

Annex B

Background – Local Experience with OM Exemption

Alberta

Over the last three years, ASC Corporate Finance compliance staff has conducted a review of various OMs filed with the ASC under the OM Exemption. In addition, ASC staff conducted a detailed review of purchaser-level information from Exempt Distribution Reports filed in respect of distributions under the OM Exemption.

As a result of the reviews conducted, staff made a number of observations regarding how the OM Exemption was being used. ASC staff also considered Statistics Canada data regarding income and net worth information and compared that against what was observed in respect of use of the OM Exemption to better understand how the exemption was being used. The observations and statistical information were considered against the policy goals for the OM Exemption and gave rise to consideration of a number of possible changes to the OM Exemption. This review also resulted in recommendations regarding changes in the data required to be reported on Exempt Distribution Reports.

Some of the recommendations that developed out of this review are reflected in the Proposed Amendments. Other recommendations are contemplated to be addressed in a second phase. Recommendations that we contemplate addressing in a second phase relate primarily to disclosure enhancements to the form of offering memorandum. We also hope to address harmonized form requirements in respect of risk acknowledgements and Exempt Distribution Reports. Other possible changes, including some of those concurrently being proposed by the OSC, have been or are being considered.

Some observations about use of the OM Exemption in Alberta

The following summarizes some of the observations by ASC staff on use of the OM Exemption in Alberta.

- The OM Exemption is the second most frequently used “capital-raising” prospectus exemption in Alberta (41% of distributions in 2012 were made under the OM Exemption) although the value of the securities distributed (\$0.5 billion in 2012) was 3.8% of the total.
- The exemption is used almost exclusively by non-reporting issuers.
- 77% of the 287 issuers raising money in Alberta in 2011 and 2012 under the OM Exemption were Alberta-based.
- In 2011 and 2012, there was approximately \$824 million raised by 223 Alberta-based issuers under the OM Exemption. Approximately 155 or 70% of issuers self-reported their industry category as real estate or mortgage-investment corporations (MIC). These real estate and MIC issuers raised 76% of the total amounts raised by Alberta-based issuers under the OM Exemption.

- Of the purchasers under the OM Exemption in 2011 and 2012:
 - 90.5% were individuals;
 - 5.9% were corporations;
 - 1.7% were limited partnerships; and
 - 1.6% were trusts.
- Approximately 61% of the individual investors made at least one purchase in an amount **greater than \$10,000**, suggesting, assuming compliance, that they qualified as “eligible investors”. These purchases represented approximately 90% of the total value of purchases by individuals.
- Approximately 39% of the individual investors purchased in amounts **not exceeding \$10,000**. These individuals may or may not be eligible investors.
- The average size of an investment by an *individual* investor (assumed to be an “eligible investor” because of an investment of more than \$10,000) in 2011 and 2012 was approximately \$45,700 and \$47,900 respectively, while the median was approximately \$26,200 and \$27,500 respectively. (These amounts were higher for non-individuals.) Approximately 24% of eligible investors purchased more than \$50,000 and approximately 8% purchased more than \$100,000 per year. The following is a further breakdown of the total number of individuals that invested in 2011 or 2012 \$50,000 or more in a single year under the OM Exemption:
 - 1773 individuals invested between \$50,000 and \$99,999;
 - 816 individuals invested between \$100,000 and \$249,999;
 - 122 individuals invested between \$250,000 and \$499,999; and
 - 26 individuals invested in excess of \$500,000.
- The ASC has received numerous complaints from investors that have invested significant amounts under the OM Exemption and incurred significant losses.
- While approximately 68.7% of individuals made only a single investment over 2011 to 2012, the following % of individuals made multiple purchases:
 - 20% made 2;
 - 5.6% made 3; and
 - 5.8% made 4 or more.
- Where individuals made multiple purchases, their average and median investment, not surprisingly, increased as well.
- Of investors who only invested in amounts of less than \$10,000 (and may be non-eligible investors) 10% in 2011 and 17% in 2012 made repeat purchases resulting in their total investment exceeding \$10,000. Typically the total investment was less than \$25,000 but approximately 111 investors who invested less than \$10,000 per distribution invested in total from \$25,000 to \$100,000 within a calendar year.

- There are a few issuer groups raising the majority of the funds under the OM Exemption in Alberta. Some of these large issuers have “in-house” exempt market dealers selling the securities on their behalf.

Some Observations regarding Exempt Distribution Reports filed in Alberta

- Approximately 47% of Exempt Distribution Reports filed in 2011 and 2012 were filed late.
- The current form of Exempt Distribution Report provides limited information, creating monitoring challenges.

Coordination with the OSC

ASC staff were aware that the OSC was considering adoption of an OM Exemption and ASC staff therefore shared its observations on the use of the OM Exemption in Alberta with OSC staff. ASC and OSC staff also shared their respective recommendations regarding the OM Exemption and Exempt Distribution Reports and efforts were made to coordinate the recommendations and our respective publications for comment.

Québec

AMF staff has been reviewing use of the OM Exemption for the past few years and has not found significant problems with it in Québec. The AMF has found that the OM Exemption is not as widely used by its market participants as other capital raising prospectus exemptions. Some concerns that had been identified are reflected in the changes made to the Exempt Distribution Reports published in the CSA’s February 27, 2014 Notice of Publication.

From a policy perspective, the AMF shares most of the recommendations made by the ASC staff following their review of the OM Exemption in Alberta and has worked closely with staff of the other CSA jurisdictions in drafting changes to the OM Exemption.

Although the AMF is not publishing the proposed Exempt Distribution Reports, these are areas that it has considered and is interested in feedback in respect of them. Following receipt of feedback on the Proposed Amendments and the concurrent FCNB and OSC proposal, the AMF anticipates actively participating in the further review of the OM Exemption in phase 2.

Saskatchewan

FCAA staff have also been reviewing use of the OM Exemption locally over the past few years and have participated in the development of CSA and local notices outlining concerns with use of the OM Exemption.