



CANADA'S VENTURE CAPITAL & PRIVATE EQUITY ASSOCIATION
ASSOCIATION CANADIENNE DU CAPITAL DE RISQUE ET D'INVESTISSEMENT

January 11, 2008

c/o Mr. L.R. Wilson, Chair
Competition Policy Review Panel
280 Albert St., 10th Floor
Ottawa, ON. K1A 0H5

Dear Sirs,

I am writing to you in my capacity of President of Canada's Venture Capital and Private Equity Association (CVCA). The CVCA is the sole national trade association representing the interests of all components of Canada's private risk capital industry. The CVCA's 120 full members include venture capital, mezzanine and buyout funds that have approximately \$60 billion in capital under management. CVCA associate members comprise the large majority of organizations, including legal and accounting firms, which provide advisory services to the private risk capital industry.

Canadian businesses face all of the same broad economic forces driving all open market economies. Emerging technology companies require active venture capital investors close to their head offices. Larger businesses require expansion capital and strategic growth driven by active private equity investors. As the private markets continue to grow in size and influence across the global economy, we need to build up our Canadian venture capital and private equity firms if we want to capture the growth potential of our own entrepreneurs and maintain leadership of our own economic growth.

We need strong Canadian investors if we want to build strong Canadian companies.

The Canadian private capital industry includes a number of strong participants. However, compared to the U.S. and other international markets, it remains relatively small and undercapitalized. A globally competitive private capital market requires more and larger Canadian venture capital and private equity funds. We must find ways to increase the flow of capital into Canadian funds both from international and domestic sources.

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If Canadian funds are unable to keep pace with their global peers, the share of private investment taken up by foreign venture capital and private equity funds will continue to grow. Company leadership and new business growth frequently migrate to their sources of capital, both in emerging technology businesses and in much larger mature companies, as seen in the current debate surrounding the "hollowing out" of our economy.

Current trends in this sector are not moving in the right direction:

- Canada's private risk capital industry is roughly one-half the size of its U.S. counterpart on a proportionate basis. The U.S. private capital markets have a much longer history than our own, which has led to a much greater level of participation in this sector by pension funds, endowment funds and foundations – deep pools of capital capable of sustaining the rapid growth in these markets. Most Canadian institutional investors do not participate in the private capital markets.
- While many Canadian funds have grown larger in recent years, they have not matched the growth pace of their peers in U.S. and other international markets. International private equity investors, including massive sovereign wealth funds, are on a global hunt for attractively priced assets and Canada represents a desirable hunting ground.
- The growing demand for private risk capital on the part of entrepreneurs, the technology industry and small and medium-sized enterprises is increasingly being met by foreign capital sources. For example, in the venture capital sector, the CVCA's most recent data indicates that foreign investment has jumped to 41% of all investment activity (53% in Ontario) from a historical level in the 25% range.
- Talented entrepreneurs, technologists and business leaders are also very much affected by capital market trends. We have increasingly seen U.S. private equity and venture capital firms attract leading individuals from business and government into their firms - individuals seeking to participate in the growth of this dynamic sector. Without strong Canadian investment firms, some of our most talented individuals may be driven away from our markets. We have seen this trend for many years in the venture capital sector, but only recently begin to emerge in our larger private equity markets.

As we move forward, there are a number of steps that could be taken to address the situation, including:

- Devising appropriate public policy instruments to stimulate domestic and foreign institutional investors' appetite for all parts of the private risk capital asset class in Canada.
- Easing the cross-border tax regulatory burden to make it easier for foreign pension funds, university endowments and other institutional investors to allocate a portion of their capital to Canadian venture capital, mezzanine and buyout funds. One longstanding issue has been the unnecessary burden imposed by the requirements of Section 116 of the *Income Tax Act* which acts as a significant deterrent to attracting new venture capital investment into Canada (as confirmed by a recent report from Deloitte).
- Maintaining an open and effective environment for private market investments, including through a competitive tax and regulatory regime across the economy generally. Many issues on the Government's agenda are already pointed in this direction, including the reductions in personal and corporate tax rates, as well as the push toward a single Canadian securities regulator. We strongly support these efforts.

My colleagues and I would be pleased to meet with the Panel to discuss these issues in greater detail. Please do not hesitate to contact either myself (416-362-2824) or our Executive-Director, Richard Rémillard (613-744-8969).

Yours truly,

Richard Nathan
President, CVCA – Canada's Venture Capital and Private Equity
Association

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cc: Richard Remillard, Executive Director, CVCA – Canada's Venture Capital and Private Equity Association