



## Results of Investor Focus Groups and Personal Interviews

### Background Report for Online Survey of Exempt Market Investors

Prepared for the  
Canadian Securities Administrators (CSA)

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## EXECUTIVE SUMMARY

- Three focus groups were held with Investors during the months of July and August 2011. Two focus groups were held in Toronto with Retail Investors and Mass Affluent Investors. One focus group was held in Mississauga with Top Quartile Investors. In addition, 15 personal interviews were conducted with Exempt Market Investors.
- There were only a few participants in the focus groups that own exempt market securities. As a result, discussion about exempt market securities was minimal at best.
- The objective of the qualitative research was to gather views and opinions of investors' level of understanding about how ownership of securities is recorded, whether in client name or nominee name. The research also explores investors' expectation and preferences with respect to what securities should be reported and the method of such reporting. Specific issues of concern relate to exempt market securities.
- Focus group participants expect to receive an account statement that contains all the securities they own. The most common purpose for receiving an account statement is to "know what is going on" with their investments. Focus group participants considered investments under the same account number to be "in the account". Among all groups, there is little understanding of the terms and concepts of securities held in client or nominee name. Nonetheless, they feel that account reporting requirements should be the same regardless of how securities are held/registered.
- The Exempt Market Investors interviewed hold a variety of investments including real estate investment trusts (REITs); mortgage investment corporations (MICs); private equity placements; limited partnerships; hedge funds; private equity funds (including a cooperative-owned fund) and debt issues.
- Exempt market securities are purchased through a combination of ways. Some are purchased directly from the issuer, others through an exempt market dealer (EMD), and others through a broker/advisor.
- Generally, participants considered securities (including exempt market securities) purchased through a dealer, whereby reporting is expected and received from the dealer, to be "in the account." For investments purchased directly from the issuer with no dealer involved, the term "in the account" has no meaning. These investments are considered separate from other account holdings.
- The majority of the investors interviewed (all but one) knew the meaning and could articulate the difference between securities held in client name versus securities held in nominee name. However, investors are not as clear about any differences in reporting between holding securities in client versus nominee name. For most, how ownership is recorded has minimal, if any, effect on account reporting.

## SUMMARY - PERSONAL INTERVIEWS WITH EXEMPT MARKET INVESTORS

- Almost all investors interviewed hold their exempt market securities in client name and do not see why they would do otherwise. Investors feel they have more control and a sense of ‘security’ holding exempt market investments in client name.
- Most of the exempt market investors interviewed would like to have client name securities reported to them if they were purchased through their broker/advisor. Investors do acknowledge that some information may not be available to report, in particular, valuation. They expect to see exempt market securities listed on their statements provided by their broker, and if possible, with account balances. Investors appear satisfied receiving transaction information only from the exempt market dealer.
- Investors receive exempt market accounting reports and investment information from different sources, typically from each issuer they have holdings with. Types of reports and information investors recall receiving include financial statements, quarterly financial reviews, and management discussion and analysis (MD&A). Investors that receive reports from their advisors/brokers note that duplication of information is not a concern.
- Receiving information on a regular basis is important, while the source of that information (i.e. advisor/broker versus issuer) may not be as important. Investors are definitely not willing to pay for information on exempt market securities from their broker/advisor, exempt market dealer and/or issuer.
- Overall, exempt market investors feel that investment valuation information they currently receive is ideal. Investors are satisfied to receive regular financial statements, annual and quarterly reports from the issuer for private placements. REITS and MICs provide ‘fair value’ valuation, while hedge funds have varying degrees of transparency on value, and monthly reports typically include net asset value.
- Overall, investors feel they receive just the right amount of reporting on their exempt market securities, regardless of the source. Online information is readily available, and is often accessed by investors between reporting periods.

## 1. INTRODUCTION

- Providing account reporting on securities is a requirement of National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations*, but there is currently no guidance in the legislation about which type of securities must be included or are considered to be “in the account”. Reporting practices for securities can differ depending on securities held in client name versus nominee name. Reporting on some securities can be particularly difficult due to an absence of established practices, as well as issues with respect to valuation.
- The objective of the qualitative research is to gather views and opinions about investors’ level of understanding of these issues in order to create an informed quantitative survey. The research also deals with investors’ expectations and preferences with respect to what securities should be reported and the method of such reporting. Specific issues of concern relate to exempt market securities.
- This report is a summary of the key findings of the issues and topics discussed in the focus groups and personal interviews.

### 1.1 METHOD

#### *FOCUS GROUPS*

- Three focus groups were held with Investors during the months of July and August 2011. Two focus groups were held in Toronto with Retail Investors and Mass Affluent Investors. One focus group was held in Mississauga with Top Quartile Investors. Participants were recruited randomly (as opposed to employing lists) by telephone by the Logit Group. Participants were screened according to personal income and amount invested and formed the following three groups:
  - **Group 1 Retail Investors:** Individuals with a personal income of less than \$200,000 per year and a combined income with spouse of less than \$300,000 per year;
  - **Group 2 Mass Affluent:** Individuals with a personal income greater than \$200,000 per year or a combined income with spouse greater \$300,000 per year;
  - **Group 3 Top Quartile Investors:** This group combines both retail and mass affluent investors, but participants have at least \$150,000 in investments.
- In addition, participants had to be at minimum 35 years of age.
- There were 20 participants in total. There were considerable **no shows** in the Mass Affluent Group.
  - Group 1 Retail Investors – 9 participants
  - Group 2 Mass Affluent – 3 participants
  - Group 3 Top Quartile – 8 participants.

## **PERSONAL INTERVIEWS WITH EXEMPT MARKET INVESTORS**

- In total, 15 personal interviews were conducted with Exempt Market Investors. The CSA recruited participants and provided The Brondesbury Group with a list of target investors. Interviews were digitally recorded and transcribed.

### **1.2 THE DISCUSSION GUIDES**

- The CSA provided detailed questions in the Request for Proposal which formed the framework for the final discussion guide. As a result, the focus group discussion guide was organized around the following topics:
  - **General Reporting** (frequency, understanding and knowledge of content);
  - **“In The Account”** (defining the term, what investments are included/excluded);
  - **Account Statement Reporting** (assessing information on account statements, most/least useful, improvements);
  - **Client Name vs. Nominee Name** (level of familiarity; affects on reporting; ownership and accounting standard preferences);
  - **Fragmentary & Supplementary Reporting** (general views on receiving, consolidating and willingness to pay);
  - **Valuation/Ownership** (preferences on reporting value on exempt market securities);
  - **Exempt Market** (preferences on account reporting information – sources, reporting on value)
  - **Closing** (general understanding of challenges; additional concerns and comment).
- The Personal Interview Guide with Exempt Market Investors focused primarily on exempt market securities/investments and included the following topics:
  - **Purchasing Exempt Market Securities** (from who; sources of account statement reporting; types of information received and preferred);
  - **“In the Account”**(i.e. defining the term, what investments are included/excluded);
  - **Valuation** (reporting of value; expectations and challenges);
  - **Closing** (general understanding of challenges; additional concerns and comment.)

### **1.3 ORGANIZATION OF THIS REPORT**

- This report summarizes responses and highlights key themes and findings of the focus groups and personal interviews.

## 2.0 SUMMARY OF KEY FINDINGS BY TOPIC

### *FOCUS GROUPS*

#### 2.1 GENERAL REPORTING

- Participants think “securities” means anything participants invest in. This includes stocks, bonds, equities, mutual funds, RRIFs, and ETFs. Complex investments like futures contracts and foreign exchange contracts are also considered to be securities. In a nutshell, securities are whatever is in the portfolio. Investors generally agreed that exempt market products are securities, including investments like limited partnerships, hedge funds, private placements, and shares in a syndicated loan or mortgage. While exempt market products are considered securities, there is agreement among the Top Quartile Group that investors in these types of securities are limited.
- With this in mind, there were very few focus group participants who invest in exempt market securities. It should also be noted that while groups were composed to reflect a varying degree of investment knowledge and sophistication, no one group appeared to be more knowledgeable about investments and securities than the others. ‘Accredited investors’ in the focus groups generally had the same level of knowledge about the topics discussed as the retail investors.
- All participants recall receiving monthly account reports and these are received from where they bought the securities --typically from a bank affiliated broker/dealer or other brokerage firm. Participants expect to receive an account statement with information on all the securities they own. It is common for participants to regularly check online how their investments are performing.
- The most cited purpose for receiving an account statement is to “know what is going on”. Components of the account statement that provide this information include investment performance, transaction activity, gains/losses and balances. Participants look for patterns over time to judge how their investments are performing. In addition to keeping track of investments, account statements are often used for tax (filing) purposes.
- Participants commented that current account statement reporting practices include a listing of all securities, book value, market value, transaction activity, number of units/shares, fees, dividends and cash balance. Frequency of reports (i.e. monthly, quarterly, annually) was not mentioned.
- Current account statement reporting requirements are explained to the participants during the sessions:
  - after any month when there is a transaction in the account, basic information about the transaction;
  - after every three months, information about all transactions made through your adviser during that time;
  - the three month report may also include account balance information, including market value, of all securities in the account, as well as any cash in the account.

- Among the groups, there were some differences in reaction to the account statement reporting requirements. The retail investor group found the language to be ambiguous and questioned who administers the standards (i.e. industry, government). Mass Affluent was satisfied with the standards, while Top Quartile Investors regard the standards as minimal. Top Quartile Investors would like to see the inclusion of a performance indicator as a standard requirement.

*“Basically you’re going to get an account statement every month if there’s any activity whatsoever. And as a default, you get it every 3 months, and it looks like something you would write in a piece of legislation. Is it comprehensive enough to be of any real use? I don’t know. It’s definitely minimal.” (Top Quartile Investor Group)*

- The participants’ main criticism about the account statement reporting requirements is the frequency that account statements are delivered. If there is no transaction activity in the account, three months is considered too long to wait before receiving account reporting. While the frequency of delivery of account statements is not a focus area of the research, we think it is important to report in this context.

*“Now why would there only be a statement when there’s a transaction? I mean, you’d want to know what’s going on. Whether it’s going up or down, not whether you bought something because if you didn’t buy it or sell it, it could be way down and you don’t know about it for three months.” (Retail Investor Group)*

## 2.2 “IN THE ACCOUNT”

- Participants considered investments under the same account number to be “in the account”. Investors may have different accounts for different activities and with different advisors/brokerage firms. The Retail Investor Group is the most uncertain if exempt securities would belong “in the account”. Mutual funds do. Mass Affluent group suggests there are two elements in the account – investments and cash. Top Quartile group articulates “in the account” as the account administered by a brokerage firm. This includes ALL investments, excluding property.
- Private company shares, purchased outside of an advisor, are considered separate and not in the account (with the advisor).
- All participants said they receive reporting on ALL securities they own from their dealer/advisor. While they do not pay directly for reporting, they clearly think that this is an expense that is part of the commission and/or fee/MER structure.

## 2.3 ACCOUNT STATEMENT REPORTING

- Participants have good recall of what appears on their account statements. Book value, market value, account balances, units held, dividends, maturity dates, number of shares, gains/losses are all top of mind when probed for details. Top Quartile participants tend to view account statements as basic and are apt to check online for more detail, especially for performance.

*“ (If you ) want to go back into performance history of any particular fund or ETF even if you want to look at PE ratios or whatever for individual stocks, you can usually access that information some place. I don’t know if they would be able to summarize it on a statement. It’d be tough.” (Top Quartile Investor Group)*

- Not surprisingly, Top Quartile participants find the information on account statement reports to be basic and can easily understand what is being reported. There is a mix of understanding among the other two groups. Book value, stock splits and stock symbols are most commonly misunderstood. Mass Affluent participants are not always clear what the numbers represent (i.e. money vs. units).
- Retail Investors would like to see more reporting on investment performance against appropriate benchmarks/indices. More detail on fees, investment returns, capital gains, dividends, and foreign currency exchange on trades are additional details they would like to get.
- Participants say account reporting statements could be improved with a level of consistency and standardization among reports. Using common terminology and providing definitions could be further improvements. More detailed information on fees and how calculations are derived, in particular what the real investment returns are after fees, commissions and MERs, is another area that participants suggested requires attention.

*“It would be good to have...like when you get a gas bill or a hydro bill, it shows you what you used a year ago. You know, you get that little graph...how it goes up and down. It would be nice to have that on so you don’t have to look back at the other statements. You have a sense of where it’s going without having to refer back.” (Retail Investor Group)*

- Participants thought the most useful pieces of information currently on account statements are transaction activity, income, balances, and performance of investments over time. There is no information that is considered ‘least useful’. All is important.

## **2.4 CLIENT NAME VERSUS NOMINEE NAME**

- Among all groups there is a lack of familiarity and understanding of the terms and concept of securities held in client or nominee name (also called “street name”). While participants in the Top Quartile Group had an overall better sense of what the terms mean, when asked how recording ownership affects reporting, participants do not know. Nonetheless, they feel that account reporting requirements should be the same regardless if securities are held in client name or nominee name.

*“I haven’t heard it and don’t know what it means, but I would think the nominee is somebody you’ve appointed, whether it’s the broker or maybe it’s another person, I don’t know.” (Retail Investor Group)*



*“So if it’s in client name, does that mean that they have the right to sell it when they feel it’s time to sell it, as opposed to us telling them to sell it?” (Retail Investor Group)*

*“Nominee is your firm would hold it in its name as part of a pool on your behalf as part of your client account, versus the security itself is registered in my name.” (Mass Affluent Group)*

*“Securities held in street name are held by the broker or the advisor in their name” (Top Quartile Group Investor Group)*

*“It’s splitting hairs. From our point of view as investors we want to know exactly what’s going on. It doesn’t matter how they record it in some register.” (Top Quartile Investor Group)*

## 2.5 FRAGMENTARY & SUPPLEMENTARY REPORTING

- Participants receive account reports about their securities from the source they were purchased from. This is typically from the advisor at a bank owned or affiliated broker/dealer or other brokerage firm. One report for each account is received. Some receive supplementary (including tax forms) information directly from the fund themselves.
- Receiving the same information about all securities from different sources (i.e. client name securities from an issuer and nominee name securities from advisor) does not seem practical for Top Quartile Investors.

## 2.6 VALUATION/OWNERHIP

- Participants trust that the value of investments reported on account statements is accurate and clear. They reiterated the need to see performance reported against a benchmark. They also comment that the net value of their investment returns after fees and MERs is often not obvious.

*“I think this thing (account statement) is highly accurate. When you want to give the market value, the question is – should you use the last transaction or do you use the current bid value? So if you wanted to liquidate everything you’d have to sell it at the current bid value, which is less usually than the market...the last transaction. So there’s a slight bit of inaccuracy but it’s trivial. I think the statement’s accurate.” (Retail Investor Group)*

*“It’s (fees and expenses) literally an industry secret. There’s no way of comparing one mutual fund to another, or even the same mutual fund that has different trailer fees or whatever. It’s very convoluted and it’s made intentionally so.” (Top Quartile Investor Group)*

### **Reporting Value on Securities that are not publicly traded**

- In each group only a very small number of participants own securities that are not traded on a stock exchange. Those that do include one person with investments in a private company and another who

holds an investment in a Labour Sponsored Fund. Many in the retail investor group would not invest in a security that did not have a market value. As a result, discussion about valuing non-publicly traded securities and the exempt market was minimal, at best.

- With this in mind, both retail investor and mass affluent participants would prefer to get an accounting estimate of the value, even though they may not be able to sell them for that amount.

*“It gives me comfort that somebody is doing something. I don’t know the degree of reliability of the information; at least somebody is trying to do a level of valuation.” (Mass Affluent Investor Group).*

- The two participants in the Top Quartile Investor Group who invest in the exempt market did not want value reported, although the last transaction value would be helpful. Referring to exempt market securities held in nominee name;

*“...so the fact they’re (advisor) not giving me a value of those shares is irrelevant to me.” (Top Quartile Investor Group)*

## 2.7 THE EXEMPT MARKET

- Of the few who own exempt market investments: two participants own private company shares purchased through the issuer (their employer) and one participant purchased a Labour Sponsored Investment Fund through an advisor.
- Participants in the Retail Investor Group feel that exempt market securities are a unique and sophisticated investment. They could appreciate that getting particular account statement information (i.e. account balance, transaction information only, etc. ) from their advisor about an exempt market security may be difficult.

*“It may not really be possible if you have a new company and you invest in it, you know, it’s not going to be quite the same. I mean, you can’t go to the index and compare.” (Retail Investor Group)*

*“If there’s a third party selling these things, then they have to be regulated. If you’re dealing directly with the people (as in the case of the issuer), it’s a different story, that makes sense.” (Retail Investor Group)*

*“There is no market value, just the fund’s best estimate what the value is. No point in level of detail that is not of value.” (Mass Affluent Group)*

*“I would prefer to get information from company/issuer. No need for advisor to know about these.” (Top Quartile Investor)*

## 2.8 CLOSING

- Overall, participants in all three focus groups did not fully understand how recording ownership of securities (client name vs. nominee name) affects account reporting standards and how these standards impact them as investors. They could not articulate any challenges their advisor may face in reporting on securities held in different ways. At the same time, participants generally feel it is important to understand these challenges in order to have a good understanding of how their investments are performing.

*“The whole reason we hold securities by and large is, it’s an investment, it’s there to earn money. To have information about what it’s earned, what it’s earning now, what the potential earnings are, it’s critical. Do we want to own this or not? If it’s going make us money, yes, and if not, we don’t.” (Top Quartile Investor Group)*

*“You know what it tells me? Here’s a group of investors, we all know something about markets and quite a bit about our money. None of us offered anything useful on the question of issue today because we didn’t even understand the distinction.” (Retail Investor Group)*

### 3.0 SUMMARY OF KEY FINDINGS - PERSONAL INTERVIEWS WITH EXEMPT MARKET INVESTORS

- During the months of July and August 2011, The Brondesbury Group conducted 15 personal interviews with Exempt Market Investors. The CSA recruited participants and provided The Brondesbury Group with a list of target investors. The response rate for interviews was excellent. These interviews were vastly more informative and the respondents were far more knowledgeable than in the focus groups. Many respondents were current or former securities registrants. These were some of the most sophisticated respondents we have encountered.

#### 3.1 PURCHASING EXEMPT MARKET SECURITIES

- The Exempt Market Investors interviewed hold a variety of investments including real estate investment trusts (REITs); mortgage investment corporations (MICs); private equity placements; limited partnerships; hedge funds; private equity funds (including a cooperative-owned fund) and debt issues.
- Exempt market securities are purchased through a combination of ways. Some are purchased directly from the issuer, others through an exempt market dealer (EMD), and others through an IIROC advisor/broker. Some use the EMD to “broker” the deal and a fee is paid up-front. Investments done via private banking are often done through an investment advisor or portfolio manager at the financial institution.

#### 3.2 ACCOUNT REPORTING ON EXEMPT MARKET SECURITIES

- Since exempt market securities are purchased through a variety of means, account reporting is varied and at times inconsistent. However, this does not mean that investors are unhappy with the reporting they receive on their exempt market investments.
- Generally, account reporting that is received from the EMD reports transaction settlement information. If the EM investment was purchased through an IIROC advisor/broker, the advisor/broker will provide account reporting to the client. Depending on the type of investment, information that is reported may include dollars invested in each security, cash position, valuation and unit value, number of units/shares held, account activity, current value of investment (if available). The advisor/broker may also provide supplementary research on the investment and sector reports, including due diligence on reports provided by the issuer. Less than one-third reported receiving regular account reporting from the EMD.

*“The dealer does in-depth research and updates research on a regular basis. I will get an update on general goings on and the issuer’s compliance. Its due diligence from the dealer. He is looking at it from his point at view, and very in-depth analysis. I am not going to get that from the issuer, just the accounting. I get updated analysis from the dealer for each holding.”*

*“I get trade settlements from the exempt market dealer – when trade is done, what is purchased. From the broker I will get a regular account statement – holdings, previous and current values. From issuer, I get annual financial statements.”*

- In other cases EMDs are used solely to broker the deal. They are paid a fee and the relationship ends. In these cases, reporting is not expected or desired from the EMD. For these investors, additional information the dealer may provide will be of little value because in most of these investments there is no market value.

*“Typically the exempt market dealer doesn’t hold the cash or securities in their account, so no reason for me to get a statement from them. If they act as agent, basically do the transaction, fund goes to lawyer in trust or to the company – they (exempt market dealer) are an intermediary, not a relationship. No need (to receive account reporting) unless they are holding the securities. The statement would essentially say nothing.”*

- For private equity funds that are purchased through a brokerage firm or bank owned affiliated broker/dealer, investors will typically receive reports from both the fund manager and the institution that administers the fund. When multiple reports are received, there are few reconciliation issues.

*“You might get reports from one source, in the case like an investment manager, running a segregated portfolio for you then (the manager) will also give you a statement. Sure, then you might compare that the holdings are the same. Maybe one incident they were off.”*

- Investors not dealing with an EMD, but rather purchasing the security directly through the issuer, will receive information about that investment from the issuer. Information that is provided by the issuer will often include quarterly financial statements and forecasts, budgets, operational and management discussion updates, including changes that have been made in terms of the financial structure (i.e. warrants exercised).
- Not all private issuers release the same level and detail of information. However, real estate funds typically provide investors with a net asset value. A third party accountant will often provide investors with an annual audited financial statement. It is noted that the quality of communication from issuers varies greatly.

*“Everyone is different. Quality of communication varies enormously. Some are fantastic – regular and thoughtful communication. Every board meeting, or every quarter there is a fulsome package that goes out to all shareholders that approaches what directors will see. The bar is very high compared to them. Most others have quarterly report which is ok, financial statements with verbiage – with a lot of spin, not a lot of juice in there. There are others that you never hear from – have to phone them to get information. No broad dissemination. Because it’s private there is no requirement legally to do that, but it would be nice.”*

- Investors are not willing to pay either EMDs or the issuer for account reporting and other related investment information. Both are viewed as expenses that should be covered either through the fees paid to the dealer, or through the operational costs of issuer.

### 3.2.1 Account Reporting Expectations

- Regardless of the source that provides account reporting, it is almost an even split between those who expect to receive regular account reporting on exempt market securities and those who do not. From the qualitative research there is no clear pattern that can distinguish who expects to receive account reporting and who does not. However, among investors who do not expect to receive regular account reporting from the EMD, most use the dealer in an intermediary role between the issuer and themselves, usually as a “middle man.”
- Investors receive exempt market accounting reports and investment information from different sources, typically from each issuer they have holdings with. Investors that receive reports from their advisors/brokers note that duplication of information is not a concern.

*“I will get some stuff from EMD, from various brokers, and I get press releases and financials from the issuer but not the same information.”*

*“I receive annual and quarterly reports, transactions, dividends, offering memorandum. No duplication of information and desire no more.”*

*“One holds bi-yearly meetings and basically goes over how the market is doing. Another sends information when they buy new buildings and lets you know what is going on with the company.”*

### 3.3 THE TERM “IN THE ACCOUNT”

- Generally, participants considered securities (including exempt market securities) purchased through a dealer, whereby reporting is expected and received from the dealer, to be “in the account.” They expect to see exempt market securities listed on their statements (quarterly and/or monthly depending on transaction activity) provided by their broker and if possible, with account balances. For investments purchased directly from the issuer with no dealer involved, the term “in the account” has no meaning. These investments are considered separate from other account holdings that are publicly traded.

*“Bought from issuer and not an exempt market dealer. No dealer of any kind involved. “In the account” has no meaning.”*

*“In the account means what are my particular holdings. I have a Canadian dollar account, a US dollar account, a margin account. Statements are for those specific accounts. You hold XYZ in one account,*

*ABC in another account, XYZ in this other account. Everything that I hold/own with one broker, that is in my account.”*

*“Anything that is held at that particular brokerage firm.”*

However, investors that use an EMD to purchase exempt market securities do not necessarily think they have an account with the dealer. EMDs that are used exclusively to facilitate trades are viewed more as a “sales” account versus an “investment” account.

### **3.4 CLIENT NAME VERSUS NOMINEE NAME**

- Majority of the investors interviewed (all but one) knew the meaning and could articulate the difference between securities held in client name vs. securities held in nominee name. Many of the investors come from the financial services industry.
- However, investors are not as clear about any differences between holding securities in client versus nominee name. It is remarked that trades seem easier to execute if held in nominee name. Depending on personal circumstances, investors feel a sense of security when held either way.

*“To me it’s in terms of trust factor. Brokers are regulated – no one is going to take my stock. For me it is more convenient to have in nominee name – getting reporting done all in one spot – the nominee name. My exempt market securities are held in client name.”*

*“Most of these securities I have are mutual funds with restricted distribution and I am not an active trader, so do not see advantage of it being in broker name to dispose of it quickly.”*

*“All investments are held in my name. Anything that happens need an authorization form from me. I reckon that if they were in a nominee name it would be easier to trade.”*

*“When in client name, it’s safer. Not sure if true, but that’s my perception.”*

*“In client name – issuer sends me information directly, so quicker to receive. If in nominee name, issuer sends stuff to broker then in turn sends to me. “*

- Almost all investors interviewed hold their exempt market securities in client name and overall, do not see why they would do otherwise. The exception is private banking investments and four-month hold securities. These are held in nominee name.
- Investors feel they have more control and a sense of ‘security’ holding EM investments in client name. Client name held securities can give investors voting privileges and can also be pledged as collateral. For most, how ownership is recorded has minimal, if any affect on account statement reporting.

*“For this particular investment vehicle, I prefer it in client name. Because I feel, even though with a stockbroker there is more regulation, I feel it is more secure”.*

*“All held in client name. Would never do exempt market securities in nominee name because there is no secondary market for them. Want my name on shares when entering “grey world” like exempt markets.”*

*“Generally held client name but there is different scenario with global banks we have relationship with. We have purchased some private equity funds – and are held in account with the global bank.”*

- Most investors would like to have client name securities reported to them if they were purchased through their regular broker. Investors do acknowledge that some information may not be available to report, in particular valuation. They expect to see exempt market securities listed on their statements provided by their broker and if possible, with account balances. Investors appear satisfied receiving transaction information only from the exempt market dealer.

*“If I buy through regular investment dealer, always in street name if possible. Even if bought through dealer in client name, reports units, but not value. For value it says “N/A”.*

*“If I bought the exempt securities from my regular broker, even in client name, I would expect them on my statement. I would expect whatever information can be provided but recognize that they can’t be valued when there is no liquidity in the marketplace.”*

*“If from broker, I want account balance. Exempt market dealer gives me transaction information – that is all I need from them.”*

- From the interviews conducted, it is not conclusive whether exempt market investors would be satisfied getting the same information for their exempt market securities as their other securities, but with some of the information coming from the issuer, instead of the adviser. Receiving information on a regular basis is important, while the source of that information (i.e. advisor versus issuer) may not be as important.
- One thing is certain -- investors are not willing to pay for information about exempt market securities from their advisor, exempt market dealer and/or issuer. Account reporting, financial statements, annual reports and supplementary investment information are considered to be value-added features of investing costs, and inherent to commissions, fees and/or operating expenses.

### 3.5 VALUATION

- For investments that do not have a market value, investors told us that information they receive on their exempt market securities that relates to value is often done by a 3<sup>rd</sup> party administrator or accounting firm. Audited financial statements, quarterly reports, last transaction value of new issues are also used to assess value. Over time, as investments start to mature, the issuer’s credibility in valuing their business becomes apparent. Exempt market securities do pose



valuation issues for investors, but investors are aware of this going into the investment and are willing to take the risk.

*“Most difficult to value are private business, venture capital type scenario. No market, no liquidity, business may be in growth mode and not generating a lot of free cash so can’t put standard multiple on cash flow.”*

*“The biggest valuation I get is the price heats from the markets. And as far as private securities are concerned the valuation I get is looking at where the stock would have traded in the last 12 months – a new issue of securities. That gives you valuation on private companies. If your company hasn’t done something in past 12 months, you are going to look at a proxy and see what that company has done and value on a relative basis.”*

*“On private equity side of things, generally on quarterly/semi-annual cycle – we get capital calls and disbursements then usually put out quarterly letter/statement – here is what is happening to business, here is the value we are carrying it at. Under fair value accounting rules, the private equity fund has to go through their accountants, has to justify its valuation that they are reporting on. It is based on methodologies that accounting signs off on. So take comfort on that process.”*

- Investors are rather split about how they would like an advisor to report on the value of securities that do not have a readily available market value. Those who chose to be informed that there can be no value assigned to securities on an account statement want to be informed what securities were bought and/or traded (i.e. transaction information).

*“I would prefer to be informed of what was bought, but don’t provide a value if it can’t properly be calculated. I would like to see how much was invested by date, as well as units held.”*

- Investors who prefer to receive an “accounting estimate of the value” do so with a sense that something is better than nothing.
- Only two interviewees prefer to receive no reporting of any kind for securities that have no known market value. They cite knowing up front the securities have no market value, therefore no value in receiving an estimate.
- The majority of investors interviewed would prefer to receive no reporting from their regular dealer or advisor on client name securities bought from other sources.

*“Actually one of the reasons why I don’t use an advisor. I don’t need the advisor to report on these. Don’t want my advisor to know everything. Want direct reporting from issuer. Advisor does not have full picture anyway. “*

*“We are a private enterprise, once bought something, none of their business afterwards.”*

- Overall, investors feel that the investment valuation information they currently receive is ideal. Investors are satisfied to receive regular financial statements, annual and quarterly reports from the

issuer on private placements. REITS and MICs provide 'fair value' valuation. Hedge funds have varying degrees of transparency on value, and monthly reports typically include net asset value.

### 3.6 CLOSING

- From the 15 interviews conducted with exempt market investors most feel they receive just the right amount of reporting on their exempt market securities, regardless of the source. Online information is readily available to many, and is often accessed by investors between reporting periods. The desire for more online information is a recurring theme in closing remarks.

*"I am ok right now. Got quarterly statement that shows units and estimate market value. Discount brokerage I can look up anytime I want. Instead of waiting quarterly."*

*"I feel satisfied with what he provides me so far. It is in depth. He asks the hard questions, he asks the same questions I would. My exempt market dealer is pretty good – that is why I chose him -- reporting is so complete. Of course, you have to trust him too."*

*"No relationship with adviser for exempt securities, so irrelevant. From the issuer, the information I get is about right."*

*"Information is sent on a timely basis. I don't have to wait for printed copies, I can get all the information online. I honestly can't think of anything else I would need."*

- Understanding the challenges the dealer/advisors may encounter when reporting on exempt securities, and in turn, getting a good understanding on investment performance, is considered important to interviewees. Recent improvements to securities regulation, in particular account reporting improvements are mentioned. Exempt market purchases are unique and investors recognize that they do not necessarily fit neatly into automated processes, such as account statements. As several exempt market investors commented, recent improvements to securities regulation, especially account reporting improvements, are commendable.

*"It is definitely important to understanding the challenges. Need to understand what is required in reporting, and I would be concerned if no action was being taken. But I take comfort that the OSC is taking action to ensure adequate and timely information on exempt market investments for investors."*

*"I think there have been significant improvements in last 3 or 4 years. Before would have some investments that never reported, monthly balance whatever. Can't think of any that do not report, but it is important to know everything is on the up and up. "*

*"This is important, but these are really sophisticated investors. All are accredited investors, and in my view, really don't need additional protection from the regulator. Having said this, it would be great if there were guidelines to help people in private placements. I think there is room for education for sophisticated investors and offered by regulatory bodies as part of maintaining accredited status."*

## 4.0 NEXT STEPS – QUANTITATIVE RESEARCH

- Insights gathered from the focus groups and personal interviews provided the framework to build the next phase of the research, an online survey with exempt market investors.
- Two provincial regulatory bodies agreed to participate in the online survey including British Columbia and Ontario. The aim is to have total of 200 respondents (100 from Ontario and 100 from British Columbia).
- The online survey went live on Tuesday September 20, 2011 and the CSA recruited exempt market investors to participate. The online survey will provide quantitative results on key questions that ask about:
  - Exempt market purchases;
  - Information sources including account statements and other financial information (i.e. annual statements and reports, cash position, current valuation, management discussion and analysis);
  - Information about exempt market securities that is reported to investors;
  - Access to reliable information about the value of exempt market securities;
  - Client name versus nominee name registration of exempt market securities.