President & Chair



Cora Pettipas DBA (candidate), CFP, CIM, MSc, FCSI

Vice President