

Backgrounder



Ontario
Securities
Commission

Commission des
valeurs mobilières
de l'Ontario

FOR IMMEDIATE RELEASE

March 20, 2014

20 Queen Street West
22nd Floor
Toronto, ON M5H 3S8

EXEMPT MARKET REVIEW

1. Request for comment – proposed prospectus exemptions and reports

The Ontario Securities Commission (the OSC or we) published today for a 90-day public comment period:

- **Prospectus exemptions** – proposed rules for four new capital raising prospectus exemptions. The exemptions are intended to greatly facilitate capital raising by businesses at different stages of development, including start-ups and small and medium-sized enterprises (SMEs), while maintaining an appropriate level of investor protection.
- **Reports of exempt distribution** – two new reports of exempt distribution, one for investment funds and the other for all other issuers. The proposed reports would enable the OSC to obtain better information on exempt market activity than is presently reported.

Please see the OSC notice and request for comment accompanying the proposed exemptions and reports. The comment period is open until June 18, 2014.

2. Proposed prospectus exemptions

The four proposed capital raising prospectus exemptions published for comment today are as follows:

Exemption	Description
Offering memorandum (OM) prospectus exemption	<ul style="list-style-type: none">• Key capital raising concept – The proposed exemption would allow businesses to raise capital based on an offering memorandum being made available to investors. The exemption would be available for a wide range of businesses at different stages of development.• Key investor protection measures – The proposed exemption incorporates important investor protection measures, including:<ul style="list-style-type: none">○ a requirement that a comprehensive disclosure document, that is subject to statutory liability if it contains a misrepresentation, be delivered to investors at the point of sale,○ investment limits for individual investors who do not qualify as accredited investors (\$10,000 or \$30,000 under the exemption in a calendar year depending on the circumstances of the investor),

Exemption	Description
	<ul style="list-style-type: none"> ○ requirements to provide investors with certain limited disclosures on an ongoing basis, and ○ a requirement for investors to be given a risk acknowledgement form highlighting the key risks associated with the investment. ● Coordination with the Canadian Securities Administrators (CSA) – The securities regulatory authorities in the other CSA jurisdictions currently have a form of OM prospectus exemption. The securities regulatory authorities in Alberta, New Brunswick, Quebec and Saskatchewan are concurrently publishing amendments to the OM prospectus exemption available in those jurisdictions. Those proposed amendments are substantially harmonized with our proposed exemption.
Family, friends and business associates prospectus exemption	<ul style="list-style-type: none"> ● Key capital raising concept – The proposed exemption would allow businesses to raise capital from investors within the personal networks of the principals of the business. It is intended to enable start-ups and early stage businesses to access capital. ● Key investor protection measures – <ul style="list-style-type: none"> ○ The proposed exemption identifies the relationship an investor must have with a principal of the business to qualify to invest under the exemption. Further guidance is provided with respect to determining whether an investor qualifies as a close personal friend or close business associate. ○ In addition, there is a requirement for investors to be given a risk acknowledgement form highlighting the key risks associated with the investment. ● Coordination with the CSA – The proposed exemption is substantially harmonized with the existing family, friends and business associates exemption available in other CSA jurisdictions.
Existing security holder prospectus exemption	<ul style="list-style-type: none"> ● Key capital raising concept – The proposed exemption would allow public companies listed on the Toronto Stock Exchange, TSX Venture Exchange and Canadian Securities Exchange to raise capital on a cost effective basis from existing investors in reliance on a company’s public disclosure record. ● Key investor protection measures – The proposed exemption incorporates important investor protection measures, including: <ul style="list-style-type: none"> ○ an investment limit of \$15,000 in the previous 12 months under the exemption, if advice regarding the suitability of the investment has not been obtained, and ○ a requirement for a pro rata distribution of securities to existing security holders. ● Coordination with the CSA – The proposed exemption is substantially harmonized with a similar exemption adopted by certain other CSA jurisdictions. Please see “Related initiatives of other CSA jurisdictions” below for further information.

Exemption	Description
Crowdfunding prospectus exemption along with regulatory requirements applicable to an online crowdfunding portal	<ul style="list-style-type: none"> • Key capital raising concept – The proposed exemption would allow businesses to raise capital from a potentially large number of investors through an online portal registered with securities regulatory authorities. Businesses could raise up to \$1.5 million during a 12 month period. The proposed exemption is aimed primarily at start-ups and SMEs based in Canada. • Key investor protection measures – The proposed exemption incorporates important investor protection measures, including: <ul style="list-style-type: none"> ○ relatively small investment limits (\$2,500 in a single investment and \$10,000 under the exemption in a calendar year), ○ requirements to provide investors with certain limited disclosures at the point of sale and on an ongoing basis, ○ a requirement for investors to be given a risk acknowledgement form highlighting the key risks associated with the investment, and ○ a requirement that all investments be made through a registered crowdfunding portal. • Coordination with the CSA – The securities regulatory authorities in New Brunswick, Manitoba, Nova Scotia, Quebec and Saskatchewan are concurrently publishing the proposed exemption.

3. Proposed reports of exempt distribution

The proposed new reports of exempt distribution published for comment today are as follows:

Report	Additional information contemplated
New report for investment funds and increase in alternative filing frequency	<ul style="list-style-type: none"> • Proposed form – A new report of exempt distribution for investment funds is proposed (Form 45-106F10 <i>Report of Exempt Distribution For Investment Fund Issuers (Alberta, New Brunswick, Ontario and Saskatchewan)</i>). • Additional information to be reported – The proposed report contemplates investment funds providing additional information such as: <ul style="list-style-type: none"> ○ the exemptions relied on and the type of investor, ○ the reporting of redemptions, ○ the size and general category of the fund, and ○ additional profile information about the fund and its key service providers. • Increase in alternative filing frequency – Currently, investment funds may report distributions under certain prospectus exemptions (including the accredited investor and minimum amount investment prospectus exemptions) annually within 30 days after their financial year-end instead of within 10 days after a distribution. We are proposing to increase the alternative filing frequency for investment funds from annually to quarterly within 30 days after each calendar quarter in which a distribution was made.

Report	Additional information contemplated
New report for all other issuers	<ul style="list-style-type: none"> • Proposed form – A new report of exempt distribution for issuers other than investment funds is proposed (Form 45-106F11 <i>Report of Exempt Distribution For Issuers Other Than Investment Funds (Alberta, New Brunswick, Ontario and Saskatchewan)</i>). • Additional information to be reported – The proposed report contemplates businesses providing additional information such as: <ul style="list-style-type: none"> ○ the size of the business and the industry it operates in, ○ where the issuer’s securities are listed or traded, ○ the identification of the principals of the business, ○ more detailed information about the securities offered, ○ aggregated and specific details regarding the prospectus exemptions relied on, on a per investor basis, and ○ details regarding the involvement of registrants, finders and insiders, including compensation paid to them.

To facilitate harmonization, we have worked closely with the securities regulatory authorities in Alberta, New Brunswick and Saskatchewan to develop harmonized reports.

4. Background to proposals published today

The following is a high-level summary of our exempt market review.

- **Initial scope of review** – On November 10, 2011, CSA staff published CSA Staff Consultation Note 45-401 *Review of Minimum Amount and Accredited Investor Exemptions*. This review largely originated out of investor protection concerns associated with these two prospectus exemptions that came to light during the 2007-2008 financial crisis.
- **Broadening of scope of review** – On June 7, 2012, we published OSC Staff Notice 45-707 *OSC Broadening Scope of Review of Prospectus Exemptions*. We indicated that, in light of feedback from stakeholders, we were broadening the scope of our review to consider whether the OSC should introduce any new prospectus exemptions that would assist capital raising for business enterprises, particularly start-ups and SMEs, while protecting the interests of investors.
- **Consultation and other steps taken in broader review** – Since June 7, 2012, we have undertaken the following:
 - Creation of advisory committee – We established an ad hoc committee, the OSC Exempt Market Advisory Committee, to advise us on possible regulatory approaches to the exempt market.
 - Publication of concept ideas for new prospectus exemptions – On December 14, 2012, OSC staff published OSC Staff Consultation Paper 45-710 *Considerations for New Capital Raising Prospectus Exemptions*. The consultation paper described four concept ideas for possible new prospectus exemptions. The comment period on the consultation paper ended on March 8, 2013 and we received 102 comment letters.
 - Stakeholder consultations and investor survey – Following release of the consultation paper, OSC staff conducted extensive public consultations and stakeholder outreach, including: holding 46 one-on-one meetings with stakeholders, hosting five town hall meetings, and participating in various other discussion panels and stakeholder forums.

- Investor survey – We engaged a third-party service provider to conduct an investor survey to gain insight into retail investors’ views on investing in start-ups and SMEs.
- **Updates on progress** – On August 28, 2013, we published OSC Notice 45-712 *Progress Report on Review of Prospectus Exemptions to Facilitate Capital Raising*. The progress report stated that the OSC was directing staff to undertake further work on developing the proposed prospectus exemptions and the proposed reports published for comment today. On December 4, 2013, we issued a news release announcing our commitment to publish the proposed prospectus exemptions in the first quarter of 2014.

5. Related initiatives of other CSA jurisdictions

- **Local existing security holder exemptions** – On March 13, 2014, certain CSA jurisdictions published Multilateral CSA Notice 45-313 *Prospectus Exemption for Distributions to Existing Security Holders* announcing that each participating jurisdiction will introduce an existing security holder exemption as described in that notice. As noted above, our proposed existing security holder exemption that was published for comment today is substantially harmonized with the CSA version of the exemption.
- **Local crowdfunding proposals** – The securities regulatory authorities in Manitoba, New Brunswick, Nova Scotia, Quebec and Saskatchewan published today a multilateral CSA notice of publication and request for comment related to both the crowdfunding prospectus exemption discussed above as well as local blanket or general orders creating an alternative form of crowdfunding prospectus exemption targeted at start-ups. The proposed local general orders are similar to General Order 45-925 *Saskatchewan Equity Crowdfunding Exemption* published on December 6, 2013. The comment period on the local blanket or general orders is open until June 18, 2014. In addition, the British Columbia Securities Commission has published BC Notice 2014/03 *Start-Up Crowdfunding* pursuant to which it is requesting comment on introducing a crowdfunding regime similar to the regime set out in General Order 45-925 *Saskatchewan Equity Crowdfunding Exemption*.

Please see CSA Staff Notice 45-314 *Consolidated List of Current CSA Exempt Market Initiatives*, published on March 20, 2014, for further information.

6. Other exempt market initiatives

In addition, in conjunction with the other CSA jurisdictions, the OSC is currently consulting on the following:

Proposal	Description	Deadline for comments
Proposed amendments to existing short-term debt prospectus exemption relating to distributions of commercial paper	<ul style="list-style-type: none"> ● The proposed amendments would modify the credit rating requirements of the exemption in order to: <ul style="list-style-type: none"> ○ remove the regulatory disincentive for some commercial paper issuers to obtain an additional credit rating, ○ provide consistent treatment of commercial paper issuers with similar credit risk, and ○ maintain the current credit quality of commercial paper distributed under the exemption. 	April 23, 2014

Proposal	Description	Deadline for comments
Proposed short-term securitized products prospectus exemption	<ul style="list-style-type: none"> The proposed amendments would limit the use of the existing short-term debt prospectus exemption and certain other prospectus exemptions to issue asset-backed commercial paper (ABCP) and other short-term securitized products. The proposed amendments would introduce a new prospectus exemption that would be limited to conventional or traditional ABCP. The new exemption would have conditions relating to credit ratings, liquidity, underlying asset pools and initial and ongoing disclosure. 	April 23, 2014
Proposed amendments to existing accredited investor prospectus exemption - general	<ul style="list-style-type: none"> The proposed amendments would require persons relying on the exemption to obtain a signed risk acknowledgment in the prescribed form from individual accredited investors who are not permitted clients and would provide additional guidance on steps issuers should take to verify an investor's accredited investor status. The proposed amendments are intended to address investor protection concerns as well as concerns regarding compliance. The proposed amendments do <u>not</u> include changes to the net income, net financial asset or net asset thresholds that must be satisfied for an individual to qualify as an accredited investor. 	May 28, 2014
Proposed amendments to existing accredited investor prospectus exemption – managed accounts	<ul style="list-style-type: none"> The proposed amendments would amend the definition of accredited investor in Ontario to allow fully managed accounts to purchase investment fund securities using the managed account category of the exemption, as is currently permitted in other CSA jurisdictions. 	May 28, 2014
Proposed amendments to existing minimum amount investment prospectus exemption	<ul style="list-style-type: none"> The proposed amendments would restrict the exemption to distributions to non-individual investors to address investor protection concerns associated with individuals investing under the exemption. 	May 28, 2014
Proposed amendments to existing report of exempt distribution	<ul style="list-style-type: none"> The proposed amendments would amend Form 45-106F1 <i>Report of Exempt Distribution</i> to enable the CSA to obtain additional information on distributions made in reliance on the accredited investor and other prospectus exemptions. 	May 28, 2014

Please see CSA Staff Notice 45-314 *Consolidated List of Current CSA Exempt Market Initiatives*, published on March 20, 2014, for further information.