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Proposed new fund Category – the ONTARIO Long-Term Fund Consultation

I appreciate the opportunity to provide comments on the Ontario Securities Commission (OSC) Proposal for an Ontario Long-Term Fund (OLTF).

When I was made aware of the OSC consultation, a few questions crossed my mind:

1. Are modest income retail investors lobbying for such a fund?
2. Why is the OSC promoting this fund and why is it a priority?
3. Why are the other provincial securities regulators not part of this "opportunity "for retail investors?
4. Are we sure quality Cornerstone investors will want to, and be legally able to, participate?
5. What is this illiquidity premium and is it a demonstrated phenomenon?

Except for item 5, I am unable to confidently answer the questions. Based on a google search I was able to conclude that the illiquidity premium is in debate and not a universally accepted investing principle In *Questioning the illiquidity Premium* – by Fiduciary Wealth Partners I note " *These studies, and more articles that we have included below under Related Reading, suggest that a private investment illiquidity premium does not necessarily exist*." https://fwpwealth.com/questioning-the-illiquidity-premium/

OLTF is a mechanism to allow private investments intended for wealthy investors with surplus cash, patience and a high risk capacity to be sold to retail investors with several protective bells and whistles added.

When sold to retail investors, Investment advisors will have to study the prospectus offering, understand it and link its character to the financial objectives of investors. This will be a time consuming challenge even for a CFP designated advisor.

A suitable investor would be an individual with a long time horizon, willing to wait years for results, has no foreseeable need for recurring income from the investment and is willing and able to take the risks involved in the private market. This is not the typical profile of the average Canadian retail investor. CIRO's Investor Survey revealed that 67 % of Canadians carry debt, and 36% are concerned about income stability. If this is the target investor market for OLTF, I expect the purchase of the long-term fund will reduce, rather than improve the financial well-being of Ontarians.In addition, investor financial literacy and competency remains an issue.

The potential upside of OLTF is portfolio diversification and a premium return for extended patience. In my view, such an outcome is less likely than a negative outcome given the significant number of market and product risks and multiple level of fees.

Prospectus
The rules should specifically require prospectus disclosures to be set out fairly, clearly, and in plain language with illustrations as needed. A OLTF may have complex features, for example, in relation to investment strategies, subscription and redemption terms and fee structures. The disclosures must give retail investors confidence that they can understand the nature of the investment and make an informed purchase decision.

Terms of sale
Unless there are special provisions permitting redemption upon death, investors would be silly to buy such a product. There would also have to be a commitment to cap the MER for the duration of the hold period and reduce it during redemption freeze periods.

Impact of long hold period
As someone who has been investing for over 30 years I really do not find the opportunity enticing. I find a long hold period a negative for a number of reasons. First, during the hold period one could be earning 4-5% dividends from liquid stocks and not pay 2% plus MER or more for years without a payout. If the fund meets objectives, there could be a significant capital gains tax if not held in a registered plan. It can be assumed that the initial minimum investment will be substantially higher than for regular mutual funds. In addition to all the fund related fees and expenses, the retail investor will almost certainly need to retain the services of an

investment advisor, thereby adding at least another 1% to investing costs. If the fund flops or is forced to wind down, the losses could be very significant for a retail modest income investor.

Valuation accuracy
Accurate valuations will be extremely difficult especially since OLTF will have limited information to work with. There could even be motivation to inflate asset valuations. A well-functioning Board could mitigate conflicts of interest but it will be an added expense of the fund. I expect there will also be more than one independent valuation each year, further adding to fund expenses.

Portfolio balancing
Balancing a portfolio containing an illiquid security can be very challenging if not impossible depending on the degree of OLTF exposure.

Chance of mis-selling
Unless the existing KYC process is upgraded, there is a real possibility OLTF will be mis-sold to seniors, new immigrants, vulnerable persons with attendant complaints and negative media coverage.

Reduced investment management focus
Fund management may need to spend an inordinate amount of time juggling liquidity rather than managing and monitoring investments.

Retail investor behaviour
The inability to sell during market volatility could cause unsophisticated investor anxiety and stress as well as economic hardship if investors must borrow cash to meet cash flow needs - such charges will impair the potential benefits of the "illiquidity premium".

Private market less efficient than public market
Based on US research, public markets allocate capital much more efficiently than private markets. A recent study found that "[a] dollar of equity allocated in public markets generates $0.35 more in annual revenue over the next three years than a dollar allocated to a comparable firm via a private market deal. *Comparing Capital Allocation Efficiency in Public and Private Equity Markets* by Ali Sanati, Ioannis Spyridopoulos: SSRN
https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4403578

Private equity (PE) may be a positive for investors but...
There is also empirical research that suggests private Equity can be harmful to the economy and private investments are not as efficient in boosting economic activity as public markets .In *Plunder, Private Equity's Plan to Pillage America* author Brendan Ballou explains how PE has reshaped American business by raising prices, reducing quality, cutting jobs, and shifting resources from productive to unproductive parts of the economy. Ballou vividly illustrates how many PE buy up retailers, medical practices, nursing-home chains, and mobile-home parks, among other businesses, using little of their own money to do it and avoiding debt and

liability for their actions. Forced to take on huge debts and pay extractive fees, companies purchased by PE firms are often left bankrupt, or shells of their former selves, with consequences to communities that long depended on them. Could this happen in Ontario? Should PE be part of OLTF?

Conclusion

Given all these facts and concerns I could not support the sale of risky illiquid assets to Main Street investors saving for retirement. I urge the OSC to (a) reflect on the issues raised by consumer groups, investor advocates and the OSC IAP and (b) assess the investor experience in other jurisdictions that have attempted to democratize investing before rolling out the OLTF in Ontario.

If despite the concerns, OLTF is implemented, I recommend that:

- OSC launch a comprehensive investor education program on private capital investing
- The Fund can only be sold by a Certified Financial Planner or equivalent
- A cap is set on fees for the duration of the hold period
- The Advisor signs an acknowledgement form certifying purchase is suitable
- Leveraging rules be tightened for OLTF purchases
- Clients are informed in writing of risk, tax ,liquidity and estate issues in plain language related to OLTF ownership prior to sale
- A enhanced investor tested Fund Facts and MRFP be made available
- Hardship provisions be part of the purchase agreement

I recommend that this initiative be shelved in favour of higher investor protection priorities.

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