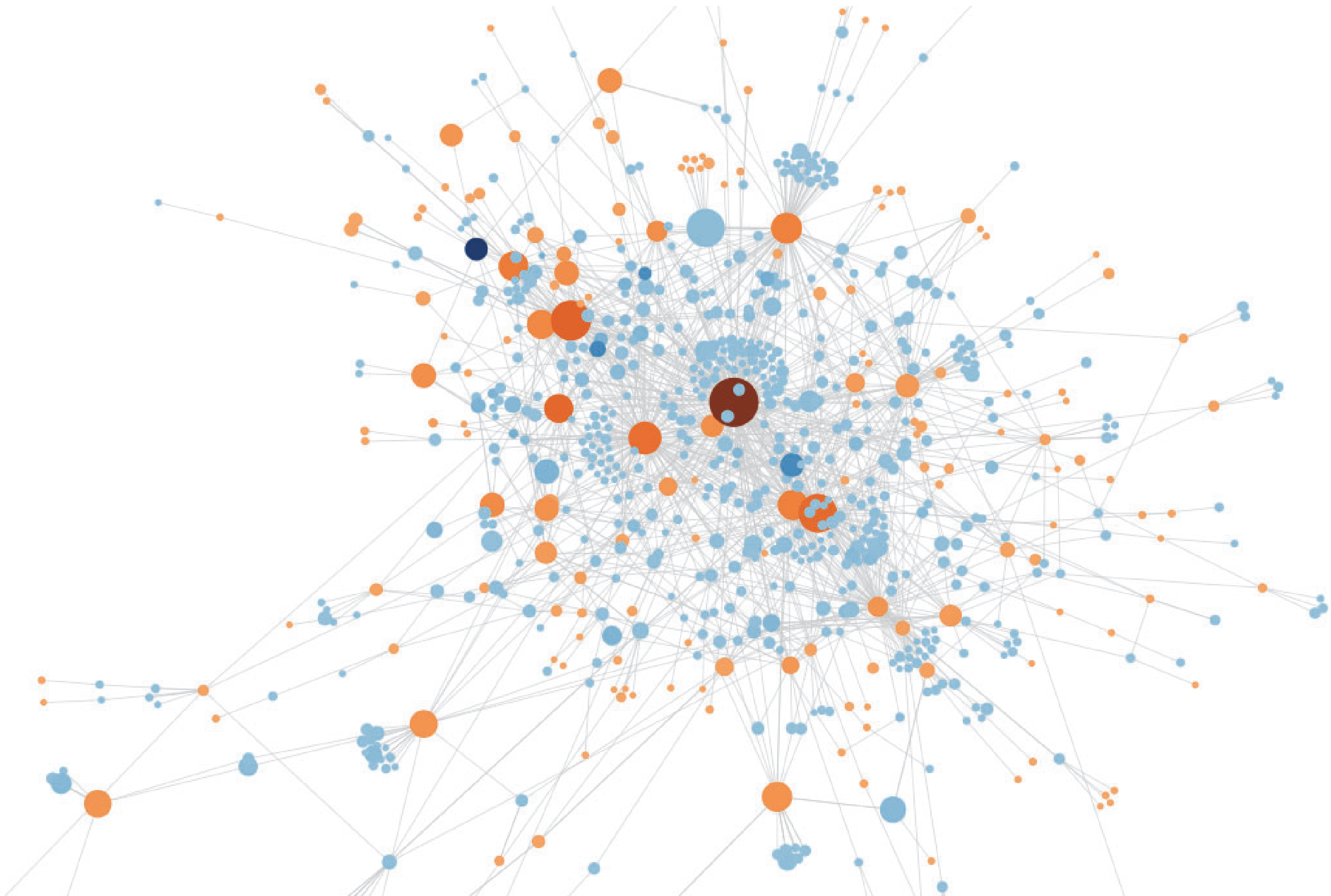
ONTARIO
SECURITIES
COMMISSION



ONTARIO EXEMPT MARKET REPORT

OSC Staff Notice 45-716

2018

ONTARIO EXEMPT MARKET REPORT 2018

TABLE OF CONTENTS

EXECUTIVE SUMMARY

The exempt market continues to be an important component of Ontario's capital market, with exempt market investments increasing in 2017.[1] Ontario institutional investors and residents invested approximately $91.6 billion in Canadian and foreign corporate (non-investment fund) issuers through prospectus-exempt offerings, a 27% increase from 2016.

This report provides a snap-shot of activity in Ontario's exempt market during 2017. The report covers capital raised by corporate issuers from Ontario-based investors during the period and highlights notable investor and issuer trends.

The key findings in this report include:

Investor Trends

- Capital raised from institutional investors[2] comprises approximately $89.4 billion (or 98%) of the total capital invested in Ontario's exempt market.
- Individual investors contributed $2.2 billion (2%) of the total capital invested in Ontario's exempt market.
- Individual investors represent a large proportion (77%) of the approximately 28,500 exempt market investors.
- Approximately 39% of total capital invested by individual investors and 10% of total capital invested by institutional investors went toward real estate or mortgage investments.

Issuer Trends

- Approximately 37% of Canadian issuers that accessed Ontario's exempt market were identified as small issuers[3], collectively accounting for less than 1% of the total capital raised in 2017.
- Close to half of the small Canadian issuers that raised capital in Ontario's exempt market were junior exploration companies, most of which were listed on a Canadian exchange.
- Small Canadian issuers that raised capital in Ontario's exempt market were also largely comprised of reporting issuers in other sectors/industries such as manufacturing, technology and life sciences.
- Although 1 in 4 small businesses relied on the family, friends and business associates exemption to raise capital, approximately 80% of their total capital was raised under the accredited investor exemption.

Impact of Newer Prospectus Exemptions

- Collectively, prospectus exemptions introduced since 2015 have continued to gain traction among issuers and investors in 2017.
- Total capital raised under the offering memorandum and family, friends and business associates exemptions doubled to $327 million since 2016.
- The offering memorandum and family, friends and business associates exemptions were used by just under 600 Canadian issuers in 2017. However, most issuers that relied on these exemptions raised most of their capital under the accredited investor exemption.
- The offering memorandum exemption has been largely used by real estate and mortgage investment entities.

[1] For more information about the exempt market, see OSC's "The exempt market" webpage at <http://www.osc.gov.on.ca/en/exempt-market.htm> or the OSC Investor Office's "The exempt market explained" webpage at <http://www.getsmarteraboutmoney.ca/>.

[2] For the purpose of this report, "institutional investor" refers to institutional investors and other non-individuals including companies, trusts or managed accounts purchasing on behalf of a beneficiary or group of beneficiaries. The "individual investor" (or "individuals") category refers to investors that were identified by their full legal name and not a corporation name or legal entity name. In some cases individual investors may also include named individuals that were purchasing on behalf of a beneficial owner.

[3] Small Canadian issuers are identified in this report as issuers with under $5 million in assets and less than $1 million in capital raised during the calendar year.

- There was no reported use of the crowdfunding prospectus exemption in 2017. However, there have been several exempt market dealers and other registered entities that have facilitated a crowdfunding-like model to raise capital predominantly from accredited investors.

The findings highlighted in this report will help inform the OSC's on-going efforts to monitor this growing market, both from an operational compliance perspective and to understand its role in capital formation for future policy making. The OSC's ongoing compliance and oversight efforts in the exempt market are outside the scope of this report. However, we note that the OSC's Compliance and Registrant Regulation Branch completed an initial sweep of compliance reviews of exempt market dealers that have facilitated the distribution of securities in reliance on the offering memorandum and family, friends and business associates exemptions. Please refer to OSC Staff Notice 33-748 *2017 OSC Annual Summary Report for Dealers, Advisers and Investment Fund Managers* for more information about this sweep. See also OSC Staff Notice 33-749 *2018 Annual Summary Report for Dealers, Advisers and Investment Fund Managers* for more information about compliance reviews and other topics of interest for exempt market dealers.

BACKGROUND

PURPOSE AND SCOPE

Using data contained in regulatory filings, this report provides a summary of trends related to exempt market capital raising activity in Ontario during 2017. The primary goal of the report is to inform market participants about exempt market activity, both in terms of businesses raising capital and investors allocating capital to businesses.

The report discusses the following:

- Annual growth and market composition
- Investor trends
- Issuer trends

The analysis is focused on exempt market capital raising by corporate issuers.

Canadian regulators adopted new prospectus exemptions beginning in 2015 to facilitate capital raising opportunities in the exempt market, especially for small and medium-sized enterprises. These prospectus exemptions also formed the basis of the OSC's exempt market reform initiative which was aimed at expanding investment opportunities for all investors, especially retail investors, while maintaining appropriate investor protections. The prospectus exemptions include the following:

- Existing security holder exemption – February 11, 2015
- Family, friends and business associates exemption – May 5, 2015
- Offering memorandum exemption – January 13, 2016
- Crowdfunding exemption – January 25, 2016

With this reform of the exempt market regime now complete, the OSC's focus has shifted to monitoring their impact and assessing whether they are achieving their expected regulatory outcomes, or if further regulatory responses are needed.

DATA

The data underlying the analysis was obtained from the Form 45-106F1 *Report of Exempt Distribution* ("the F1 Report") filed with the OSC by corporate issuers that raised capital from Ontario investors. Generally, issuers are required to file the F1 Report within 10 days of the first distribution date. Therefore, an issuer in continuous distribution over a period longer than 10 days is required to file multiple F1 Reports to cover the distribution period.

Only certain prospectus exemptions trigger a requirement to file an F1 Report and so the information gathered from the filings does not represent all exempt market activity. For more information on which exemptions require the filing of an F1 Report, see Part 6 of NI 45-106. For example, issuers with fewer than 50 investors (excluding current and former employees) can rely on the private issuer exemption under subsection 73.4(2) of the Securities Act (Ontario) (the Act) to raise capital and would not be required to file an F1 Report.[4]

The findings in this report incorporate several assumptions and inferences as a result of OSC staff analysis of filed F1 Reports. The analysis reflects information provided by filers at a point in time, and therefore may not reflect filer amendments that were submitted at a later date.[5]

[4] However, in some cases, written offering materials may be considered an "offering memorandum" and subject to a requirement to deliver the written offering materials to the OSC. See Part 5 of OSC Rule 45-501.

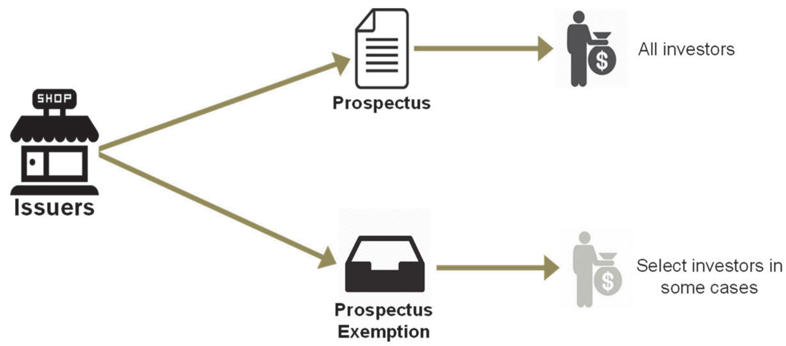
[5] Some issuers may have filed or amended Reports pertaining to 2017 distributions after the data was collected for this report. These amended filings and filings with missing information or data quality issues were excluded for this analysis. These types of filings represent less than 1% of all filings in a given year.

WHAT IS THE EXEMPT MARKET?

A company seeking to raise capital from investors may, generally, distribute securities either[6]:

- under a prospectus, or
- without a prospectus, in reliance on a prospectus exemption.

Figure 1 – How issuers raise capital from investors



One of the key principles of Canadian securities law is that securities may not be distributed unless a prospectus is filed with a Canadian securities regulator. A prospectus is a comprehensive disclosure document that sets out detailed information about an issuer and describes the securities being issued and the risks associated with purchasing those securities. An issuer that obtains a receipt from a Canadian securities regulator for a prospectus becomes a reporting issuer and can then use the prospectus to offer and sell securities to the public (i.e. all investors). Companies that are reporting issuers must make certain information about their activities and financial status available to the public. These reporting issuers may also choose to publicly list their securities on a Canadian stock exchange such as the Toronto Stock Exchange (TSX).

In certain cases, securities may be offered without a prospectus, in reliance on certain prospectus exemptions. The "exempt market" describes the segment of our capital markets where securities can be sold without the protections afforded by a prospectus. Such offerings are sometimes also referred to as exempt distributions or private placements. Most exemptions from the prospectus requirement are set out in Part XVII of the Act, OSC Rule 45-501 *Ontario Prospectus and Registration Exemptions* (OSC Rule 45-501) and National Instrument 45-106 *Prospectus Exemptions* (NI 45-106). Each prospectus exemption has its own rules about who can sell securities and who can buy securities under the specified exemption.

Each prospectus exemption is premised on a specific policy rationale that justifies not requiring a prospectus and, consequently, the distribution may be limited to certain classes of investors with specific attributes. Investors who buy securities through prospectus exemptions generally do not have the benefit of ongoing information about the issuer or the security that they are investing in. As well, they often do not have the ability to easily resell the security.

Companies that are reporting issuers may also rely on prospectus exemptions to raise capital either separately or concurrently with a prospectus offering.

[6] Issuers can also concurrently rely on both a prospectus and prospectus-exempt offering to raise capital especially in cross-border offerings or strategic deals.

MARKET PARTICIPANTS

There are three key stakeholders in the exempt market: issuers, investors and, in some transactions, intermediaries such as underwriters or dealers that assist in brokering transactions between issuers and investors.

Issuers across all sectors, sizes and jurisdictions, both Canadian and foreign, can access Ontario's exempt market.

Among the investors, institutional investors (such as pension funds, asset management firms, and other entities like investment trusts and corporations) account for most of the invested capital in the exempt market. The remaining investors are individual investors, comprised mainly of high-net-worth individuals, angel investors or individuals related to the issuer.

In some exempt market offerings, intermediaries such as underwriters, investment dealers or exempt market dealers may be involved.[7] Traditionally, the intermediary role was delegated to an individual or group of individuals; however, more recently, a few registered on-line portals have also been facilitating these exempt market transactions.

KEY MARKET SEGMENTS

Ontario's exempt market encompasses a mix of issuers and investors. Issuers with financing needs generally represent the demand for capital while investors provide the supply of this capital.

Figure 2 - Market segments identified

In this report, exempt market activity is broadly classified into broad investor and issuer segments as illustrated in Figure 2. The supply of capital or investor market consists of individuals and institutional investors. On the demand side, issuers have been grouped by relative size: small issuers and large issuers.

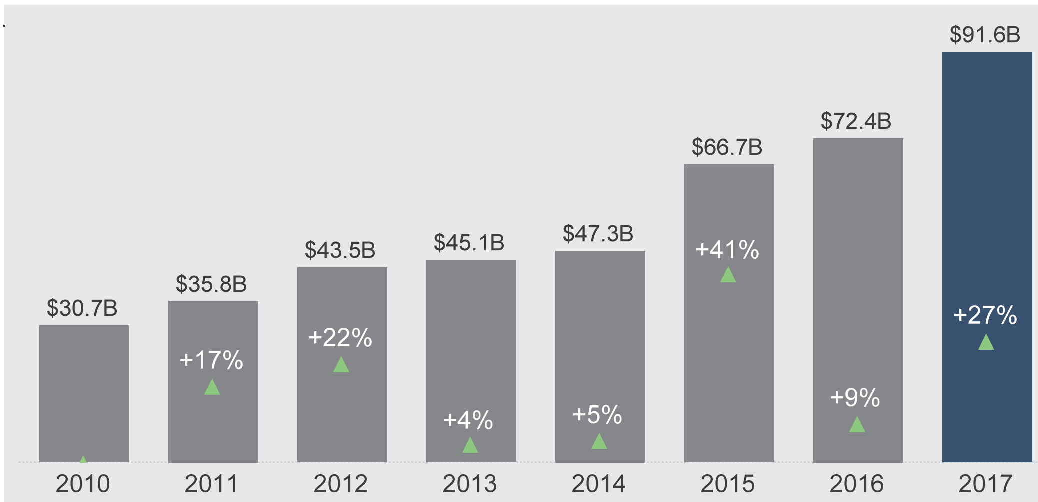
[7] Companies that rely on prospectus exemptions to distribute securities commonly rely on registered dealers to distribute the securities to investors. A company that seeks to distribute securities to investors without registered dealer involvement may itself be required to register as a dealer. For additional guidance on when companies and intermediaries need to be registered, see Companion Policy to National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations*.

ANNUAL GROWTH AND MARKET COMPOSITION

CAPITAL FLOWS REACHED NEW HIGHS IN 2017

Annual capital flows in Ontario's exempt market have been increasing over the years, as illustrated in Figure 3. Ontario investors allocated approximately $91.6 billion to roughly 2,970 corporate issuers through purchases of prospectus-exempt securities in 2017, nearly three times the size of similar capital flows in 2010. Capital raised through the exempt market in 2017 represents a 27% increase in proceeds raised from 2016 and a 17% increase in the number of issuers.

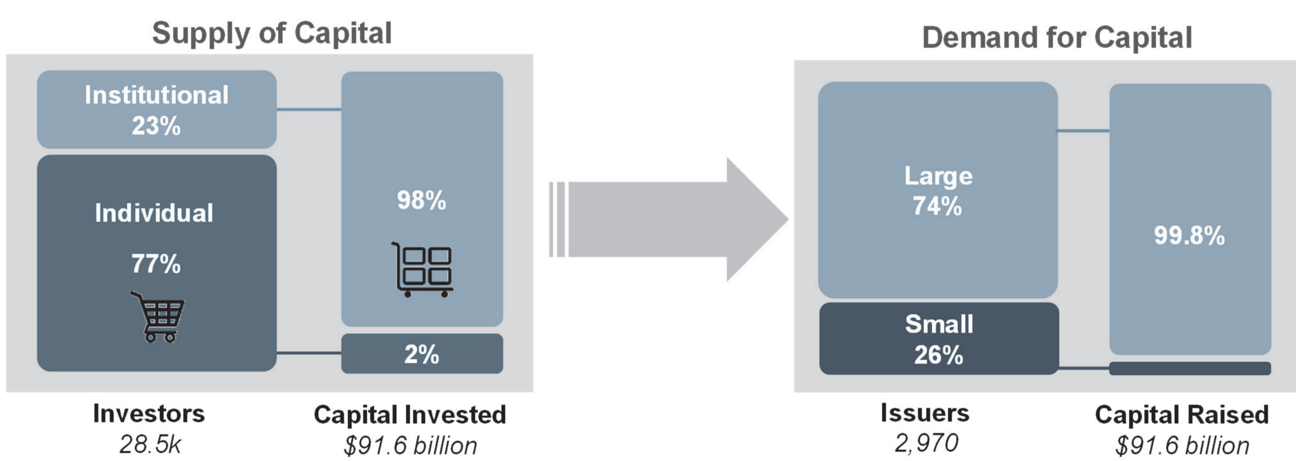
Figure 3 - Annual capital raised from Ontario investors



INSTITUTIONAL INVESTORS ACCOUNT FOR THE MAJORITY OF INVESTED CAPITAL

The exempt market is largely comprised of capital flows from institutional investors. In 2017, institutional investors invested approximately 98% of the aggregate capital raised by issuers while comprising less than one-quarter of Ontario investors purchasing prospectus-exempt securities (see Figure 4). The largest component of these capital flows from institutional investors continues to be invested in foreign (predominantly U.S-based) issuers ($54 billion) and mainly in the form of large fixed income issuances ($34 billion).

Figure 4 – 2017 Ontario exempt market

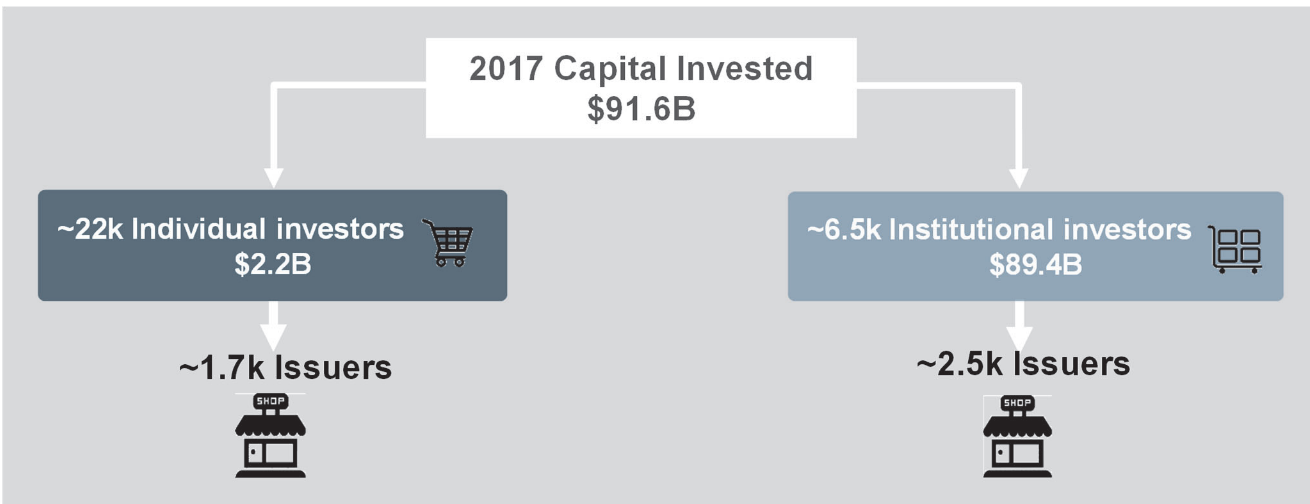


INVESTOR TRENDS

Investment activity and relative exposure across key sectors and asset classes differs significantly by investor group. Figure 5 illustrates the share of capital invested in Ontario's exempt market by individual and institutional investors in 2017. To summarize:

- 22,000 individual investors allocated $2.2 billion across 1,700 issuers.
- 6,500 institutional investors allocated $89.4 billion to 2,500 issuers.

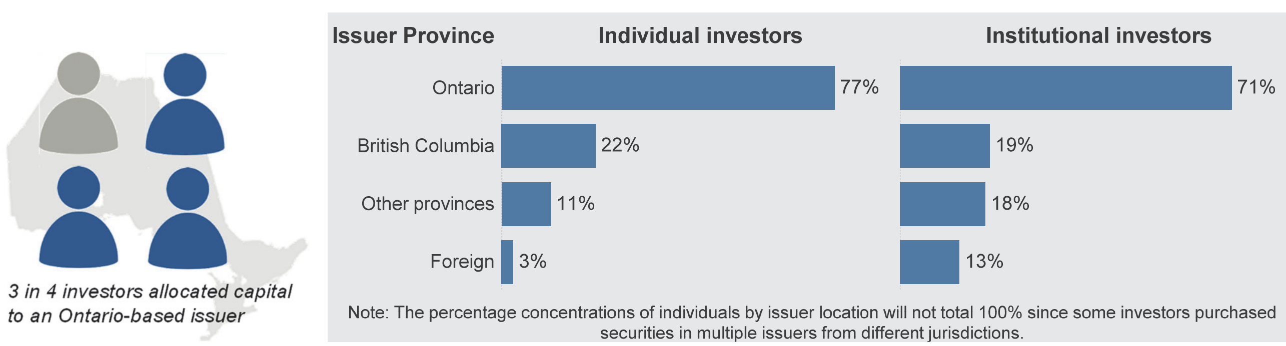
Figure 5 - 2017 Ontario exempt market activity by investor segment



INDIVIDUAL INVESTOR CAPITAL CONCENTRATED AMONG ONTARIO-BASED ISSUERS

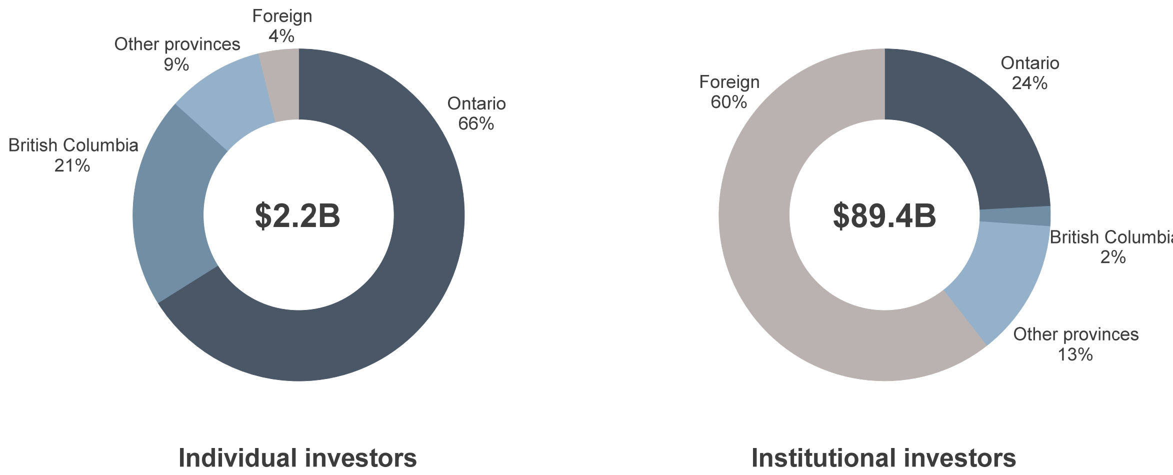
In both investor groups, roughly three out of every four investors allocated capital to an Ontario-based issuer (Figure 6).

Figure 6 - Proportion of investors by issuer's head office location



Ontario-based issuers also received the largest proportion (66%) of the total invested by individual investors (Figure 7). However, the total amount invested by institutional investors was disproportionately concentrated among foreign issuers. Foreign-based issuers were comprised of mostly large and well-established U.S.-based issuers in the financial and non-financial sector placing fixed income securities with institutional investors.

Figure 7 - Invested capital by issuer's head office location



MOST INDIVIDUAL INVESTORS HAD REAL ESTATE OR MORTGAGE-RELATED INVESTMENTS

In 2017, 2 in 5 exempt market investors (individuals and institutional investors) had allocated capital to an issuer that primarily held real estate or mortgage-related assets. However, individuals contributed a higher proportion of their invested capital in these issuers than institutional investors. Individual investors invested approximately $850 million (or 39% of total invested capital), whereas institutional investors invested $9.2 billion or 10% of their total invested capital (Figure 8).

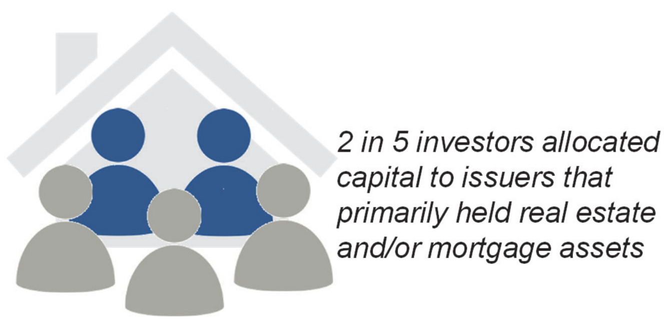
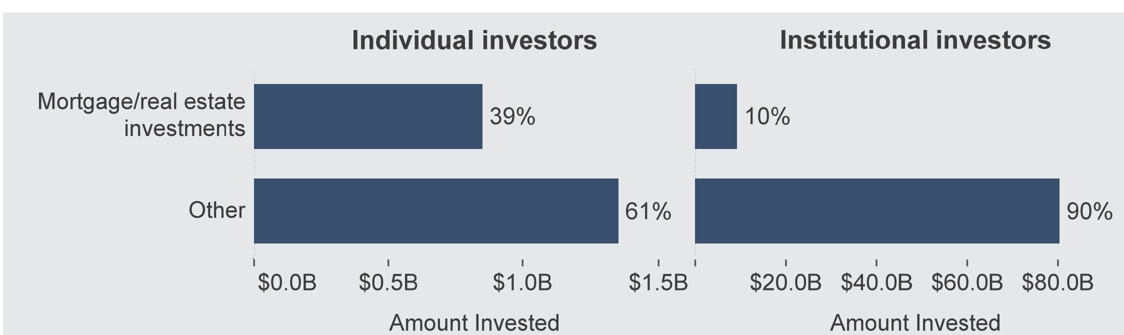


Figure 8 - Capital invested in issuers with real estate or mortgage-related assets

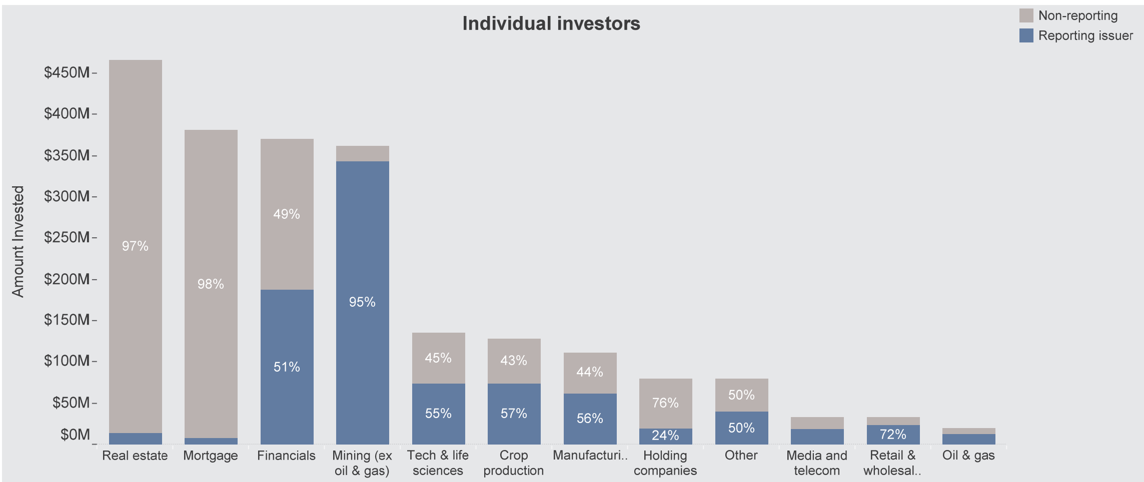


Individual investors allocated almost as much capital in issuers with real-estate assets as they did in issuers that primarily held mortgage assets (see Figure 9). Individuals also predominantly held investments in these real estate and mortgage issuers through an equity stake (~ 93% of capital invested). In contrast, institutional investors had most of their capital invested in real estate issuers (see Figure 10) and mainly through holdings of debt or other fixed income securities (~47% of invested capital). Issuers that held mortgage-related assets largely consisted of mortgage investment entities, whereas issuers with real estate assets included real estate investment trust (REITS), property development firms and other real estate investment companies.

INDIVIDUAL INVESTORS ALLOCATED MORE CAPITAL TO REPORTING ISSUERS

Individual investors allocated a high proportion of capital to reporting issuers, especially in key Canadian sectors such as mining, technology and life sciences. Individual investors continue to invest in these high-growth sectors, while changes to cannabis regulations have also attracted individual investors to the agriculture or crop production sector. Aside from real estate and mortgage investments which were comprised primarily of non-reporting issuers, individuals also invested significantly in other financial issuers (such as private equity or venture capital funds and linked-notes issued by commercial banks).

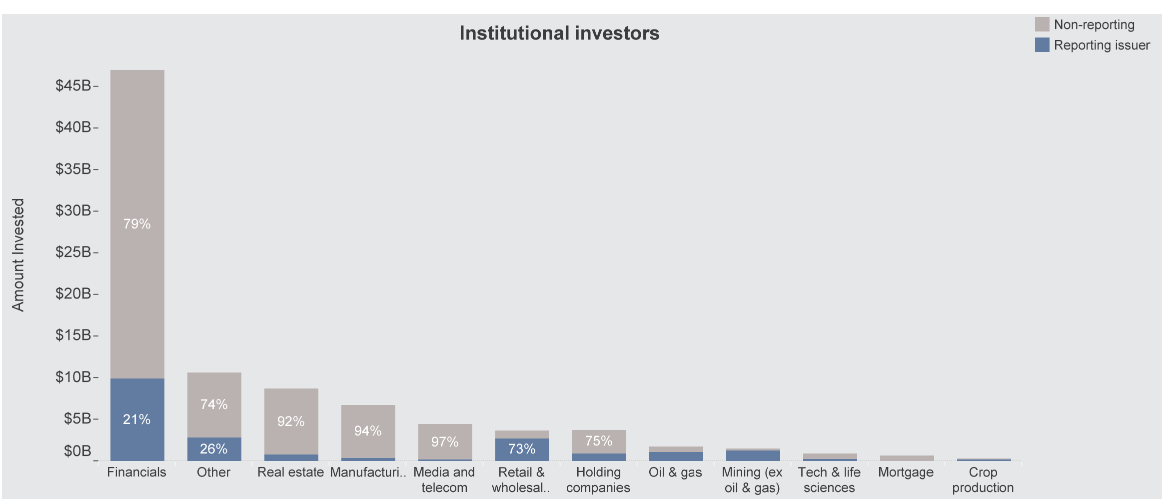
Figure 9 – Capital invested by individual investors across key sectors/industries



INSTITUTIONAL CAPITAL WAS LARGELY INVESTED IN FINANCIAL ISSUERS

Institutional investors allocated most of their capital to financial issuers (approximately $47 billion or 53% of total invested capital), with the top ten financial issuers in 2017 each raising over a billion dollars from institutional investors alone. These financial investments were mainly in the form of fixed income securities issued by financial credit intermediaries and foreign commercial banks, or equity investments in global private investment firms. Financial credit intermediaries in Ontario's exempt market raised capital predominantly from institutional investors and continued to be largely comprised of captive finance companies of global auto makers or securitization vehicles backed primarily by non-mortgage related consumer-debt. Institutional investors' exposure to commercials banks occurred mainly through large global debt offerings of senior unsecured medium-term notes. As Figure 10 demonstrates, aside from-financials, institutional investors invested their capital in more traditional sectors such as manufacturing, media, telecom and utilities.

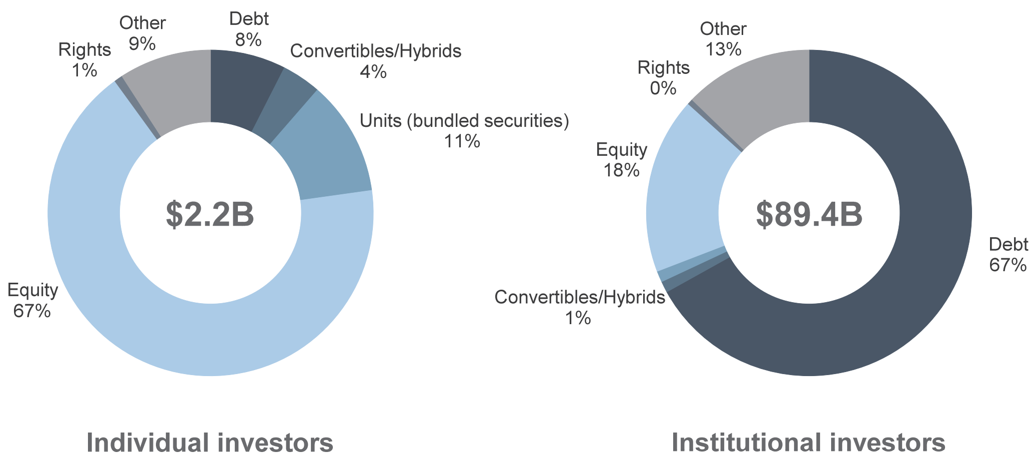
Figure 10 –Capital Invested by institutional investors across key sectors/industries



EQUITY WAS THE MOST COMMON TYPE OF SECURITY DISTRIBUTED

Individuals invested almost 90% of their capital in equity or non-debt offerings, while institutional investors invested 67% of their capital in debt or fixed income-type securities. These debt offerings were predominantly sold to a few large institutional investors as evidenced by the disproportionately small number of institutional investors (1 in 10) that participated in a debt offering. In contrast, a much larger proportion of institutional investors (2 in 3) participated in equity offerings.

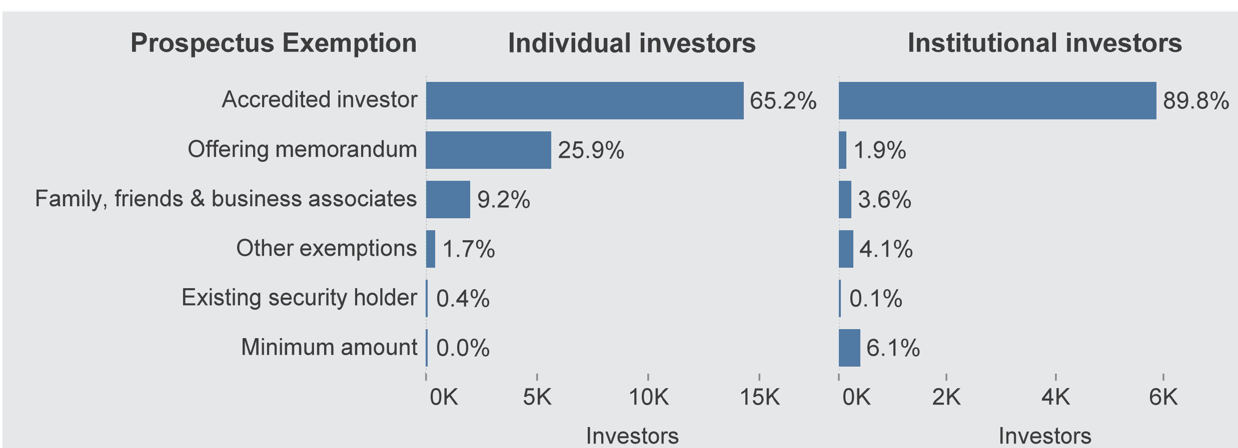
Figure 11 - Capital invested by security type



NEWER EXEMPTIONS INCREASINGLY USED BY INDIVIDUAL INVESTORS

The accredited investor exemption is still predominantly used to raise capital in Ontario. However, two newer exemptions – the family, friends and business associates and offering memorandum exemptions – have also been increasingly used by individual investors.[8] After the accredited investor exemption, the family, friends and business associates and offering memorandum exemptions were the most frequently used to raise capital from individual investors. In 2017, the family, friends and business associates and offering memorandum exemptions together accounted for approximately 7,600 individuals (or approximately 35% of all individual investors).

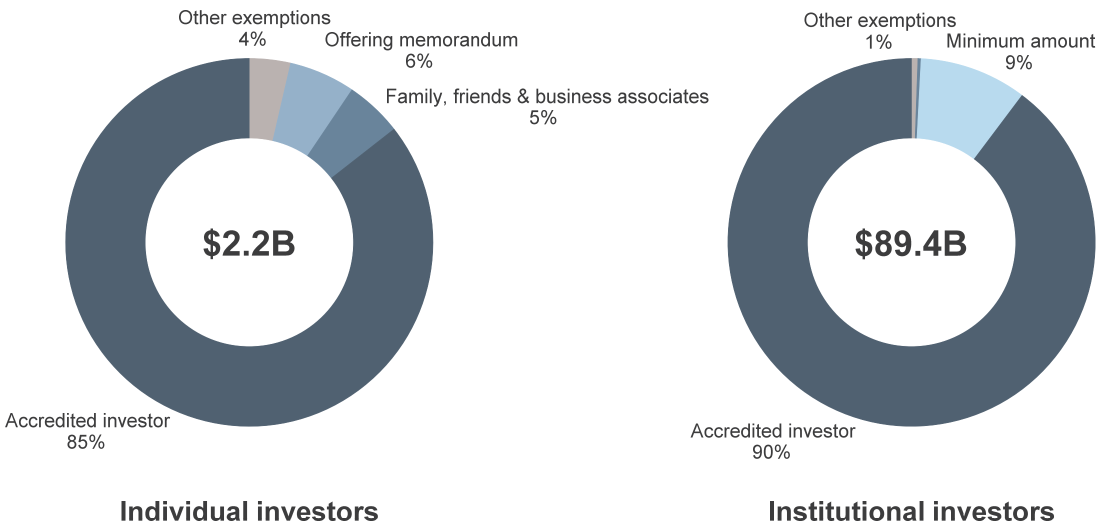
Figure 12 - Investors by exemption type



[8] For more information on the newer prospectus exemptions see "Summary of Key Capital Raising Prospectus Exemptions in Ontario," January 28, 2016 at <http://www.osc.gov.on.ca/documents/en/Securities-Category4/ni_20160128_45-106_key-capital-prospectus-exemptions.pdf>.

Although the offering memorandum exemption was relied on by twice the number of investors than the family, friends and business associates exemption, the offering memorandum exemption raised only marginally more capital ($124 million compared to $113 million).

Figure 13 - Capital Invested by prospectus-exemption

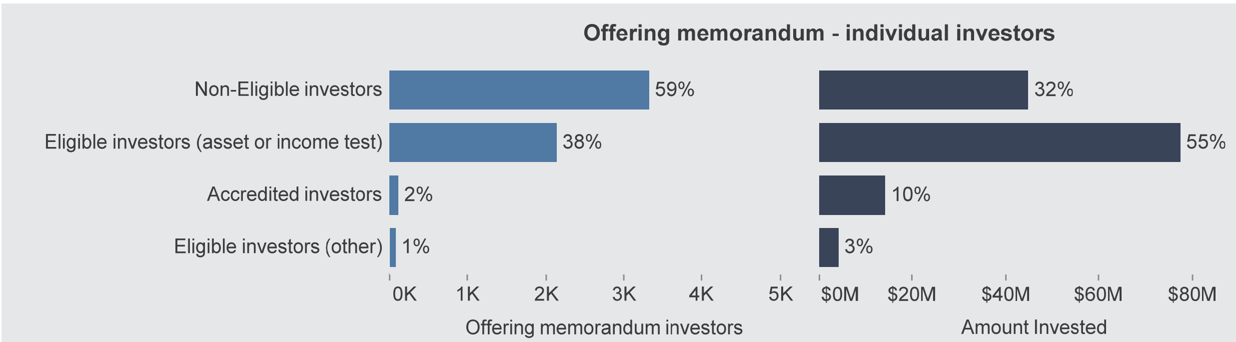


There have been no reported filings under the crowdfunding prospectus-exemption since it was implemented in January 2016. However, there have been several exempt market dealers and other registered entities that have facilitated a crowdfunding-like model to raise capital predominantly from accredited investors. In 2017, these registered portals or intermediaries are estimated to have facilitated just under $100 million in capital raised from Ontario investors.

ELIGIBLE INVESTORS ACCOUNTED FOR THE LARGEST SHARE OF DOLLARS RAISED

In Ontario, investors relying on the offering memorandum exemption are subject to investment limits depending on whether they qualify as an eligible investor.[9] Approximately 38% of offering memorandum investors were reported to be eligible investors (based on asset or income test) and together they invested 55% of the capital reported under the offering memorandum exemption in 2017. Roughly 2% of offering memorandum investors were also reported to be accredited investors, raising 10% of total capital.

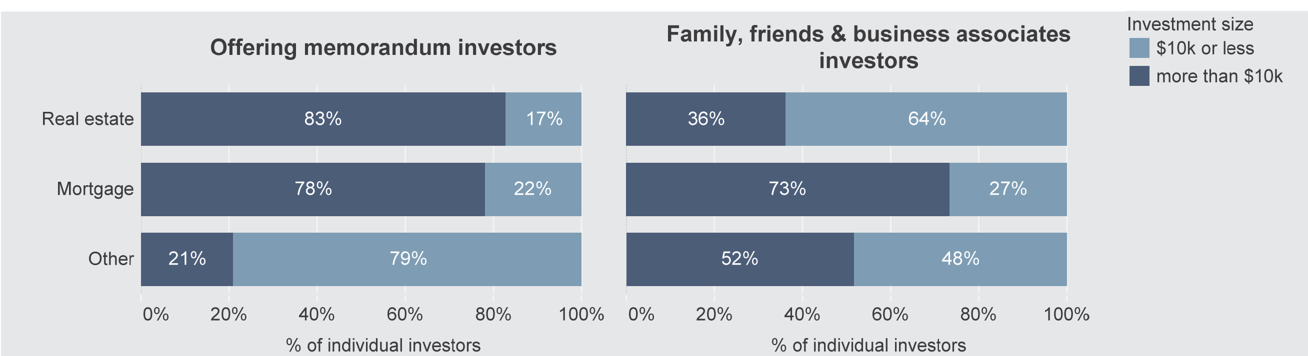
Figure 14 – Offering memorandum investor types



INDIVIDUAL INVESTORS UNDER THE OFFERING MEMORANDUM EXEMPTION MADE LARGE INVESTMENTS IN REAL ESTATE AND MORTGAGE ISSUERS

A high proportion of offering memorandum investors allocated more than $10,000 to real estate or mortgage investments over the year, especially when compared to investments in other sectors. Investments in real estate or mortgage issuers under the offering memorandum exemption were mainly comprised of investors that purchased more than $10,000 in securities. This ratio was considerably lower for offering memorandum investors in other sectors, where only 21% of investors invested more than $10,000.

Figure 15 - Investor breakdown by investment size



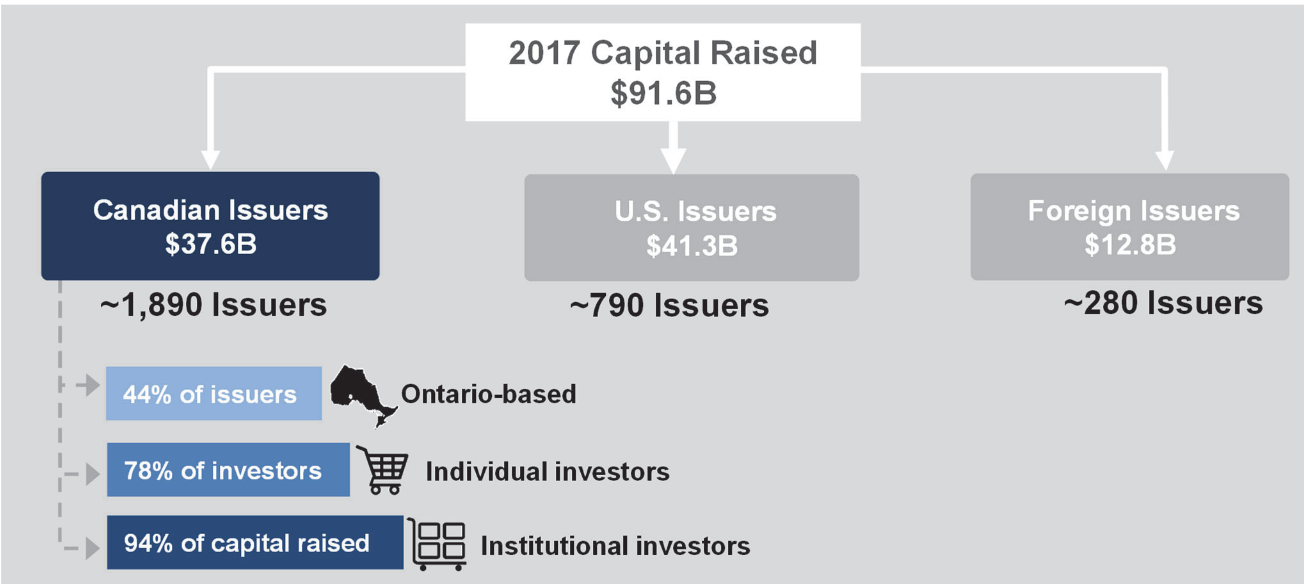
[9] For more information on eligible investors and investment limits under the offering memorandum exemption see "Summary of Key Capital Raising Prospectus Exemptions in Ontario", January 28, 2016 (http://www.osc.gov.on.ca/en/SecuritiesLaw_ni_20160128_45-106_key-capital-prospectus-exemptions.htm).

CANADIAN ISSUER TRENDS

This section provides a detailed analysis of Canadian issuers in Ontario's exempt market with an emphasis on small issuers and the impact of prospectus-exemptions introduced beginning in 2015.

Most exempt market issuers are based in Canada. In 2017, Ontario investors allocated about $37.6 billion to approximately 1,890 Canadian issuers. Although Canadian issuers raised 94% of their capital from institutional investors, their investor base was predominantly comprised of individual investors (78%). Approximately 44% of Canadian issuers were headquartered in Ontario. Those issuers raised a combined $23.3 billion in 2017 through the exempt market.

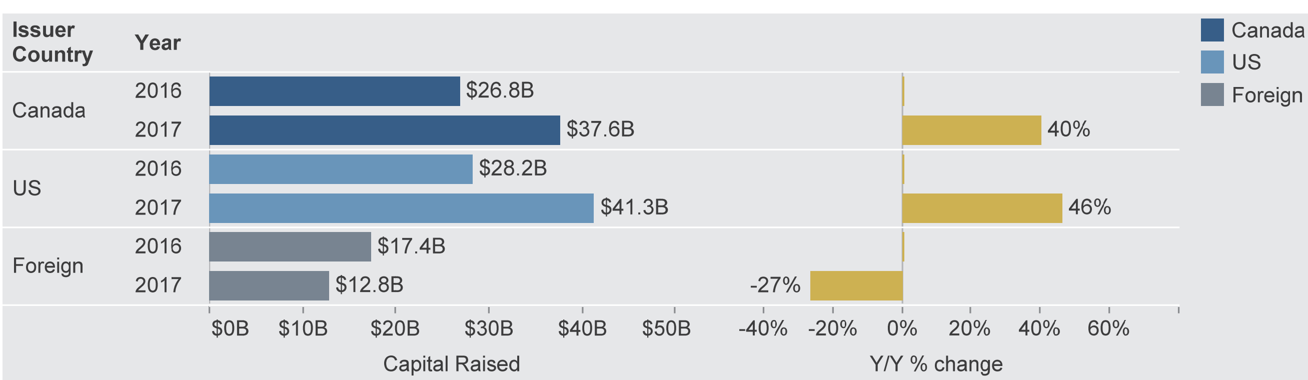
Figure 16 - Ontario exempt market activity by issuer location



HIGHER LEVEL OF CAPITAL RAISED BY CANADIAN AND U.S. ISSUERS

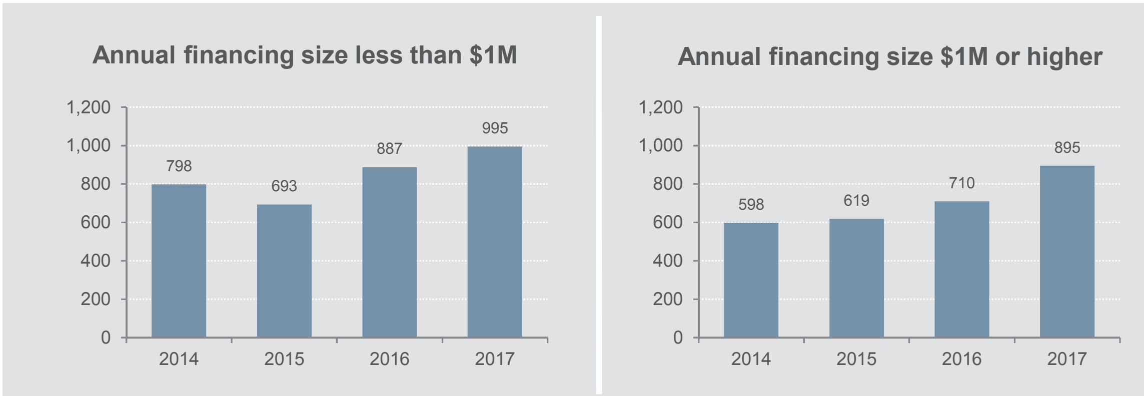
The number of Canadian and U.S. issuers has increased since 2016 by 18% and 16% respectively. Figure 17 displays the corresponding increase in the annual capital raised by Canadian and U.S. issuers in Ontario's exempt market. Although capital raised by foreign issuers dropped by 27% over the same period, there was a 25% increase in the number of foreign issuers that accessed Ontario's exempt market. Much of the capital raised by U.S. and other foreign issuers is in the form of fixed income securities that are purchased by Canadian institutional investors.

Figure 17 - Y/Y Capital raised by issuer country



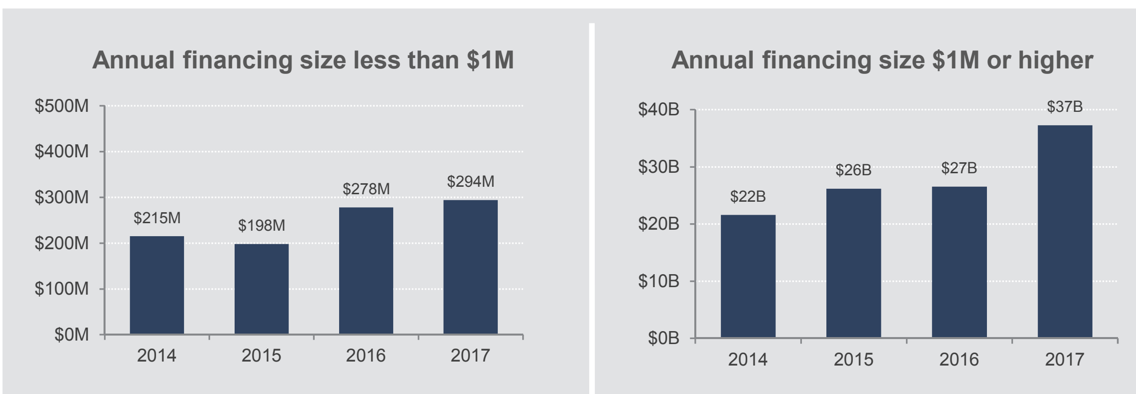
In 2017, almost 80% of U.S. and foreign issuers raised $1 million or more, but over half of Canadian issuers raised less than $1 million. Canadian issuers with smaller financings (less than $1M) have been quite active in Ontario's exempt market, marginally outnumbering foreign issuers and Canadian issuers with larger financings.

Figure 18 – Number of Canadian issuers by annual financing size



The number of Canadian issuers in both the small (under $1 million) and large financing groups ($1 million or more) increased since 2014, with a more notable increase in issuers with large financings in 2017 (Figure 18). The total capital raised by both small and large Canadian issuers has also increased from 2016 (Figure 19), but evidently more so for issuers that raised over $1 million.

Figure 19 - Total capital raised by Canadian issuers by annual financing size



REDEFINING SMALL BUSINESS ACTIVITY

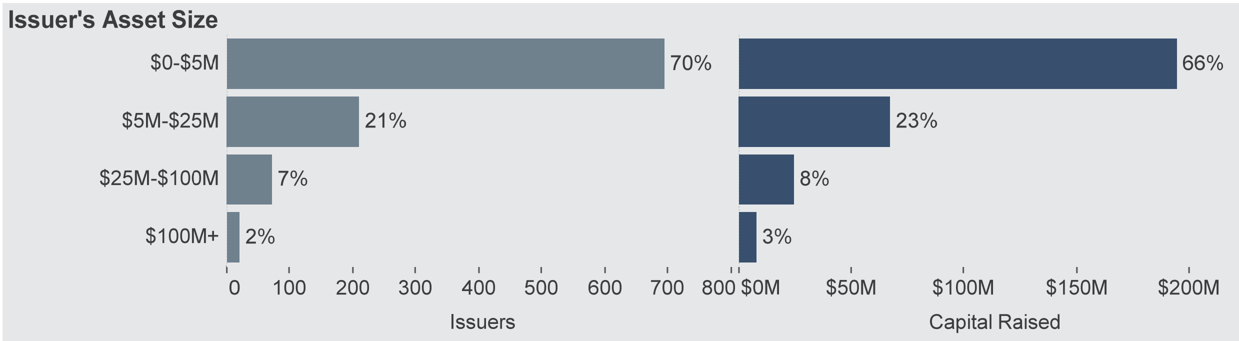
Our previous analysis of exempt market activity identified small issuers by an annual financing size of under $1 million.[10] Financing size provided the closest proxy to small issuer activity given the lack of issuer information that was collected on the F1 Report prior to June 2016. Since the implementation of the new F1 Report,[11] filers are now required to indicate the issuer's size of assets which has enabled us to refine our analysis of small issuers. In 2017, only 70% of issuers with an annual financing size of under $1 million had reported assets of under $5 million. The remaining issuers appear to be much larger entities based on their reported assets of $5 million or higher (Figure 20). Therefore, in order to capture exempt market activity by start-ups and issuers in early stages of funding, small Canadian issuers are identified in this report based on both annual financing size (under $1 million) and asset size (under $5 million).[12]

[10] For more information see "OSC Staff Notice 45-715, Ontario Exempt Market Report", June 2017.

[11] The new harmonized NI-45-106 F1 Reports of Exempt distribution came into effect on June 30, 2016. For more information see "CSA Notice of Amendments to National Instrument 45-106 Prospectus Exemptions relating to Reports of Exempt Distribution," April 7, 2016.

[12] An alternative option was to just rely on asset size as a proxy for small issuers, but our analysis found that under-reporting of asset size was common among financing subsidiaries of larger entities that raised more capital than the total assets they reported.

Figure 20 – Distribution of Canadian issuers that raised under $1 million in 2017 by their asset size



SMALL CANADIAN ISSUERS PREDOMINANTLY RAISED CAPITAL FROM INDIVIDUALS

In 2017, small Canadian issuers accounted for approximately 700 Canadian issuers (37%) and $194 million or less than 1% of total capital raised by all Canadian issuers. Small Canadian issuers predominantly raised their capital through the issuance of equity securities and bundled units (87% of gross proceeds) and their investor base consisted primarily of individual investors (77% of investors).

Figure 21- Small Canadian issuers in 2017

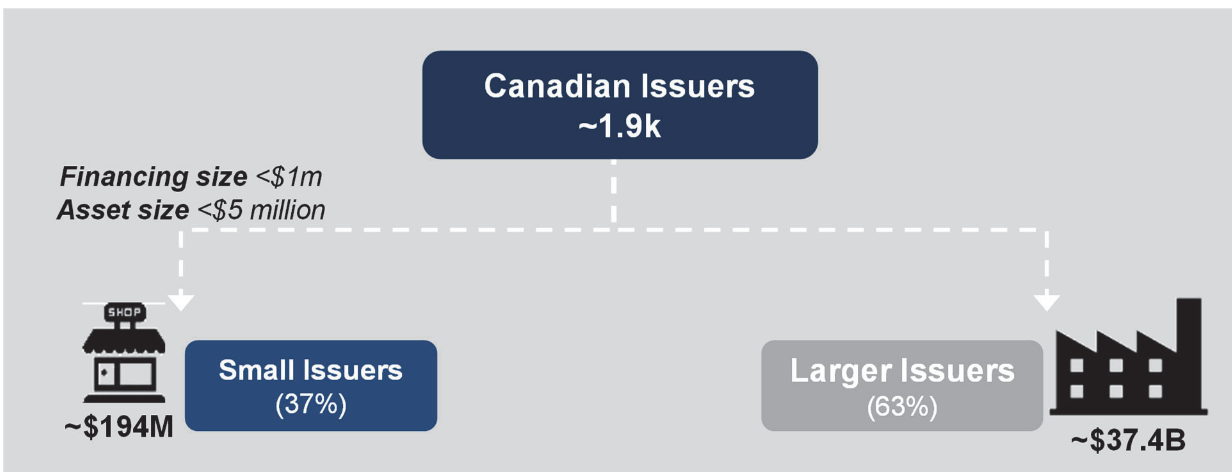
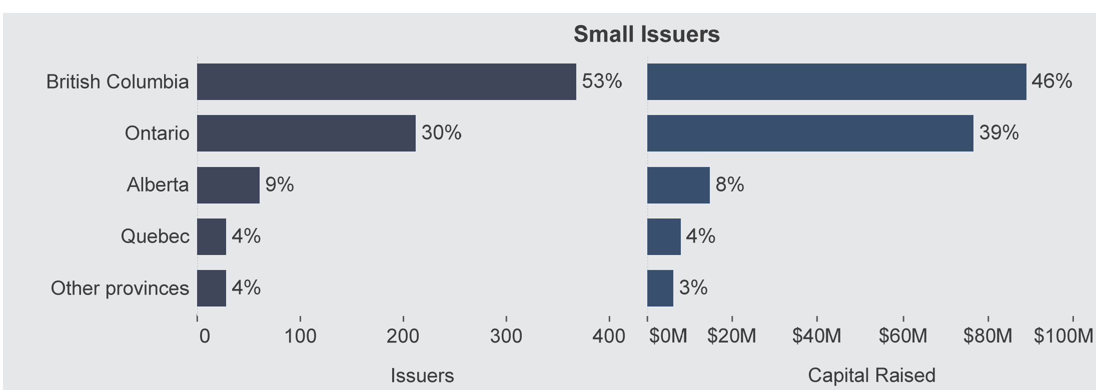


Figure 22 illustrates that most of these small issuers were based in British Columbia (53%) and Ontario (30%).

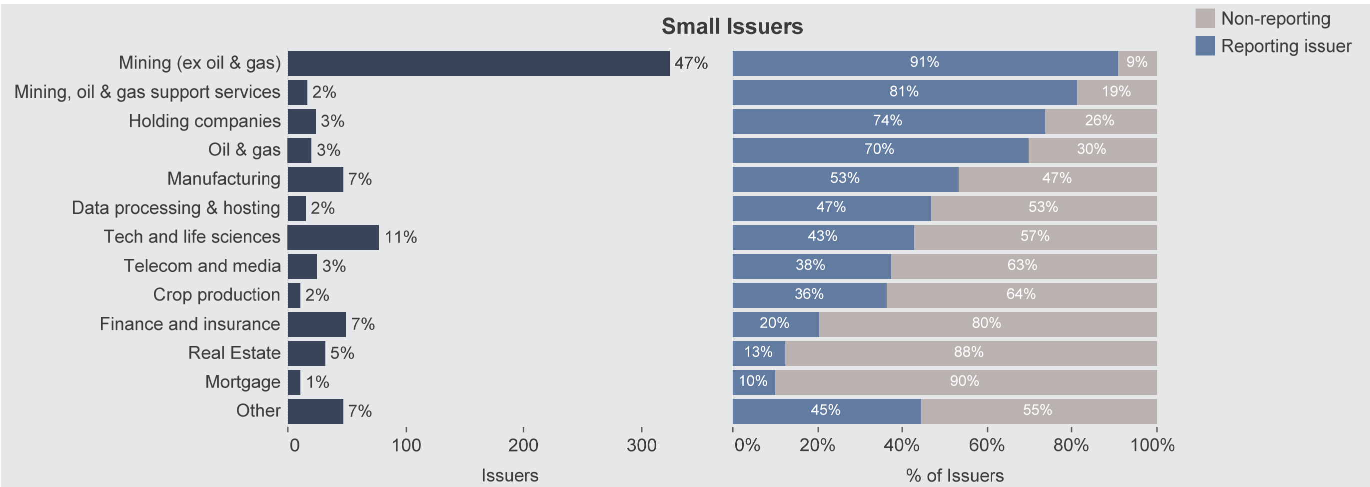
Figure 22 - Small issuers by HQ location



MINING FIRMS WERE THE MOST ACTIVE AMONG SMALL CANADIAN ISSUERS

Close to half of the small Canadian issuers identified were in the mining industry – 96% of these were in the exploration stage and 91% were reporting issuers. Small issuers were also present in other sectors including technology and life sciences, manufacturing and finance. Reporting issuers also comprised a sizeable proportion of small issuers especially in the non-financial sector (Figure 23).

Figure 23 – Small Canadian issuer by key sectors/industries



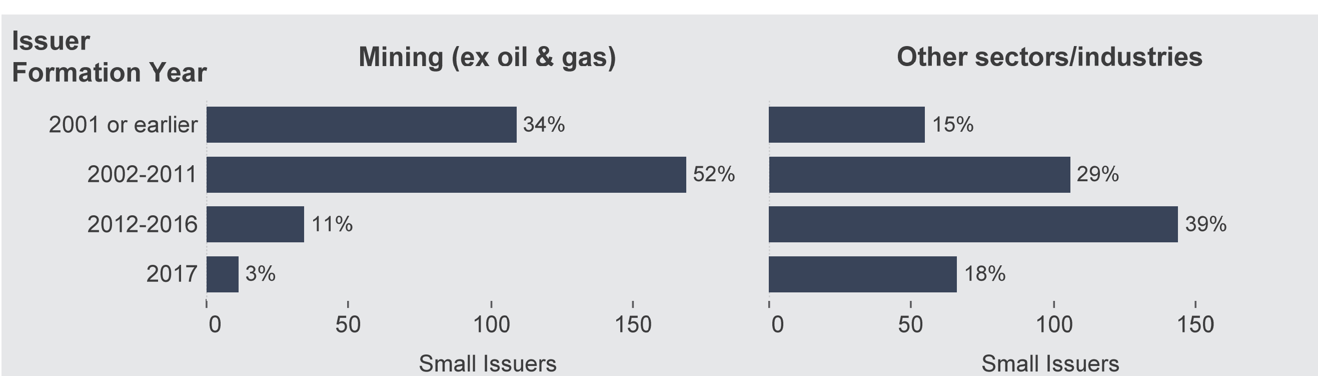
In 2017, Canadian mining issuers raised approximately $1.6 billion through Ontario's exempt market, although only $85 million (or 5%) went to small mining firms that raised less than $1 million and had total assets of under $5 million. Like small Canadian mining issuers, most of the large Canadian mining issuers were also in the exploration stage (81%). Exploration stage companies accounted for 95% of the capital raised by small mining issuers and just 60% of capital raised by large mining issuers. The remaining 40% of the capital raised by large mining issuers were in the production (31%) and development stage (9%).

Small Canadian mining firms relied predominantly on the accredited investor exemption to raise capital (88% of issuers, 83% of capital). However, the family, friends and business associates exemption was the second most relied upon exemption, used by about 1 in 4 small mining issuers and mainly in conjunction with the accredited investor exemption.

MOST SMALL MINING ISSUERS HAVE BEEN IN BUSINESS FOR AT LEAST 5 YEARS

A significantly large proportion (86%) of small mining issuers that rely on Ontario's exempt market to raise capital have been in business for over 5 years, whereas a higher proportion of small issuers from other sectors or industries have been in business for a shorter period of time (Figure 24).

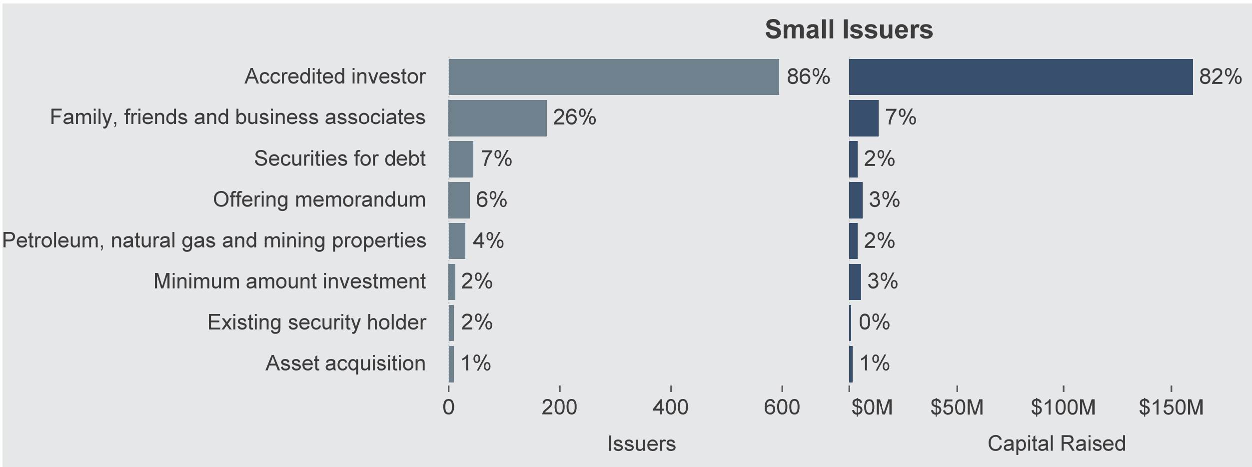
Figure 24 – Small Canadian Issuer's year of formation



SMALL ISSUERS RELY ON ACCREDITED INVESTORS AS MUCH AS LARGE ISSUERS

The accredited investor prospectus-exemption is used very broadly by both small and large issuers to raise capital from individuals and institutional investors. Approximately 86% of small issuers used the accredited investor exemption to raise capital. The accredited investor exemption also accounted for 82% of the total capital raised by small issuers. The family, friends and business associates exemption was used by just under 180 small Canadian issuers (approximately 26% or 1 in 4 small issuers) but only raised about 7% of small issuer capital (Figure 25). Many issuers that relied on the family, friends and business associates or offering memorandum exemption also relied on the accredited investor exemption concurrently to raise capital.

Figure 25 - Prospectus exemption use by small issuers

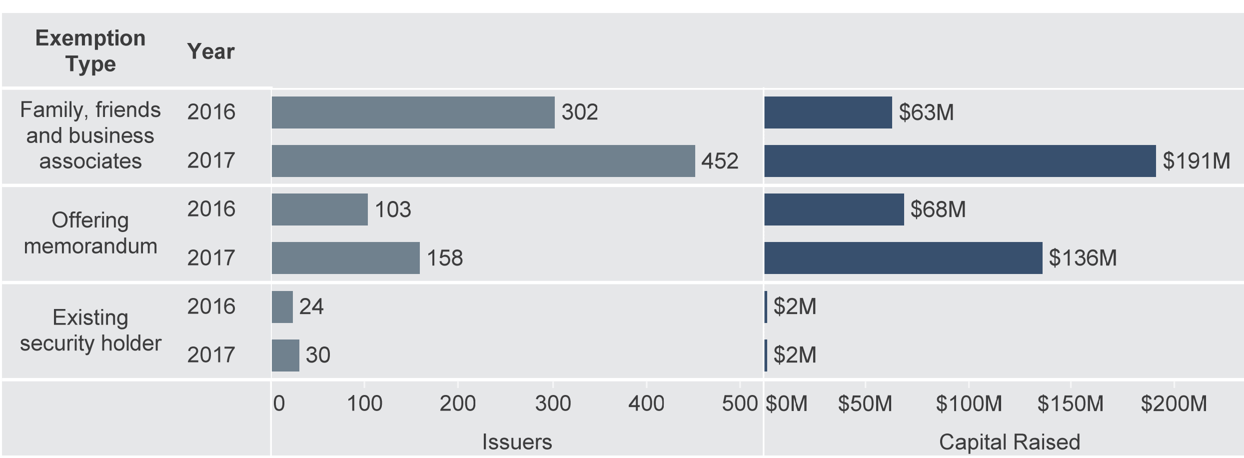


Note: The percentage of issuers across exemption types will not total 100% since some issuers may have raised capital under multiple prospectus exemptions and therefore be counted multiple times.

USE OF NEWER EXEMPTIONS HAS INCREASED

Collectively, the newer prospectus exemptions have gained traction among issuers in 2017. Among the four prospectus exemptions that were introduced in 2015 and 2016, the family, friends and business associates and offering memorandum exemptions have been the most frequently used and almost entirely by Canadian issuers raising capital from individual investors.[13] Since 2016, the combined amount raised under these two exemptions has doubled to approximately $327 million in 2017. The existing security holder exemption was used by only 30 issuers to raise a total of just under $2 million. There has been no reported use of the crowdfunding prospectus exemption in 2017.

Figure 26 - Newer prospectus exemptions



[13] For more information on the newer prospectus exemptions see "Summary of Key Capital Raising Prospectus Exemptions in Ontario," January 28, 2016 at <http://www.osc.gov.on.ca/documents/en/Securities-Category4/ni_20160128_45-106_key-capital-prospectus-exemptions.pdf>.

Although the family, friends and business associates and offering memorandum exemptions have been increasingly used by Canadian issuers, the total capital raised under both exemptions represents a small proportion of capital raised. Moreover, most issuers relying on these two exemptions raised larger sums of capital under other prospectus-exemptions, most notably the accredited investor exemption (Figure 27 and Figure 28). In 2017, there were fewer than 60 issuers that solely relied on the family, friends and business associates exemptions and fewer than 40 issuers that relied only on the offering memorandum exemption.

Figure 27 – Other exemptions used by issuers relying on the family, friends and business associates exemption

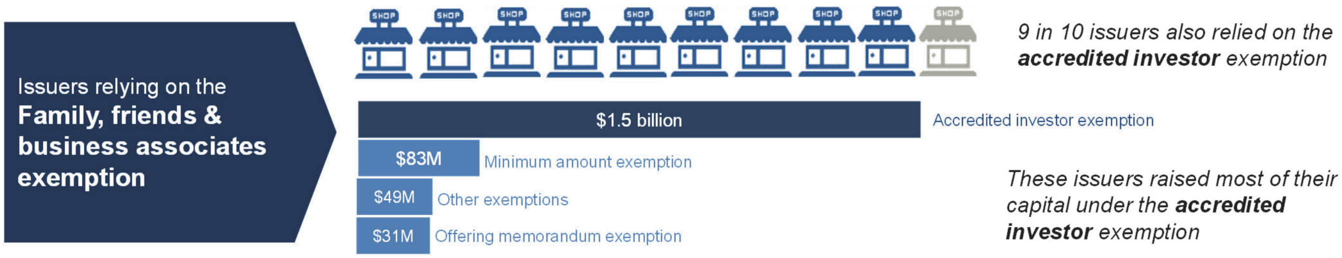
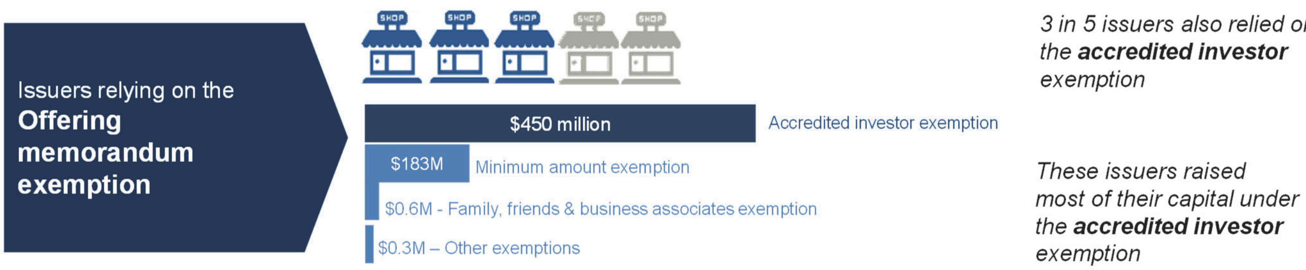


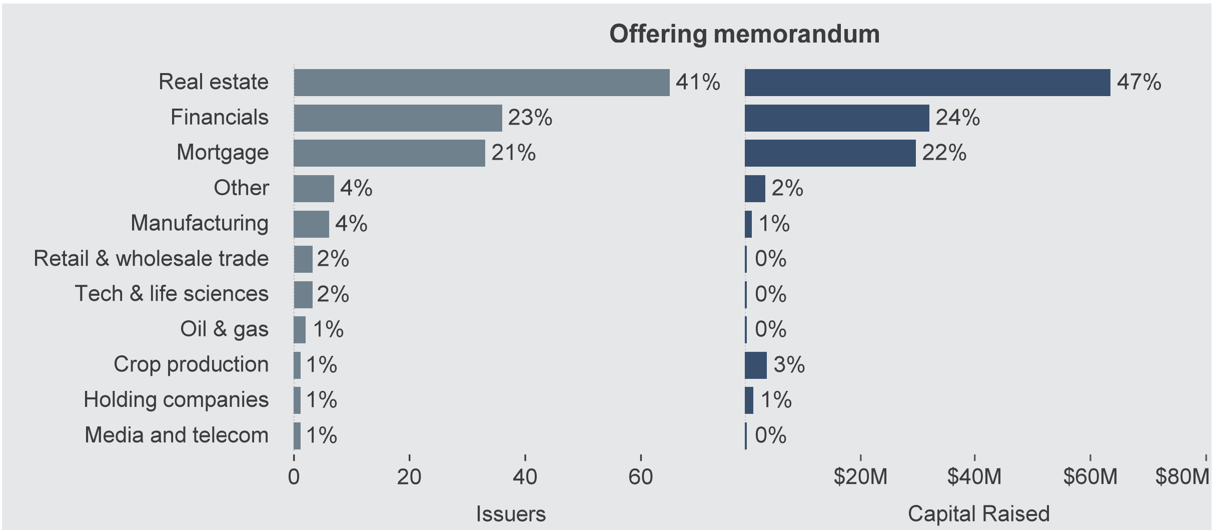
Figure 28 - Other exemptions used by issuers relying on the offering memorandum exemption



USE OF THE NEWER EXEMPTIONS IS CONCENTRATED IN CERTAIN INDUSTRIES

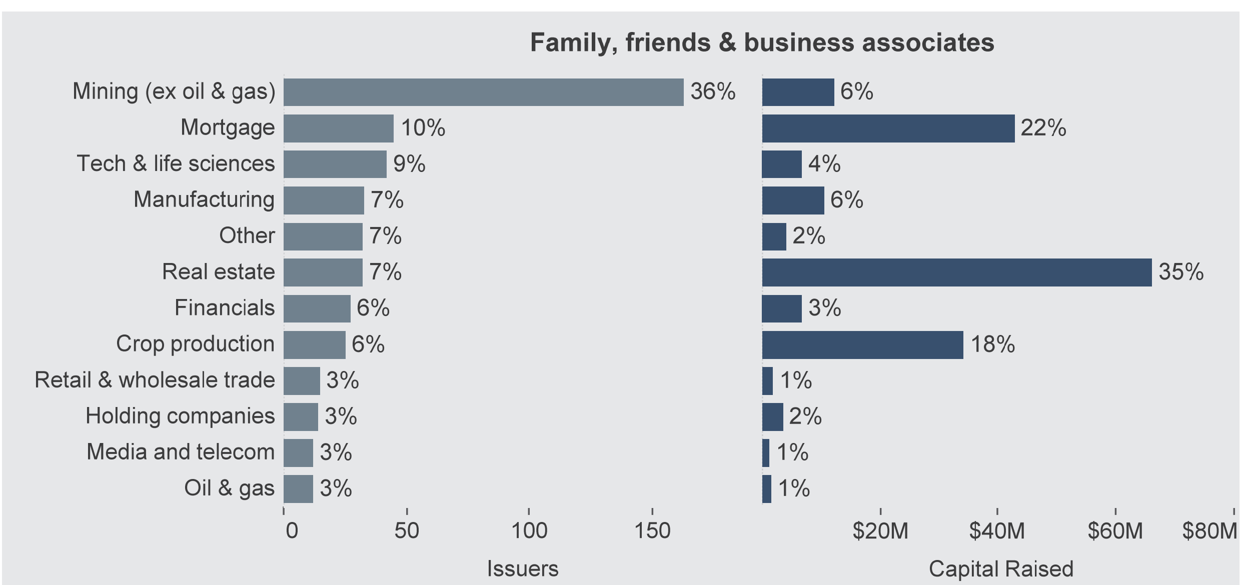
Since the offering memorandum exemption was introduced, it has largely been used by real estate and mortgage investment entities. In 2017, these issuers received approximately 70% of the total capital invested under the offering memorandum exemption, while most of the remaining capital (24%) was allocated to other financial issuers (Figure 29).

Figure 29- Key sectors/industries of issuers that relied on the offering memorandum exemption



Real estate and mortgage investment entities were also responsible for a sizeable share of the capital raised (57%) under the family, friends and business associates exemption. However, unlike the offering memorandum exemption, issuers from various other sectors were responsible for the remaining capital raised under the family, friends and business associates exemption. Most notable among these sectors was crop production which primarily consisted of cannabis issuers. Roughly 36% of the issuers relying on the family, friends and business associates exemption were in the mining industry, although this translated to only 6% of the capital raised under the exemption.

Figure 30 – Key sectors/industries of issuers that relied on the family, friends and business associates exemption



NEXT STEPS

The findings highlighted above and in future exempt market activity reports will help inform the OSC's on-going efforts to monitor this growing market, both from an operational compliance perspective and to understand its role in capital formation for future policy making. In the last two years, the OSC's Compliance and Registrant Regulation Branch has also completed a compliance review of exempt market dealers that facilitated the distribution of securities in reliance on the offering memorandum and family, friends and business associates exemptions.[14]

The amount of capital raised under the recently introduced offering memorandum and family, friends and business associates exemptions have more than doubled in the last year. Small issuers are also making use of these capital raising prospectus exemptions, but the accredited investor exemption continues to account for a much larger share of their total financing activity.

Although there has been no reported use of the crowdfunding prospectus exemption in 2017, there have been several exempt market dealers and other registered entities that have facilitated a crowdfunding-like model to raise capital predominantly from accredited investors. In 2017, these registered portals or intermediaries are estimated to have facilitated just under $100 million in capital raised from Ontario investors. In addition, the OSC, together with its CSA partners, plans to consider ways that crowdfunding can be a more effective capital-raising tool for start-ups and small issuers.

[14] Please refer to OSC Staff Notice *33-748 2017 OSC Annual Summary Report for Dealers, Advisers and Investment Fund Managers* and OSC Staff Notice 33-749 *2018 Annual Summary Report for Dealers, Advisers and Investment Fund Managers* for more information about compliance reviews and other topics of interest for exempt market dealers.

QUESTIONS

Please refer your questions to any of the following OSC staff:

Kevin Yang
Senior Research Analyst, Strategy and Operations Branch
Ontario Securities Commission
416-204-8983
kyang@osc.gov.on.ca

Robert Dryden
Research Analyst, Strategy and Operations Branch
Ontario Securities Commission
416-263-7661
rdryden@osc.gov.on.ca

Jo-Anne Matear
Manager, Corporate Finance Branch
Ontario Securities Commission
416-593-2323
jmatear@osc.gov.on.ca

Samreen Beg
Legal Counsel, Corporate Finance Branch
Ontario Securities Commission
416-597-7817
sbeg@osc.gov.on.ca