December 23, 2020

Cathy Tearoe
Senior Legal & Policy Counsel
Alberta Securities Commission
Suite 600, 250 – 5th Street SW
Calgary, AB T2P 0R4

Dear Ms. Tearoe:

Re: Canadian Securities Administrators (CSA) Multilateral Notice 45-327, *Proposed Prospectus Exemption for Self-Certified Investors*

Thank you for the opportunity to comment on CSA Multilateral Notice 45-327, *Proposed Prospectus Exemption for Self-Certified Investors* which was published for comment on November 20, 2020 for local blanket orders, which if adopted would provide a new prospectus exemption entitled *Prospectus Exemption For Self-Certified Investors* (**Proposed Blanket Order**) intended to be available to Alberta and Saskatchewan issuers distributing securities in either or both of Alberta and Saskatchewan. We appreciate the opportunity to be a part of the CSA's reform process and to contribute to these important developments.

The Proposed Blanket Order will expand the angel investor[1] ecosystem on an interim, three-year basis, to self-certified investors through an additional prospectus exemption for use by Alberta and Saskatchewan businesses to facilitate their capital raising efforts, permitting them to distribute securities to investors in those provinces, provided that the investor signs a statutory declaration attesting to having completed a Self-Certified Investor Statement and Acknowledgement related to financial education or experience requirements, investment risks and considerations, and subject to specific investment limits over the last 12 month period. A stated goal of the exemption

[1] Angel investors are typically defined as high net worth or net income individuals that would qualify as "accredited investors". They will often invest in early-stage companies that are not yet at the stage of development to attract institutional investors, such as venture capital. They may invest individually or invest together with other angel investors through special purpose vehicles, e.g., corporations or limited partnerships, created to invest in a single business. Recently, NACO has expanded the definition of "angel investor" to include individuals that put their capital at risk in the early-stage ecosystem, which includes individuals that invest as limited partners (LPs) in angel funds, and/or venture capital funds.

is to allow self-certified investors to invest alongside "accredited investors"[2] in Alberta and Saskatchewan to facilitate growth of the angel investor ecosystem.

As CEO of the National Angel Capital Organization (**NACO**), I have a special appreciation for the important role that our provincial securities regulators play in protecting Canadian investors, particularly as a lawyer member of the Ontario Bar with experience having worked on secondment in the Corporate Finance Branch of the Ontario Securities Commission (**OSC**). For over 20 years, NACO has represented Canada's angel investors with a growing membership that includes more than 4000 angel investors and 40 angel groups. Over the past decade, NACO's angel members have invested over $1 billion into more than 1500 Canadian companies. Our work to expand access to capital in Canada includes an Annual Report on Angel Investing in Canada published in partnership with Innovation, Science and Economic Development Canada (ISED), which has data that was referenced in ASC Consultation Paper 11-701 *Energizing Alberta's Capital Market* (**11-701**).[3]

Overview

We commend the Alberta Securities Commission (**ASC**) and the Financial and Consumer Affairs Authority of Saskatchewan (**FCAA**) for your leadership in taking steps to mobilize capital for entrepreneurs through the proposed prospectus exemption for self-certified investors. We recognize that this undertaking is part of a broader initiative to contribute to Canada's economic recovery by strengthening, adapting, expanding, and diversifying our provincial economies. Importantly, this endeavour is taking place within the CSA's mandate to ensure appropriate securities regulation that protects investors and fosters a vibrant capital market.

Generally, we are supportive of the intent of the Proposed Blanket Order and we recognize the CSA's significant efforts and difficult task in striking a balance between investor protection and reducing the burden of raising capital for entrepreneurs. To meaningfully contribute to Canada's economic recovery, both non-accredited and accredited investors should be well-positioned to make informed and sustainable investment decisions. In striving to achieve an appropriate balance between protecting investors without unduly burdening the businesses trying to raise

[2] The term "accredited investor" defined in National Instrument 45-106 Prospectus Exemptions includes various specified institutions and wealthy individuals. The definition contemplates individuals with annual net income in excess of $200,000, net assets of at least $5,000,000 or net realizable financial assets of at least $1,000,000.

[3] https://www.albertasecurities.com/-/media/ASC-Documents-part-1/Regulatory-Instruments/2019/06/5466593-_-Consultation_Paper_Energizing_Alberta_s_Capital_Market.ashx

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capital to build and grow, we encourage a reevaluation of the fundamental assumptions underlying the accredited investor exemption. After careful consideration and review, we have identified several areas of opportunity in relation to this proposed exemption. Our comments in some cases are broader in scope than the Proposed Blanket Order, with a view to informing the policy objectives of the CSA. As it relates to the Proposed Blanket Order, we specifically recommend additional review of the financial, investment education, and experience requirements.

Angel investors are the primary source of early-stage funding for young companies, putting their own capital at risk in local communities and spurring job creation. Angel investors play a crucial role in the startup ecosystem, facilitating follow-on investment from venture capital firms and institutional lenders and providing mentorship, access to client networks and invaluable guidance to scaling companies. We applaud this initiative to enable more Canadians to join the angel investment community.

The Accredited Investor Standard

The current “accredited investor” standard is generally informed by two key policy rationales, particularly that wealth is a reasonable proxy for sophistication and that individuals with high net worth or annual income can sustain the loss of their investment. When viewed through the lens of the CSA’s broader initiative to strengthen, expand, and diversify our provincial economies, these rationales are flawed.

While relatively high annual income and net worth may increase the ability of a prospective investor to bear the loss of their investment, where those investments are uninformed (particularly as it relates to due diligence, valuation, and diversification within the early-stage asset class) investors are highly likely to lose their investment or experience illiquidity over an extended period of time. When investors suffer losses that could have otherwise been avoided through appropriate education, mentorship, or training (for ease of reference, referred to as “**avoidable losses**”) that capital evaporates from the early-stage ecosystem and additional capital allocations to other potentially higher-calibre businesses become less likely. As angel investing is a relationship-oriented activity, avoidable losses suffered by one investor can have a ripple effect, discouraging other prospective investors from supporting viable businesses. As a result, informed investing preserves the integrity of the angel investor ecosystem, which is critical to the growth and diversification of Canada’s economy.

The current standard overlooks the role of diversification in protecting investors against the risk of loss. A diversified but non-accredited investor with a net worth of $900,000 is not permitted to invest even 1% of her or his portfolio into early stage companies, yet an "accredited investor" with a net worth of $1,100,000 could potentially invest 100% of that money into a single startup and lose her or his entire life savings. Next, the elderly, in some cases a vulnerable population, may lack both financial sophistication and loss-bearing capacity, meet the current standard's wealth metrics, and yet best practices suggest that as an investor grows older, they should tilt their portfolio towards assets with lower risk and greater liquidity. By failing to consider the role of diversification in mitigating risk and conflating wealth and income thresholds with sophistication and ability to sustain loss, accredited investors under the current definition are exposed to losses that could be avoided through education, mentorship, or training.

Professional Designations are a Systemic Barrier

The Proposed Blanked Order's focus on financial and investment credentials does not take into consideration the systemic barriers that impact access to higher education and creates an inequitable barrier to participation in the angel investor ecosystem. Angel investing can lead to economic opportunity for both the investor and entrepreneur and should not be limited to those who have obtained a professional designation such as those listed in the proposal. Many of our country's most impactful angel investors are former entrepreneurs themselves who did not pursue professional designations, yet have years of experience building and scaling businesses.

> **Recommendation 1**
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> To minimize the impact of systemic barriers, we recommend additional review of the financial, investment education, and experience requirements in the Proposed Blanket Order. Targeted angel investment education combined with accredited angel group membership should be considered (as an alternative credential) to ensure the Self-Certified Investor criteria is inclusive.

Investment Limits to Protect Non-Accredited Investors

We support investment limits to protect non-accredited investors from loss stemming from any one company. However, to ensure the Proposed Blanket Order achieves its intended purpose in contributing to economic growth, while reducing the risk of loss to self-certified investors, we recommend that the maximum investment in any one company in a 12 month period be set to $25,000, but to facilitate diversification, that aggregate investments be allowed in a 12 month period of up to $100,000. The proposed maximums are otherwise too low and self-certified investors may lose access to high quality companies, thereby being exposed to the risks inherent within lower quality investment opportunities and a lack of diversification.

Recommendation 2

We recommend that the maximum investment in any one issuer in a 12 month period be set to $25,000 and the aggregate investments in a 12 month period be set to $100,000.

Recommendation 3

We recommend a diversification acknowledgement be added to the proposed Self-Certified Investor Statement in the form of acknowledgement on awareness of the benefits of diversification within both a broadly diversified portfolio, and within the angel asset-class itself (including through fund investments).

Sustainability of the Angel Investor Ecosystem

In addition, the current proposal assumes that a familiarity with investment and finance decreases the risk associated with angel investing. The challenge with this assumption is that if incorrect, we risk losing new investors who may exit the ecosystem if they make poor investment decisions and suffer otherwise avoidable losses. Assessing the growth and return potential of a pre-revenue, early-stage company is challenging even for seasoned angel investors. As a result, NACO in collaboration with Ryerson University developed a robust training program in 2017 to fortify the education and skill set of its angel investor members and increase the sustainability of investment outcomes. NACO has an online educational curriculum available on-demand to educate prospective investors on best practices, diversification, due diligence and valuation.

An adequate level of *angel investor training* is critical to minimizing the risk of avoidable losses for new investors, regardless of their professional designations. While the CFA/CPA designations and university level credentials including a Master of Business Administration (**MBA**) and Juris Doctor (**JD**), are reasonable proxies for general sophistication, the sustainability of the angel investor ecosystem requires more targeted education. Otherwise, as a country we risk losing a generation of investors and the capital they can bring to help diversify, expand, and grow our provincial economies.

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Recommendation 4

We recommend an educational acknowledgement be added to the proposed Self-Certified Investor Statement in the form of an acknowledgement on awareness of the availability of training, education and best practices of investing within the angel asset-class.

The risks associated with angel investing can be further decreased through affiliation with an accredited fund or angel group. A combination of angel investor training and participation in a fund or angel group can de-risk the investment and increase the likelihood of an investor remaining engaged in the ecosystem. NACO is well-positioned to administer the accreditation of angel groups and angel funds, while either NACO, the Canadian Venture Capital and Private Equity Association (**CVCA**) or the Business Development Bank of Canada (**BDC**, which invests in venture capital funds) could assist in the accreditation of venture capital funds.

In closing, we would like to thank the Alberta Securities Commission and the Financial and Consumer Affairs Authority of Saskatchewan for your leadership in endeavouring to expand the angel investor ecosystem. We welcome future opportunities to contribute to these important developments, particularly in helping the CSA to strike an appropriate balance between protecting investors and increasing access to capital for Canada's entrepreneurs to drive meaningful economic growth in communities across the country.

Yours very truly,

National Angel Capital Organization

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Appendix A: Biography of Claudio Rojas

Claudio Rojas is Chief Executive Officer of the National Angel Capital Organization (NACO). As CEO, he leads Canada's only nation-wide industry association for both angel investors and incubators and accelerators. For over twenty years, NACO has provided intelligence, best practices, tools and resources to unlock capital and mentorship for Canada's entrepreneurs. NACO members have invested over $1 billion into more than 1500 entrepreneurial companies.

As a lawyer and corporate finance professional with a specialization in complex areas of intersection between law and finance, Claudio has published a manuscript on corporate governance in the University of British Columbia Law Review, a top ranking peer-reviewed law journal. His primary research interest is in the integration of legal and economic analysis, with particular emphasis on the impact of ownership structure and governance on economic efficiency.

Claudio holds a Juris Doctor (JD) from Western University, Master of Business Administration (MBA) from the Ivey Business School, has achieved all three levels of the Chartered Financial Analyst (CFA) examinations, is a practitioner member of the European Corporate Governance Institute, and is a practicing lawyer member of the Bar of Ontario, Canada.