

## Corporate Securities Law

December 21, 2012

### Ontario Securities Commission Considering Crowdfunding and Other New Prospectus Exemptions

The Ontario Securities Commission (the “OSC”) recently published Consultation Paper 45-710 *Considerations For New Capital Raising Prospectus Exemptions* (the “**Consultation Paper**”). The Consultation Paper seeks feedback on concept ideas for new prospectus exemptions in Ontario aimed at giving start-ups and small and medium sized enterprises greater access to capital markets while maintaining appropriate investor protection.

The Consultation Paper is an extension of the Canadian Securities Administrators’ (“CSA”) review of the minimum amount (\$150,000) and accredited investor exemptions. That review is ongoing, with conclusions to be reported in 2013. During consultations associated with the CSA review, many stakeholders highlighted the desirability of providing greater access to the exempt market for both issuers and investors as well as further harmonization of prospectus exemptions across Canada. That feedback prompted the OSC to initiate a broader review of the exempt market, including consideration of whether new prospectus exemptions should be introduced in Ontario.

The principal potential prospectus exemptions discussed in the Consultation Paper are:

- crowdfunding
- offering memorandum
- “sophisticated” investor
- registrant advice

#### Crowdfunding

Crowdfunding is a way of funding projects or ventures by raising small amounts of money from a large number of people via an internet portal. In the United States, the *Jumpstart Our Business Startups Act* (the “**JOBS Act**”) created a crowdfunding exemption subject to the adop-

tion of (as yet unreleased) rules by the Securities and Exchange Commission.

The Consultation Paper outlines a conceptual crowdfunding exemption that encompasses many of the elements contemplated by the JOBS Act. It would let Canadian issuers to raise up to \$1.5 million in any 12-month period by crowdfunding through a internet portal registered in an appropriate dealer or adviser category.

The crowdfunding exemption would allow securities to be sold to any investor, regardless of his/her income, net worth or investment sophistication. As a result, the exemption would be subject to several conditions designed to provide greater investor protection, such as: (a) limits on the amount an investor can invest in reliance on the exemption (\$2,500 in any single investment and a maximum of \$10,000 per year); (b) disclosure requirements (a ‘streamlined’ information statement and financial statements); (c) investor execution of a risk acknowledgement form; (d) a two-business day “cooling off” period; and (e) provision of ongoing disclosure.

#### Offering Memorandum

Ontario is currently the only Canadian jurisdiction that does not have a prospectus exemption for distributions made pursuant to an offering memorandum. The Consultation Paper suggests that the OSC is prepared to consider adopting an offering memorandum exemption in Ontario.

The conceptual offering memorandum exemption would be subject to most of the same restrictions as the crowdfunding exemption, including limitations on the amount that could be raised using the exemption in any 12-month period and on the amounts each investor could invest. As a result, the offering memorandum exemption outlined in the Consultation Paper would be significantly more constrained than the offering memorandum exemptions in other Canadian provinces, which do not limit the amount that an issuer can raise in reliance on the exemption and have no or much less restrictive limits on the amount individual investors can invest.

#### Investment Knowledge

The Consultation Paper considers a new prospectus exemption for distributions to “sophisticated”

# Goodmans<sup>LLP</sup> Update

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investors who satisfy work experience (at least one year in the investment industry in a position that requires knowledge of securities investments) and education (CFA Charter, CIM designation or MBA) requirements. A similar concept is currently found in the United Kingdom's regulatory regime. Like the accredited investor exemption, there would be no restrictions on: (a) the type of security that may be distributed; (b) the size of the investor's investment; or (c) the size of the offering.

The OSC notes that this exemption may provide greater investment opportunities for "sophisticated" investors and may increase the investor pool for issuers. On the other hand, the OSC recognizes a number of challenges associated with the concept including: (a) a potentially small impact; (b) implementation and compliance issues; (c) appropriate framing of qualification criteria; and (d) implications for the registration regime.

## **Registrant Advice and EMDs**

The Consultation Paper also considers a new prospectus exemption for distributions to investors who have received appropriate advice from a registrant. Only dealing representatives within the investment dealer would

be qualified to provide advice for the purposes of the exemption. Investment dealers do not include other types of registrants, such as exempt market dealers ("EMD").

On a related note, the Consultation Paper points out in a number of places that the OSC has concerns that a number of EMDs are not operating in a manner that is compliant with applicable regulatory requirements. This suggests that the OSC will continue to closely scrutinize the operations of EMDs and may be considering whether any changes in the regulatory regime applicable to EMDs are required.

## **Status**

The Consultation Paper is intended as an initial step in soliciting input from all interested stakeholders on access to exempt markets, including the potential new prospectus exemptions it describes. The OSC has asked for comments on the Consultation Paper by February 12, 2013.

For further information on the Consultation Paper and the proposed new prospectus exemptions, please contact any member of our Corporate Securities Group.