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Denise Weeres  
Manager, Legal, Corporate Finance  
Alberta Securities Commission  
250-5<sup>th</sup> Street SW  
Calgary, Alberta T2P 0R4  
[Denise.weeres@asc.ca](mailto:Denise.weeres@asc.ca)

Me Anne-Marie Beaudoin  
Directrice du secrétariat  
Autorité des marchés financiers  
800, square Victoria, 22<sup>e</sup> étage  
C.P. 246, tour de la Bourse  
Montréal, Québec H4Z 1G3  
[Consultation-en-cours@lautorite.qc.ca](mailto:Consultation-en-cours@lautorite.qc.ca)

Government of Saskatchewan  
Financial and Consumer Affairs Authority  
Suite 601, 1919 Saskatchewan Drive  
Regina, Saskatchewan S4P 4H2

Dear Sirs/Mesdames:

**Re: Multilateral CSA Notice of Publication and Request for Comment (the “Notice”) – Proposed Amendments to NI 45-106 *Prospectus and Registration Exemptions relating to the Offering Memorandum Exemption and in Alberta, New Brunswick and Saskatchewan, Reports of Exempt Distribution dated March 20, 2014 (the “Proposed Amendments”)***

We are writing on behalf of McDougall Gauley LLP in response to the request for comment by the Canadian Securities Administrators (the “CSA”) with respect to the Proposed Amendments. Part I of our comment letter are general comments to the Proposed Amendments and Part II of our letter are responses to the specific questions set out in the Notice. Our firm actively represents issuers and registrants involved in the exempt market and as a result we are keenly interested in the Proposed Amendments and we appreciate the opportunity to provide our comments to you.

## **Part I – General Comments**

McDougall Gauley LLP represents issuers and registrants in the public and exempt markets throughout Canada, with a focus on western Canada. We have been involved in many offerings relying on the exemptions available under National Instrument 45-106 *Prospectus and Registration Exemptions* (“NI 45-106”) and have found the offering memorandum exemption to be a valuable tool for clients raising capital in Western Canada, and more particularly in Saskatchewan. Saskatchewan’s economy and capital markets have seen tremendous change and growth in the last 10 years. Because of Saskatchewan’s size and proximity to robust large scale economies such as Alberta, Saskatchewan has traditionally struggled to develop its own capital market. The offering memorandum exemption is an efficient and cost effective option for issuers to raise capital in Saskatchewan. In the Saskatchewan market, where there is not a deep high net worth investor pool that qualifies as accredited investors such as exists in Ontario, the offering memorandum exemption allows issuers to go into that specific marketplace and raise capital. Saskatchewan’s economy continues to grow and develop and it would be imprudent to limit or restrict the tools in which capital is raised in the province.

The primary area of concern we have in Proposed Amendments is the \$30,000 annual investment cap for eligible investors. We do not support any investment caps on eligible investors or issuers relying on the offering memorandum exemption, as it does not take into account the circumstances of the parties being affected. The variety of investors affected by the investment cap is wide and the Proposed Amendments unnecessarily apply the same restrictions on all of them equally and limit their freedom of choice and prerogative on investing.

This investment restriction will also hamper the issuers and registrants who utilize or rely on the offering memorandum exemption. Issuers would be forced to spend more time and effort to raise the same amount of capital because of the annual cap, thereby building inefficiencies into this exemption. Enforcement of the \$30,000 annual investment limit would also be an issue. Enforcement would likely fall on the issuer, and the issuer would have no definitive way to confirm if the investor is under the annual investment limit before accepting the subscription. The purpose of the offering memorandum exemption is for issuers to use it in strict compliance of the guidelines set out in NI 45-106. The restrictions in the Proposed Amendments materially limit the usefulness of the offering memorandum exemption.

## Part II – Responses to Questions in the Notice

### Question 1:

*Under the current framework in Alberta, Quebec and Saskatchewan, both individual and non-individual investors are subject to the \$10,000 annual investment limit if they do not meet the definition of an eligible investor. Should non-individual investors, such as companies, be subject to the \$10,000 limit if they do not qualify as an eligible investor? Please explain.*

### Comment:

Non-individual investors, such as companies, should be subject to the \$10,000 limit if they do not qualify as an eligible investor, as the current framework is structured. If the principals behind the corporation do not meet the eligibility criteria then the corporation should not be allowed to invest.

We also note the question references a \$10,000 annual investment limit. We understand the \$10,000 investment limit in NI 45-106 is not an annual limit.

### Question 2:

*Are there circumstances where it would be suitable for an individual eligible investor who is not an accredited investor and not eligible to invest under the FFBA exemption to invest more than \$30,000 per year under the OM Exemption? If so, please describe them.*

### Comment:

Yes, there are many circumstances where it would be suitable for an individual eligible investor who is not an accredited investor and not eligible to invest under the FFBA exemption to invest more than \$30,000 per year under the offering memorandum exemption. There is a large space between the \$400,000 net asset requirement of the eligible investor definition and the \$5 million dollar minimum net asset threshold of the accredited investor, and the number of investors within this bandwidth is enormous. Further, there are several additional material factors that come into play to determine whether investing more than \$30,000 per year under OM exemption is appropriate:

- the age of the investor
- the investor's financial sophistication and literacy
- the nature of the issuer's business, as some businesses are inherently more risky than others
- fluctuations in an investors asset base and income, particularly for self-employed individuals
- changes in the economy and the capital markets

- availability of attractive offerings in a particular year
- individual choice to forego investing during a particular year and then investing a larger amount in the exempt market in the subsequent years, based on the timing of exits of other investments they hold

In our view imposing the same blanket restriction of \$30,000 per year under the offering memorandum exemption on every single individual who falls within this category is unnecessary and unfairly restricts investor choice and prerogative. The regulators should be policing the issuers not the investors.

**Question 3:**

*Given the costs associated with doing so, how likely is it that an individual would create a corporation or other entity to circumvent the \$30,000 cap?*

**Comment:**

There will be some individuals who would create a corporation to circumvent the \$30,000 cap but the number would be fairly limited, in our view. It would depend upon the individual and the overall usefulness of an investment company for them.

**Question 4:**

*Investors who do not qualify as eligible investors based on net income or net assets can qualify as eligible investors on the basis of advice from a registered investment dealer. In what circumstances do investors actually seek and receive advice from a registered investment dealer? Does this introduce any complications or difficulties?*

**Comment:**

In our experience individuals typically do not seek or receive advice from registered investment dealers to qualify as eligible investors.

**Question 5:**

*The eligible investor definition includes persons that have a net income of \$75,000 and persons that have net assets of \$400,000. These income and asset thresholds currently apply equally to individual and non-individual investors, such as companies.*

*a. Should the \$75,000 income threshold only apply to individuals? If so, please explain.*

**Comment for 5a:**

We support keeping the current regulatory frame work the same and have the income and asset thresholds currently apply equally to individual and non-individual investors, such as companies. This is meant to protect those individuals behind the corporation who are at risk and to ensure

that they meet the appropriate requirements to invest in investments offered by the offering memorandum exemption.

- b. Should the net asset amount exclude the value of the principal residence for individual investors? If so, should the \$400,000 net asset threshold be lowered as a result?*

**Comment for 5b:**

No, the net asset amount should not exclude the value of the principal residence for individual investors. Depending on the market where the individual lives, principal residences form a significant percentage of the overall net worth of the individual and is often the place where investors direct their equity.

- c. Should pensions be included in the net asset test under the OM Exemption? Please provide the basis for your answer.*

**Comment for 5c:**

Pensions should be included in the net asset test under the offering memorandum exemption because they are an asset. Though pensions offer some challenges to value, valuation can be done and the pension should not be excluded from the net asset test.

**Question 6:**

*The FCAA would appreciate feedback on whether lawyers and public accountants should continue to be considered “eligibility advisers” in Saskatchewan for purposes of the OM Exemption. Please provide the basis for your opinion.*

**Comment:**

Lawyers and public accountants should continue to be considered eligibility advisers in Saskatchewan because they usually are able to review the investment and give investors a summary of the risks and issues related to the investment.

**Question 7:**

*How common is it for an issuer that relies on the OM Exemption to make annual financial statements available to security holders?*

- a. How is this done? Are they delivered?*

**Comment for 7a**

In our experience it is very common for issuers that rely on the offering memorandum exemption to make unaudited annual financial statements available to security holders, regardless of whether they are corporations, partnerships or trusts. Financial statements are typically

distributed by mail to the investors as part of an overall reporting packet, prior to the annual general meeting.

*b. Are those financial statements typically audited?*

**Comment for 7b:**

These financial statements are not typically audited unless there is something in the constating documents, bylaws or shareholders agreements that require an audit.

*c. If the financial statements are not typically audited, is there an auditor involved and, if so, what standard of engagement is typically applied?*

**Comment for 7c:**

The financial statements that are distributed by issuers using the offering memorandum exemption typically have an auditor or a third party accounting firm involved and the financial statements are usually notice to reader.

*d. Do issuers that prepare financial statements in accordance with IFRS for inclusion in their OMs typically continue to prepare financial statements in accordance with IFRS or do they transition to generally accepted accounting principles for private enterprises (ASPE)?*

**Comment for 7d:**

Issuers that prepare financial statements in accordance with IFRS for inclusion in their offering memorandum typically transition to generally accepted accounting principles for private enterprises after closing and for financial reporting going forward. IFRS financial reporting does not improve financial reporting for smaller issuers relying upon the offering memorandum exemption, and it materially increases the accounting costs. Therefore, the issuer usually moves to ASPE.

*e. Is it common for security holders to request annual financial statements? Do they request audited financial statements?*

**Comment for 7e:**

As above, issuers routinely provide annual financial statements without being requested to do so by security holders. Investors sometimes may request audited financial statements but it is uncommon largely due to the cost and effort in doing so.

*f. What do you estimate as the annual cost of preparing the proposed audited annual financial statements?*

**Comment for 7f:**

The estimate for an annual cost of an audited financial statement in accordance with IFRS would be anywhere between the \$10,000 to \$25,000 range and upwards, depending on the nature and size of the business.

- g. Do you anticipate that issuers will mail annual financial statements to security holders or place them on a website?*

**Comment for 7g:**

Issuers typically use mail for annual financial statements. In our experience non-reporting issuers do not put the financial statements on their website.

- h. What do you estimate as the cost of making annual financial statements available to security holders?*

**Comment for 7h:**

The cost of making annual financial statements under ASPE available to security holders would be in the \$5,000 range. The increased cost for IFRS audit would be \$10,000 to \$25,000 and up.

**Question 8:**

*Under the Proposed Amendments, issuers relying on the OM Exemption would be required to deliver annual financial statements until the issuer either becomes a reporting issuer or ceases to carry on business. Are there other situations when it would be appropriate to no longer require ongoing annual financial statements for such issuers? If so, please describe them.*

**Comment:**

There are no situations where it would be appropriate to no longer require ongoing annual financial statements for issuers relying on the offering memorandum exemption. Financial statements are a part of standard business operations, even when there is little business activity, and the financial statements should still be provided to investors.

**Question 9:**

*How do issuers relying on the OM Exemption typically communicate with their security holders? Do they maintain websites?*

**Comment:**

Issuers relying on the offering memorandum exemption typically communicate with their security holders via regular mail and email. They typically do not use websites.

**Question 10:**

*Should issuers be permitted to cease providing annual financial statements to their security holders after proceeds of a distribution are fully spent? If so, is there a period of time after which it is reasonable to assume that the proceeds of a distribution under the OM Exemption will have been fully spent?*

**Comment:**

Issuers should be providing annual financial statements to security holders going forward until the issuer ceases operations and undergoes an orderly windup.

**Question 11:**

*Should non-individual investors (e.g., companies or trusts) be required to sign a risk acknowledgement form? Please explain.*

**Comment:**

We feel it is good policy to have all investors, including non-individuals, signing risk acknowledgement forms as the investment risks are borne equally by individuals and non-individuals alike.

**Question 12:**

*Should “permitted clients”, as defined in National Instrument 31-103 Registration Requirements, Exemptions and Ongoing Obligations be required to sign a risk acknowledgement form? Please explain.*

**Comment:**

We take no position on this question.

**Question 13:**

*Should non-redeemable investment funds continue to be permitted to use the OM Exemption?*

**Comment:**

Yes. The decision to invest should be left to the investor.

**Question 14:**

*Are there certain types of issuers that should be excluded from using the OM Exemption?*

**Comment:**

No. The decision to invest should be left to the investor.



**Question 15:**

*Should issuers that are related to registrants that are involved in the sale of the issuer's securities under the OM Exemption be permitted to continue using the OM Exemption?*

**Comment:**

Yes. Registrants related to the issuer are bound by the same know your client, know your product and suitability obligations under National Instrument 31-103 as are third party registrants, and investors enjoy that additional regulatory protection as a result. All registrants are subject to the same oversight by securities regulators to ensure strict compliance. Conflicts of interest are adequately managed and addressed through proper disclosure of the conflict to the investor, so the investor can make an informed decision.

**Question 16:**

*Currently, most CSA jurisdictions that have an OM Exemption have adopted local blanket orders that permit an issuer to raise up to \$500,000 under the OM Exemption without having to include audited financial statements in the OM. Further, the blanket orders permit the financial statements to be prepared in accordance with ASPE rather than IFRS.*

a. *Should these blanket order be continued or revoked? Please provide the basis for your answer.*

**Comment for 16a:**

This blanket order should be continued however the maximum amount should be raised so it is utilized more.

b. *If you believe the blanket order should be continued, should the same threshold amount be used in determining which issuers are subject to an ongoing annual financial statement requirement or an audit requirement? Please provide the basis for your answer.*

**Comment for 16b:**

We don't feel that the same threshold amount should be used in determining which issuers are subject to an ongoing annual financial statement requirement as all issuers that rely on the OM Exemption should be required to provide annual financial statements. The audit requirement should be left to the investors themselves as determined by the constating documents, bylaws and applicable agreements.

Thank you for the opportunity to comment on the Notice. Should you have any questions about the forgoing, please contact the below.

Yours truly,

McDOUGALL GAULEY LLP



CHAD M. HAAF  
Partner

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