

Investor Forum

Appendix C

Working together: The 2007 Investor Forum



Exempt Market Issues

Exempt Market

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Exempt Market Issues

- ▶ Understanding the additional risks
- ▶ Are they suitable for you?

Meaning of Exempt

- ▶ Exempt from rules requiring a prospectus
- ▶ Offered under an exemption
 - Deposits including principal protected notes with Schedule I and II chartered banks
 - Insurance annuity contracts including segregated funds
 - Securities offered by means of offering memorandum to accredited investors and under the \$150,000 exemption

Principal Protected Notes

- ▶ Majority issued by Chartered Banks
- ▶ Deposit amount guaranteed by issuer only if held to maturity
 - Time horizons vary widely
 - If sold prior to maturity, price received will be based on value of assets linked to the note
 - Not covered by deposit insurance
- ▶ Minimum purchase generally \$2,000

Principal Protected Notes

- ▶ Portfolio fee is higher than MER of linked asset
- ▶ Some principal protected notes use leverage
- ▶ Look to suitability of linked asset
 - If linked asset is medium risk and suitable for long term growth then PPN should be considered medium risk and suitable for long term growth
 - If linked asset is high risk or speculative then consider potential income as high risk or speculative

Exempt Market Securities

- ▶ Limited partnerships
- ▶ Promissory notes
- ▶ Mortgage investment corporations
- ▶ Land development
- ▶ Factoring corporations

Who Can Buy

- ▶ **Accredited Investors include individuals:**
 - who beneficially own (either by themselves or with a spouse) \$1 million of financial assets
 - whose net income before taxes exceeded \$200,000 in each of the 2 most recent calendar years or whose net income before taxes combined with that of a spouse exceeded \$300,000 in each of the 2 most recent calendar years and who, in either case, reasonably expects to exceed that net income level in the current calendar year,
 - who, either alone or with a spouse, have net assets of at least \$5 million
 - Assumption is that an Accredited Investor afford to obtain independent advice

Who Can Buy

- ▶ Non-Accredited Investors who purchase a minimum of \$150,000 of the security
 - Assumption is that anyone with \$150,000 to invest in a single security is sophisticated and can obtain independent advice
- ▶ Can you risk \$150,000 in a single investment?
- ▶ Can you risk \$150,000 of borrowed money?

Prospectus VS. Offering Memorandum

Prospectus

- ▶ Regulator reviews for completeness
- ▶ Must include full disclosure of risks
- ▶ Full disclosure of all material facts
- ▶ No misrepresentations

Offering memorandum

- ▶ Regulator does not review for completeness
- ▶ Must include full disclosure of risks
- ▶ May include less information than prospectus
- ▶ No misrepresentations

Know Your Client Rule

- ▶ Advisors may only recommend trades that are suitable in terms of client risk tolerance and investment objectives
- ▶ Advisor must make sure that client understands the risk

Understand the Risks

- ▶ Review the risk factors that are stated in the offering memorandum
- ▶ If the document states that the securities offered are high risk or speculative it means they are high risk or speculative and suitable only for investors who
 - can afford to lose part or all of the investment
 - have significant investment knowledge
 - have a high net worth

Understand the Risks

- ▶ “An investment in the Funds offered hereby is appropriate only for investors who have the capacity to absorb a loss of some or all of their investment and for investors who have a significant degree of investment knowledge and sophistication as well as a high net worth”

Quality Varies Widely

- ▶ Look at more than one product

Analysis of Product

- ▶ Look at management history and track record
- ▶ Look at risk factors
- ▶ Look at objectives
- ▶ Look at markup
- ▶ Look at business plan
 - Analyze numbers; review for completeness
- ▶ Are objectives, markup and business plan reasonable?

Hedge Funds

- ▶ Different than mutual funds
- ▶ Less transparency than mutual funds
- ▶ Various strategies, many of which use leverage
- ▶ Underlying assets may be illiquid

Real Estate Limited Partnership

- ▶ Look at the promoter's mark-up
- ▶ Look at the price per rental/condo unit relative to similar properties
- ▶ Look at qualifications of the appraiser
- ▶ Look at income stream
 - What will property manager do to enhance value?
- ▶ Will you get all tax benefits described?
- ▶ Look at what can go wrong

Land Development

- ▶ What happens if the land doesn't appreciate over a specific term?
- ▶ What annual fees does the promoter charge?
- ▶ What is the price you pay relative to the price the promoter paid?

Promissory Notes

- ▶ Who is the issuer?
- ▶ Is the asset secured?
- ▶ What is your security?
 - Interest coverage
 - Asset coverage
 - Five year history should be required
- ▶ Who is the trustee?

Factoring Corporations

- ▶ Copies of the debenture and trust deed;
- ▶ The name and address of the trustee and its qualifications;
- ▶ Actual commission rates paid on one, two and three year debentures.
- ▶ Audited Financial Statements including detailed statements of investments for the past three years and current interim statements;
- ▶ Provisions of revolving credit agreements;
- ▶ Copy of the company's standard form of factoring agreement;

Factoring Corporation

- ▶ Copy of checklist or other documents used in accessing loan applications;
- ▶ The Chief Executive Officer's statutory declaration advising of any specific licensing arrangements that apply to the company, any defaults in past five years including but not limited to loan agreements, debenture interest payments and principal repayments, any judgments, any material litigation;
- ▶ Brief biographies of key personnel and owners including disclosure of any disciplinary actions by regulators, bankruptcies, judgments;
- ▶ Copy of the company's business plan; and
- ▶ Details on procedures that assure that investors receive interest prior to payment of fees to management.

Mortgage Corporations

► Risks

- General economic risks
- Credit risks
- Interest rate risk
- Borrowing risk

Donation Programs

- ▶ Tax shelter gifting programs
 - These are not securities
 - These are not investments

- ▶ Canada Revenue Agency has denied \$1.4-billion of claimed donations so far

Before You Invest

- ▶ Do you understand the risks?
- ▶ Do understand the product?
- ▶ Can you accept the risks?
- ▶ Can you afford negative consequences?
- ▶ Diversify