Submission to the Ontario Securities Commission on Regulatory Burden

From the National Crowdfunding & FinTech Association of Canada

March 1, 2019

National Crowdfunding & Fintech Association

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Executive Summary

In response to the Ontario Securities Commission's (OSC's) January 14, 2019 request for comments, this submission responds to the eight questions set out in the OSC's Staff Notice 11-784. This submission draws heavily on, and also updates, the Association's earlier submission to the OSC dated August 24, 2017 (see Appendix), which primarily focused on the crowdfunding requirements in Ontario.

The National Crowdfunding and Fintech Association of Canada (the Association) represents over 2,000 fintech SMEs and individual members that support financial and capital market innovation, small businesses and technology. We are pleased that the Ontario government is undertaking this important regulatory burden reduction initiative to the benefit of all Ontarians.

The Association has consulted a number of diverse crowdfunding and fintech stakeholders – including exempt market dealers, industry experts, securities lawyers, regulators and government agencies and is proposing several recommendations to reduce unjustifiable burdens placed on Ontario's businesses.

The Association recommends that the province undertake the following:

• The OSC conduct a review and publish a report evaluating the effectiveness of Ontario's crowdfunding regulations (45-108) compared to other jurisdictions in Canada and international competitors such as the UK, US and Australia, including a comparison of the relative cost of capital;

• The OSC continue its recently announced work to harmonize the crowdfunding regime across Canada (CSA Staff Notice 45-324) but do so with the goal of reducing unjustified regulatory burden and establishing harmonized regulation that make sense for the sector. In particular, all jurisdictions should review B.C.'s crowdfunding regime and consider either adopting a similar approach in harmonization;

• Modify existing requirements so that they are principles based – detailed or prescriptive controls should only be imposed when clearly justified (ie. controls that can be quantified) and harmonized;

• Implement specific burden reduction amendments to crowdfunding regulations:
– Increase the 12 month issuer cap to $5 million or higher (from $1.5 million);
– Increase the 12 month investor caps to $10k (from $2.5k) and allow accredited investors to fully participate;
– Allow advertising and general solicitation on social media for all crowdfunding;
– Eliminate requirements for financial statements unless raising more than $1.5 million; and
– Allow fintech solution to streamline KYC and suitability tests.

Implementing these recommendations will help drive entrepreneurship, innovation and job growth. Benefits to Ontario include:

• Increased capital investment in the province and increased economic growth;

• Increased investment options for investors that support small businesses across all of Ontario;

• Crowdfunding sources remain in Canada;

• More capital and improved access to capital specifically for small businesses, rural businesses, economically-

challenged sectors, and underserviced groups (ie. women or Indigenous business owners);

• Encourages liquidity and transparency in the markets;

• Improved probability of retaining high growth companies in Ontario; and

• Accelerated commercialization of new products and services.

Crowdfunding drives innovation, economic activity and job growth. It fills a critical early stage funding gap (commonly referred to as the 'valley of death'), enables more productive investment in venture markets and strengthens early stage capital markets. Crowdlending also provides support to more mature companies looking to access capital that may fall outside the parameters of bank lending.

Background and Context

Contrary to the intent of the crowdfunding exemption, Ontario's crowdfunding requirements hinder access to capital for SMEs across a multitude of sectors. These requirements have also restricted innovative opportunities for retail investors and our members feel the impact of this directly. Ontario's economic growth is being hindered by regulation like the crowdfunding requirements that fails to promote economic growth. The potential of opening up regulation is significant increase in job creation and economic development. For example, Ontario's 417,000 small businesses would benefit from the increased access to capital that crowdlending offers and the effects would be a strong boost in job creation throughout the province.

Canada has fallen behind international competitors like the U.K. and the U.S. Crowdfunding platforms now represent the largest investments at the seed stage in the U.K. and peer-to-peer platforms now represent 15% of all new bank lending to small businesses.

> "Regulation Crowdfunding is proving to be a jobs engine (creating on average 2.9 jobs per issuer), economic generator (pumping over $289 million of revenues into local economies)."– Crowdfund Capital Advisors US (2018 data)
>
> "U.K. crowdfunding platforms [are] involved in 24% of all equity deals in 2017, but had a larger share of seed stage deals, with 30% of seed stage deals in 2017." – British Business Bank, Small Business Equity Tracker 2018

Ontario's Fintech startups, small business innovators and entrepreneurs operate in a highly prescriptive, complex and costly regulatory environment:

"The Crowdfunding Exemption introduced by the [OSC] in January 2016 turned out to be much too onerous for young companies… Ontarians are locked out of equity crowdfunding and Canadian companies are restricted from accessing capital. … Unfortunately, we had to disappoint over 100 start-ups in Canada that wanted to raise capital from their supporters in Ontario." – FrontFundr, Ontario Exempt Market Dealer

"It's extremely complex and it can be very discouraging for a lot of small entrepreneurs. There are numerous examples where in Ontario we [are] really pushing talent away or setting them up for failure because of the red tape, and the burden is huge. It is hard [enough] to start a business. You know the wages are very expensive, the rents... The regulation and the burden [is] just the complete killer." – Anonymous NCFA member

"As a small firm, we have very tight budgets. Our compliance team has asked that we dig up very detailed and 'historic' information on emails, social media ads, and related campaigns. We had to devote 2 full time individuals over several months. Check-ins and site visits to confirm the material presented in the compliance report and to assist registrants in fulfilling their obligations would be far more productive. The former (exhaustive reviews) take an incredible amount of resources for both regulator and registrant and are not cost-effective." – Anonymous NCFA member

Without a streamlined, flexible, nimble, and principles-based regulatory system – one that allows new rules to be formulated, while expelling old, outdated rules – Ontario's regulatory climate will continue to stifle innovation and drive business costs up and productivity down. Ontario's economy, businesses and consumers at all levels suffer, however, small businesses, innovators and entrepreneurs are the hardest hit.

"Ontario's crowdfunding requirements have choked off access to capital for SME's across a multitude of sectors – they have also shut out retail investor opportunities. Our members are completely stifled by OSC requirements and this is contributing significantly to Ontario's weak economic performance. "- Anonymous NCFA member

On behalf of the burden reduction committee at NCFA, we look forward to contributing ongoing input into Ontario's burden reduction initiatives. Please contact us at any time to discuss further.

Sincerely,

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1. About the NCFA

The NCFA is a national non-profit organization engaged with both social and investment crowdfunding and fintech stakeholders across the country. Headquartered in Ontario, the NFCA provides education, research, leadership, support and networking opportunities to over 2,000 members and works closely with industry, government, academia, and community and eco-system partners and affiliates, to create a strong and vibrant crowdfunding industry in Canada. The NCFA supports 'innovation finance' and aims to make the financial ecosystem more accessible and inclusive and to enhance the use of technology for smarter, faster and better decisions and services. The Association plans to expand globally to help Canadian fintech companies export overseas and bring new investment to Ontario.

2. Overview: Crowdfunding and Fintech are Being Held Back in Canada

Canada's crowdfunding and fintech "ecosystem" should be competitive, be in line with global trends, and enable early stage entrepreneurs to access smaller amounts of capital (i.e. < $5 million) at a reasonable cost. Unfortunately, it is not and does not. There is a 'funding gap' as smaller companies find it very challenging to raise debt or equity financing in Canada.

There is a 'valley of death' for start-ups at around the $250,000 level. Venture capital funding has increased, but VC dollars are mostly going to expanding firms. Angels are a lot less active than in the U.S. and their investment amounts are lower. Banks generally steer clear of start-ups. This means fewer innovative start-ups, fewer opportunities for investors, lower economic growth and productivity and fewer jobs.

"Regulation may be the largest constraint to FinTech development in Canada, as we have not set out many of the same principles as in the U.S. and U.K." [1]

The National Crowdfunding & Fintech Association of Canada (NCFA) has conducted numerous stakeholder consultations which overwhelmingly tell us that regulatory requirements are overly prescriptive, complex and burdensome – which raise the costs of doing business for start-ups. Entrepreneurs are reluctant to start up in Canada due to high costs (relative to a small financing), along with concerns about ongoing regulatory burdens such as overreaching and complex reporting requirements and compliance reviews. It should go without saying that unnecessary costs will either inhibit capital raising, and innovation generally, or be passed on to the consumer, or both.

Investors – which are potential sources of capital – are inhibited by restrictions like caps on investment. This causes many talented entrepreneurs and investors to move to overseas jurisdictions that better understand (and support) innovation and the economic potential of start-ups and SMEs.

If the NCFA recommendations that follow were to be implemented, the experience of other jurisdictions makes clear that more capital would be raised, especially for under-serviced sectors (e.g. women and minority groups, including First Nations, and rural communities). More jobs would be created. Investors would have increased confidence and more freedom to invest as they choose – any increase in investor downside risks are anticipated to be low.

> *"I'm really interested in the £10m/$15m companies that dominate the landscape. We just don't look at those role models. In terms of domestic employment of Fortune 500 companies, it's something like 7-8% of the American working population - they're not who employs us." Tom Peters* [2]

[1] An Overview of FinTech in Canada. Global Risk Institute. March 2018: https://globalriskinstitute.org/publications/an-overview-of-fintech-in-canada/.

[2] https://www.managementtoday.co.uk/tom-peters-speaking-tips-power-lunch/leadership-lessons/article/1427643.

A. Ontario

While the Offering Memorandum (OM) Exemption has gained some traction in Ontario, it is primarily aimed at companies wishing to raise more than $250,000 (due to the high costs of preparing the necessary legal and financial documentation, which remains the same regardless if raising $50,000 or $500,000). Thus, most early stage companies seeking to raise smaller amounts of capital cannot realistically use the OM Exemption.

Nor can they use the Integrated Crowdfunding Exemption (MI 45-108).

> *"It's extremely complex and it can be very discouraging for a lot of small entrepreneurs. And we've seen a lot of companies either never really took off or they took off and they just failed. And there are numerous examples where in Ontario we were really pushing talent away or we are setting them up for failure because of the red tape and the burden is huge. It is hard [enough] as it is to start a business. You know the wages are very expensive, the rents very expensive in Toronto... The regulation and the burden [is] just the complete killer." (Unattributed quotations in this submission, as here, are from an NCFA member.)*

> *"Canadian companies raising capital through investment crowdfunding are forced to jump through the hoops of different (often conflicting) provincial regulations. In Ontario, our most populous province, the situation is particularly bad: the province has no viable crowdfunding rule that actually works. The Crowdfunding Exemption introduced by the [OSC] in January 2016 turned out to be much too onerous for young companies… That means Ontarians are locked out of equity crowdfunding and Canadian companies are restricted from accessing capital.*

> *"FrontFundr, operating as a registered Exempt Market Dealer in eight provinces and* [is a leading] *online private capital markets platform, is democratizing investing in start-ups and growth companies… Unfortunately, we had to disappoint over 100 start-ups in Canada that wanted to raise capital from their supporters in Ontario."* [3]

The exemptions are also inadequate for most marketplace lending platforms – another alternative to conventional sources of financing. For example, they do not allow the multi-party participation of public, private and government blended funding models which have developed in the U.K. and elsewhere, or membership marketplace lending models. (For more information on lending platforms, see Appendix 5: P2P Lending.)

B. British Columbia

B.C. and some other jurisdictions have less burdensome crowdfunding requirements[4] that allow small firms to raise up to $250,000 per offering (twice a year), with participation from other provinces. While still not ideal, these less burdensome exemptions have proven to be much more effective than MI 45-108 in Ontario.[5]

For background on exemptions in Canada see – https://www.bcsc.bc.ca/Securities_Law/Policies/PolicyBCN/PDF/BCN_2018-01__February_14__2018/. (This BCSC Notice expresses well many of the points we raise in this submission.)

[3] "Open Open Letter to Securities Regulators: You Are One Call Away From Changing The Future of Canadian Business", Peter-Paul Van Hoeken, Founder & CEO, FrontFundr, Toronto, 4 Feb 2019.
[4] ie, the 'Start-up Crowdfunding Registration and Prospectus Exemptions – https://www.bcsc.bc.ca/45-535_[BCI]_09212017/.
[5] See – https://www.bcsc.bc.ca/For_Companies/Private_Placements/Crowdfunding/.

C. Canada's Uncompetitive Position

Canada has fallen behind international comparators such as the U.K. and the U.S. Crowdfunding platforms now represent the largest investments at the seed stage in the U.K. – U.K. crowdfunding platforms were involved in 24% of all equity deals in 2017, but had a larger share of seed stage deals, with 30% of seed stage deals in 2017.[6]

To see the advantages of a uniform, cross-border, and flexible crowdfunding regime, one need look no further than Regulation D in the US. The following are quotes from the recent Crowdfunding Capital Advisers Report.[7]

> *"2018 saw triple digit growth in unique offerings, proceeds and investors. More importantly, start-ups are successfully using Regulation Crowdfunding to raise meaningful capital in a relatively short period of time and at costs that are less than a typical Regulation D offering."*
>
> *"Unlike venture capital, where less than 6.5 percent of start-ups successfully raise funds, the success rate in Regulation Crowdfunding hovers around an impressive 60 percent. A key data point for industry followers is that the average raise ($270,996) helps start-ups hurdle the "valley of death" they often face after expending their internal or personal capital."*
>
> *"Regulation Crowdfunding is proving to be a jobs engine (creating on average 2.9 jobs per issuer), economic generator (pumping over $289 million of revenues into local economies)… There is still a lot of room for growth with Regulation Crowdfunding offerings as they equate to only 1.2 percent of all Regulation D offerings and only 4 percent of all capital raised under Reg D."*
>
> *"The fact that the velocity of capital into funded offerings continues to be steady without signs of abnormal activity or irrational investor behaviour is a healthy indicator. Meanwhile, the rapid increase in the number of offerings and investors proves there is continued appetite for Regulation Crowdfunding from both issuers seeking capital as well as investors looking to diversify. This is true across the [US]."*
>
> *"Regulation Crowdfunding is also proving efficient. If we compare the average days to close (113) in 2018 and average raise ($250,635) of a successful Regulation Crowdfunding campaign to a traditional Regulation D offering, Regulation Crowdfunding most likely represents the most efficient, cost effective way to raise capital for start-ups and SMEs."*

The type of (published) data collection and analysis provided by the above report is rare in Canada, which is another serious impediment to decision making in this area. NCFA must rely largely on anecdotal evidence from its members.

[6] https://www.british-business-bank.co.uk/wp-content/uploads/2018/07/Equity-Tracker-Report-2018.pdf.
[7] https://venturebeat.com/2019/01/30/regulation-crowdfunding-performed-solidly-in-2018-heres-the-data/.

D. Canada's Competition Bureau

As the Competition Bureau has pointed out[8], a more flexible approach to regulation and better government support would provide significant economic benefits by freeing entrepreneurship. It would also help to keep our entrepreneurs in Canada (along with the related jobs), boost GDP (especially by improving productivity), and encourage the commercialization of new products and services generally.

It is well-documented that overly complex, prescriptive regulation is a much higher burden for smaller firms and so is inherently anti-competitive.

For a disappointing progress report on the Buereau's recommendations of Dec 2017, see: http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/04392.html.

[8] Dec 2017 – http://www.competitionbureau.gc.ca/eic/site/cbbc.nsf/eng/04322.html.

3. Considerations for a Less Burdensome Regulatory Approach

A. Ontario's Regulatory Approach

At the heart of regulatory burden in Ontario is an 'old school' approach to regulation. With the best will in the world, regulatory staff cannot regulate efficiently and effectively (and certainly not quickly) unless they adopt a more flexible, risk based, and outcomes-focused approach that is based on hard data and transparent analysis. Such a change would require strong direction from political leaders, senior management and the regulator, and industry leaders.

Meanwhile regulatory staff must resist the urge to constrain the market where no market problem has been identified or the cost of a regulatory solution exceeds the benefits (if a problem warranting a regulatory solution has been identified). A "gap" does not necessarily require to be filled (or to be filled by the regulator).

B. Cost-benefit Analysis

The NCFA encourages all regulators not only to adopt a more risk-based approach, but also to improve the measurement of the costs of a proposed regulatory solution against its benefits. Detailed or prescriptive controls should only be imposed when clearly justified. (See Appendices 2 and 3: 'Prohibitions on Advertising and Solicitation' and 'Frequency of Reporting Requirements' for a high-level analysis of two requirements where we conclude that the costs far outweigh any benefits.)

And stakeholders have a right to know how the regulator decides whether a regulatory solution is needed and justified to mitigate perceived problems or harm. Without clarity on the data and analysis, effective consultation is impossible. (See Appendix 4: Regulatory approach.)

C. Onus of Proof

Related to this is the very difficult position in which stakeholders are placed when they are asked for views on whether a regulatory burden should be removed. First, this puts the onus of proof on stakeholders, when it is the regulator that should demonstrate that the regulatory requirements are and continue to be justified.

Second, the OSC rarely releases its analysis (and related data) to support its views, unlike, for example, the Canadian Office of the Superintendent of Financial Institution or the UK Financial Conduct Authority (FCA). Stakeholder are left to fill in the blanks, while usually being in no position to collect the data and do the formal analysis themselves.

4. Regulatory and Administrative Burden in Ontario: Operational problems, Harmonization, and Unjustified Requirements

A. OSC Questions[9]

1. Are there operational or procedural changes that would make market participants' day-to-day interaction with the OSC easier or less costly?

Yes.

(a) All stakeholders respect OSC staff, but interaction can be hard because the underlying culture at the OSC is risk averse, and primarily focused on finding problems rather than solutions.

Example: The processes for authorisation and compliance reviews are both painful experiences for most start-ups. OSC staff tend to spend too much time on perceived concerns that are simply not important in the general scheme of things or reflect a lack of understanding of the business.

We recognize that start-ups must spend some time educating staff about the business, but suggest that separate and specialized teams at the OSC should be created to handle authorisations and compliance reviews for digital/online businesses.

(b) More specifically (from our members):

Overly granular reviews

> *"Registered portals undergo a rigorous process to gain registration, after which they should be given the benefit of the doubt on their activities, assuming no significant complaints by investor and issuer clients. There is the perception in the industry that registrants are easy targets for overly granular reviews by regulators, while some unregistered entities may continue to operate below standard until the damage they inflict becomes a headline, which feeds the public's imagination of major failures within the industry. The OSC should focus on important risks to its objectives, rather than on potential processing faults, and be a leader to ensure the integrity of our markets rather than a meter maid."*

Exhaustive reviews unrelated to risks

> *"After registration, a portal should submit their annual compliance reports not only to their board (as required by 31-103) but also to the regulators through NRD; after which they should not expect regular reviews which invariably require months of engagement to unearth administrative deficiencies which seem to us less about protecting the capital markets and more about demonstrating regulatory activity for its own sake. Check-ins and site visits to confirm the material presented in the compliance report and to assist registrants in fulfilling their obligations would be far more productive. The former (exhaustive reviews) take an incredible amount of resources for both regulator and registrant and are not cost-effective."*

[9] While we don't discuss the regulation of crypto-assets (or ICOs) in this submission directly, we draw attention to a recent paper: "The compliance trilemma: challenges for ICOs", iComply Investor Services, Mitacs Canada, & the University of British Columbia, Nov 2018.

Vague or unjustified requests for information

Regulatory staff often ask for what appears to be 'nice to have' information under the guise of a broader policy.[10] This adds to costs (and concern about ongoing regulatory costs after a portal is registered). This also raises moral hazard issues (and costs) for the regulator.

Client information gathering

> *"During the course of compliance reviews, we have been asked to provide where our clients have been sourced from and when. The reality of the online world is that such information flows through to us via various channels. We have ads on Google, LinkedIn, and other social media channels. Anyone can join our mailing lists.*
>
> *"Similarly, as a technology and digital company, we are in the business of marketing our product not only via You Tube videos but also through online webinars. We cannot track the accreditation status of investors that log in to view webinars. Much as we would like to gather such information, investors often find such questions / inquiries (before they even know of us or our product) to be offensive.*
>
> *"This is the business we are in. As a small firm we have very tight budgets. Our compliance team has asked that we dig up very detailed and 'historic' information on emails, social media ads, and other related campaigns. We have had to devote 2 full time individuals over several months to work on such requests.*
>
> *"In addition, policing the actions of issuers working outside the platform during an offering is difficult. Regulators should recognize this difficulty during a compliance review.*
>
> *"Since sourcing information appears not to add any meaningful value to the compliance review process, we ask for such information requests to be rescinded."*

Emails access and portal log in access

> *"Regulatory staff ask for the names of individuals who have access to company email accounts (info, marketing, research, contacts, etc) and for portal users and their levels of authorization. While it is right that we maintain that information in-house, we do not see why it should be provided to the regulator as a matter of course. It increases the privacy risk and of course is one more compliance burden."*

Consolidating oversight/fees

> *"Our firm pays over $25,000 in fees annually through NRD alone, not including costs associated with OBSI, Fintrac etc… and we only have four registered individuals - two of whom are dealing representatives. Consolidating oversight overall and lessening fees would be very welcome."*

[10] E.g. Books and Records of NI31-103 Registration Requirements, Exemptions and Ongoing Registrant Obligations.

2. Are there ways in which we can provide greater certainty regarding regulatory requirements or outcomes to market participants?

Yes. The Association recommends:

- Clear, complete, and transparent analysis published by the OSC for comments before final decisions which sets out how the proposed requirements should achieve the regulatory objectives or purposes and why the OSC thinks that the costs will not exceed the benefits;
- Harmonisation of requirements and supervisory approach across Canada;
- Giving one regulator lead responsibility for authorisation and ongoing supervision and enforcement in Canada;
- Much more (and faster) feedback and data on progress (or not) via more mechanisms e.g. roundtables, newsletters, webcast knowledge hours, etc;
- Real collaboration with the private sector on training, industry education, investor education, data collection and analysis;
- Much quicker reporting on the aggregated results of compliance reviews;
- Much quicker feedback to applicants for authorisation.

More guidance

> *"A regulator makes rules yet will often not provide interpretation of or guidance on the rules. This poses a problem for smaller market participants. Legal opinions are expensive and may be contested at some point by a regulator. For those rules that require interpretation (e.g. adequate systems and controls), market participants need more help to comply in a way that is cost-effective for their business. Part of protecting capital markets is ensuring that its participants have a viable playing field upon which to succeed."*

More certainty or visibility to allow for business planning

> *"The difficulty in being a small business in a highly regulated industry is that it is difficult to forecast revenues and make operational decisions on hiring, investing, engaging third party suppliers etc. when we have no visibility into when we will be able to engage in certain activities. That is, applications and procedures with the OSC are a black box with no ability to discern when decisions will be made, what further information will be requested, what other gating requirements will be imposed, etc. There should be better defined procedures for engaging with the OSC that set out target time frames for responses, define what the steps will be to secure a successful outcome, and ensure that OSC staff are working towards those deadlines and targets. At the very least, the OSC has the data that can be used to provide some estimates of how long certain applications or procedures will take."*

3. Are there forms and filings that issuers, registrants or other market participants are required to submit that should be streamlined or required less frequently?

Yes – see below under question 6.

In addition:

> *"The annual compliance report mentioned in 1(b) above could include a standard form for all jurisdictions providing detail on a registrant's business as under the 'participation' fee process. Standardizing this would limit a registrant's largely wasted efforts to address each regulator individually."*

Avoid Duplicate Data Collection

> *"To make the capital markets more efficient, it would be worthwhile to centralize certain information to avoid duplication. For example, a single PIF or similar database can be used for regulated individuals that can be updated once and used across different roles with different organizations who are regulated by different regulators. It should also be easier to update Outside Business Activities (OBAs) into one central database that can be accessed by all the regulators. OBAs should be able to be updated by individuals directly through a web portal that is easily accessible.*
>
> *"Also, there should be some centralized database of accredited investors or some other way to allow market participants to rely on other regulated participants to verify accredited status so that investors don't need to go through the exact same process multiple times to make investments with different registered dealers."*

4. Are there particular filings with the OSC that are unnecessary or unduly burdensome?

Yes – see below under question 6.

In addition:
As per #3.

Trade record confirmation sheet

> *"The requirement that account statements be physically delivered is outdated. Online notification is adequate to alert clients to trades and account statements."*

Secondary trading

Companies are staying private longer (the median time to Initial Public Offering (IPO) in the late 90s in the U.S. was ~3.0 years, compared to ~7.5+ years today). All this makes a robust secondary market for private assets even more important.

> *"Holders of private securities purchased through an Exempt Market Dealer should be able to sell the securities, in limited circumstances, to individuals or entities qualified through the EMD which originated the sale, outside of the scope of an offering but within the applicable exemption. The system for public offerings (e.g., IPO, Reverse Take-Over) has created a situation where issuances of questionable value might be placed within a public market without proper seasoning and testing. There is an opportunity for existing online EMDs to provide this framework and provide regulators with the confidence of an historic relationship with an issuer which can be assessed and measured."*

5. Is there information that the OSC provides to market participants that could be provided more efficiently?

> *"The OSC has a good outreach program but we suggest a 'relationship manager' for those registrants that are not directly under the OSC's supervision as a 'principal' regulator. Market participants perceive the OSC's relationship with them as adversarial. A more personal relationship between the CCO of a registered firm and a dedicated OSC rep would help the firm to meet its requirements, build greater understanding of the firm's business at the regulator and build goodwill within the industry overall."*

Provision of funding for crowdfunding education and data collection

Education is at the core of a successful implementation of a vibrant crowdfunding sector. A greater effort by all stakeholders, including the private sector and government, could provide both better education and data collection.

In both the U.S. and the U.K., regulators and government agencies work together with the private sector to actively educate and promote alternative capital.

6. Are there requirements under OSC rules that are inconsistent with the rules of other jurisdictions and that could be harmonized?

Yes.

There are currently three basic versions of crowdfunding specific exemptions in Canada that form a patchwork that varies with respect to offering documentation, ongoing disclosure requirements, capital raising and investor limits or caps, and advertising. These differences make it more costly for early stage companies, most of which want to raise funds and do business in more than one jurisdiction.

Some of the differences among the regulatory exemptions are outlined in Appendix 1. While the table is now dated, it illustrates how complex and varied the requirements are, causing confusion and frustration for all market participants. Appendix 1 shows that differences exist even among jurisdictions participating in the same instrument.

The differences among or within the exemptions seem to us not cost-effective for the risks they are presumably intended to mitigate. These also impose high demands on start-ups. On costs, the NCFA estimates (based on anecdotal evidence from its members) that a lack of harmonisation and the resulting complexity adds $5,000 - $20,000 in legal fees alone per deal.

The differences are exacerbated by the differences in supervisory approaches among the regulators (e.g. procedures, specific concerns, compliance requests).

> *"[It's] like you are trying to operate in 12-15 different jurisdictions globally within the same country. So that is extremely painful for entrepreneurs."*

> *"[We] don't understand why Canada is doing this to itself. Start-ups and growth companies are the biggest driver for economic growth and jobs...".*

7. Are there specific requirements that no longer serve a valid purpose?

Yes. We set out requirements below that in our view were not justified when they were first imposed.

45-108

There can be no doubt that MI 45-108 has been a failure and a waste of time and money for so many early stage companies who have reviewed it, only to reject it. Even if there were to be no other changes, Ontario would be much better off if the OSC were to replace it with the BC crowdfunding exemptions.

Examples:

Accreditation verification

> *"We agree that a portal should be required to take reasonable steps to authenticate the accreditation status of an investor.*
>
> *"However, for our business to gain any meaningful traction, we must make the investor on-boarding process smooth. When an investor comes to our portal for the first time they are not interested in providing detailed personal information. They want to see our marketplace, get a basic understanding of the kinds of deals, and then they may decide to proceed.*
>
> *"But the regulator requires that we not let an investor be on-boarded and then proceed to the deals page until we have done the detailed KYC, accreditation verification, and suitability assessment. In a way, the regulator has prevented any potential investor loss by forcing us to operate in this manner. If no investor gets on-boarded, there is no investment and investor loss has been prevented!*
>
> *"We strongly support investor self-accreditation, at which point the investor should be able to proceed to the deal page. We provide clear definitions for accreditation [on our website]. Investors understand the definitions. There is no ambiguity. [And an] investor cannot invest at this stage.*
>
> *"If a prospective investor then wants to proceed, they will then have to submit full accreditation and KYC information.*
>
> *"However, we are then required to collect too much information. The 'burden' on an online portal to do further testing, e.g. to collect NOAs, T4's, etc. becomes 'policing' and is often thought to be offensive by the investor and is a turn off. In an online world, people do not feel comfortable sharing too much of their personal information. Such 'policing' beyond the investor's confirmation of their income/net worth and certain other essential information to support of their accreditation status is not justified in risk terms and slows us down significantly."*

Suitability testing

> *"We fully understand and appreciate that one of the key pillars of selling an investment [through a portal] is to ensure that a particular investment fits well with the overall risk-return profile of the investor. Our portal is actually in total sync with this goal. We provide lots of educational blogs and information. We ask questions that an investor needs to answer before they are able to proceed further. The questions are fairly detailed e.g., we ask about other holdings, diversification of assets, risk tolerance, liquidity concerns and more. If the answers do not fit well with the nature of the product, then the investor is declined, or*

their investment amount may be reduced.

"In other words, we comply. But the requirements are excessive. We think the regulator's testing requirements are those of a nanny-state. An investor – if educated and pointed in the right direction by our online questionnaire – is fully capable of doing their own suitability assessment.

"The suitability burden (ironically) has forced us to hire more dealing reps and so the costs go up and the process becomes traditional EMD. These unnecessary costs are passed on to the investor.

"We ask the regulator to work with us to better understand our business constraints around this particular point. If the inputs allow for outputs which comply with desired outcomes (e.g., suitable), then the regulator should be flexible on the approach individual businesses decide to take to get there."

"The use of technology to determine e.g., suitability is inevitable. The rules should allow for more principles-based oversight which still ensures the collection of material information (or its availability) without compromising client privacy. We need reasonable parameters, which allow for thoroughness without compromising user experience."

2017 Submission

The following table sets out burdens that we discussed with the OSC in 2017. For more detail see Appendix 6.

Description	Benefit / Impact
Harmonize MI 45-108 and Offering Memorandum requirements	Reduce regulatory burden for all stakeholders
Allow advertising and general solicitation (prohibited under 45-108, rule 11)	Increase investor participation -- more liquidity and more investors
Increase threshold for required review and audited financial statements	Increase investor participation -- attract more companies, reduce undue burden
Reduce frequency of exempt distribution reports	Reduce burden (especially for small EMDs/ funding portals)
Allow accredited investors to fully participate (without caps)	Increase investor participation to reach funding targets, assist scale-up
Increase $1.5M issuer caps to $5M or more	Increase investor participation, assist scale-up
Increase retail investor cap per deal from $2.5k to $10k	Increase investor participation -- suitable for more economic sectors
Increase retail investor cap per year to >$10k	More liquidity, more investors

8. Should the OSC try harder to promote the use of plain language in regulatory disclosure?

Absolutely. We support plain language requirements that are enforced, as in the U.K.[11] Plain language also helps start-up entrepreneurs. For example, we like the BCSC's crowdfunding webpage. [12]

5. Conclusion

Crowdfunding drives innovation, economic growth, and jobs and enables more productive investment in venture markets. It also strengthens the early stage capital market. Canada is clearly under-performing in this sector, but global trends present a market opportunity which Canada must grasp soon.

As the recent CB Insights Report tells us:

> *"**Early-stage** deals [for fintech], as a percentage, fell to a 5-year low as investors concentrated bets in perceived winners: Global seed and Series A fintech deals grew 5% on an annual basis in 2018, but fell as a percentage of total deals to 57%. U.S. early-stage deals were flat YOY as investors concentrated their bets in established fintech unicorns."*

Ontario would especially benefit from encouraging smaller start-ups at this time.

> *"Asia made a run at the U.S. as the top market for fintech with a surge in early-stage and mega-round investments: Asia saw the biggest boost in deals, growing 38% YOY and a record level of funding raising $22.65B across 516 deals. Political and trade war tensions may have caused some of the pull back in H2'18, but 2019 could see Asia overtake the U.S."*

The clock is ticking. North America may no longer be powering fintech growth. A window of opportunity may be closing.

Nevertheless "2018 was a stellar year for fintech with over 1,700 deals worth nearly $40B globally".

- Fintech is growing with deals outside of core markets (US, UK, and China) accounting for 39% of deals.
- The U.S. remained the top market for deals with 659 investments worth $11.89B funding, both a new annual high.
- There are now 39 VC-backed fintech unicorns worth a combined $147.37B.

"Findings from 2018 suggest that fintech will continue its upward tear. With more areas ripe for fintech disruption, more technologies emerging, and more fintech deal hubs materializing across the world, 2019 could be an exciting year." https://www.cbinsights.com/research/report/fintech-trends-2019/

[11] See – https://www.theglobeandmail.com/investing/personal-finance/article-why-its-not-your-fault-its-so-hard-to-understand-investing/.
[12] https://www.bcsc.bc.ca/For_Companies/Private_Placements/Crowdfunding/.

Make no mistake, Canadian start-ups and Canadian talent are being actively solicited by countries like the U.K. to help build value in their ecosystems. This is not the time for Ontario to hold back.

Sincerely,

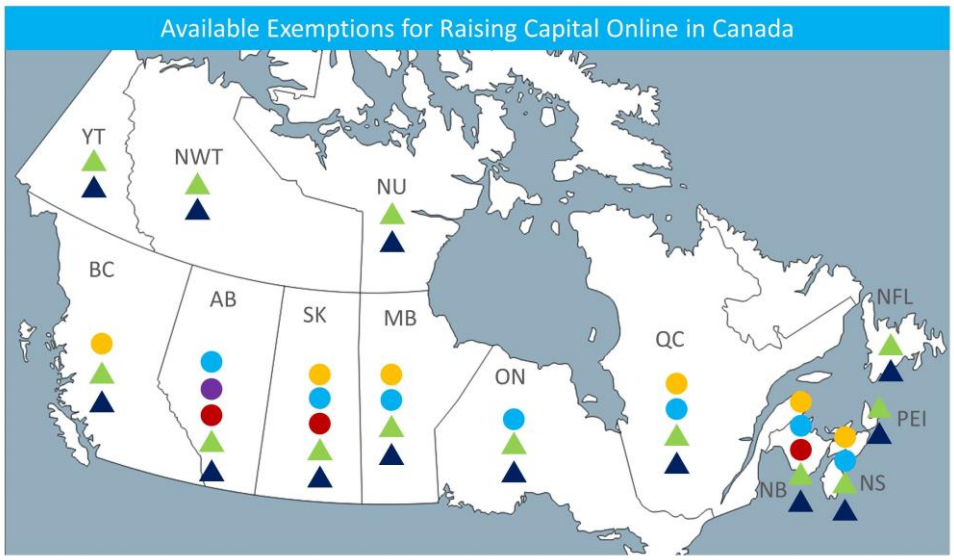
Craig Asano
CEO & Founder NCFA

Copied to: Premier, the Honourable Doug Ford
Minister of Economic Development, Job Creation and Trade
Minister of Finance
Cabinet Office

Appendices

Appendix 1: Comparison of complex crowdfunding requirements in Canada

(as of Feb 2016 - *for illustrative purposes only*)



Securities Exemption	Retail	Accredited	Max Raise
The Startup Crowdfunding Exemption [i]	✓	✓	$500K/year
Integrated Crowdfunding Exemption [ii]	✓	✓	$1.5M/year
Startup Business Exemption [iii]	✓	✓	$1.0M/lifetime
Offering Memorandum Light Exemption [iv]	✓	✓	$500K/lifetime
Offering Memorandum Exemption [v]	✓	✓	Unlimited
Accredited Investor Exemption [vi]		✓	Unlimited

EQUITY CROWDFUNDING IN CANADA TODAY (February 2016)						
	Available Now					Pending
Securities Exemption Relied On	Accredited Investor Exemption[1]	Offering Memorandum Exemption[2]	Offering Memorandum Light Exemption[3]	Start-Up Crowdfunding Exemption[4]	Integrated Crowdfunding Exemption[5]	AB/NU Start-Up Business Exemption[6]
Jurisdictions	BC, AB, SK, MB, ON, QU, NB, NS, NFL, PEI, NU, YK, NWT	BC, AB, SK, MB, ON, QU, NB, NS, NFL, PEI, NU, YK, NWT	AB, SK	BC, SK, MB, QU, NB, NS	MB, ON, QU, NB, NS Pending: SK	AB, NU
Offering Limit	Unlimited.	Unlimited.	$500,000 cap every 12-month period.	$250,000 cap per offering $500,000 aggregate cap every 12-month period. Limit of two offer-	$1,500,000 cap every 12-month period.	$1,000,000 lifetime cap.

				ings using exemption per 12 month period		
Type of Securities	All.	All but securitized products and in AB, SK, ON, QU, NB and NS[8] specified derivatives and structured finance products.	All but derivative type securities.	All but derivative type securities.	All but derivative type securities.	All but derivative type securities.
Issuer Restrictions	None. Available to reporting and non-reporting issuers involved in all business sectors.	Available to reporting and non-reporting issuers involved in all business sectors, except not available to investment funds in AB, NS, SK, NB, ON and QU[8], unless if offering is in AB, NS, SK issuer is a non-redeemable investment fund or mutual fund that is a reporting issuer.	Not available if a reporting issuer, investment fund, mortgage investment entity or an issuer engaged in the real estate business.	Not available if a reporting issuer or investment fund. Head office must be resident in a participating jurisdictions.	Available to reporting and non-reporting issuers involved in all business sectors except investment funds. Must be incorporated or organized under the laws of a jurisdiction in Canada and have head office in Canada.	Not available if a reporting issuer or investment fund. Head office must be resident in a AB or NU or in participating jurisdiction of the Start-up Crowdfunding Exemption.
Investor Restrictions	Must be an accredited investor based on annual income ($200,000 individually or $300,000 with spouse) or net financial assets ($1 million excluding home) or net assets ($5 million). No limits on investment amount.	If investing $10,000 or more and from MB, PEI, NU, YK or NWT, must be an eligible investor based on annual income ($75,000 individually or $125,000 with spouse) or net assets ($400,000), or a close friend, family or business associate, or accredited investor, or have obtained the advice from an eligible adviser on suitability. Eligible investors resident in AB, NB, NS, ON, QU and SK[8] have a 12 month investment cap of $30,000 unless investor receives suitability advice from regis-	12 month investment cap of $2,000 in all securities of issuer group. No 12 month investment cap for all distributions under exemptions.	Must be resident in one of the participating jurisdictions and over the age of 18. 12-month investment cap of $1,500 per distribution by an investor.	Must be resident in one of the participating jurisdictions. 12-month investment cap of $2,500 per distribution and $10,000 for all distributions under exemption, unless an accredited investor who is not a permitted client, than $25,000 per distribution and $50,000 for all distributions under exemption, issuers. No cap for permitted clients.	Must be resident in AB or NU or in participating jurisdiction of the Start-up Crowdfunding Exemption. 12-month investment cap of $1,500 per investment or $3,000 per issuer group unless investor receives suitability advice from registered dealer than cap of $5,000 per investment or $10,000 per issuer group.

		tered dealer than cap of $100,000 for all distributions under exemption in 12 month period.				
Financial Statements	Optional.	IFRS audited.	PE-GAAP unaudited.	Optional. If included may be audited or unaudited and use either IFRS or PE-GAAP.	IFRS audited if amount raised under all prospectus exemptions $750,000 or more or issuer is a reporting issuer. Unaudited IFRS financial statements with review report if non-reporting issuer and amount raised under all prospectus exemptions is more than $250,000 and less than $750,000.Unaudited financial statements if a non-reporting issuer and amount raised from all prospectus exemptions is under $250,000.	Optional. If included may be audited or unaudited and use either IFRS or PE-GAAP.
Document Requirements	Subscription Agreement , Investor Questionnaire and Form45-106F9 Form for Individual Accredited Investor.	Offering memorandum in prescribed form (Form 45-106F2 for Non-Qualifying Issuers; or Form 45-106F3 for Qualifying Issuers); subscription agreement and Form 45-106F4 – Risk Acknowledgement.	Offering memorandum in prescribed form (Form 45-106F2 for Non-Qualifying Issuers; subscription agreement and Form 45-106F4 – Risk Acknowledgement.	Offering document prescribed form: Form 1 - Start-up Crowdfunding - Offering Document; subscription agreement and Form 2 Start-up Crowdfunding Risk Acknowledgement.	Offering document prescribed form: Form 45-108F1 Crowdfunding Offering Document; subscription agreement, Form 45-108F2 Risk Acknowledgement ; and Form 45-108F3 Confirmation of Investment Limits.	Offering document prescribed form: Form 1 - Start-up Crowdfunding - Offering Document; subscription agreement and Form 2 Start-up Crowdfunding Risk Acknowledgement..
Statutory or Contractual Right of Action	None.	Two-day right of withdrawal.[7] Statutory or contractual right of action for rescission or damages if misrepresentation in offering memorandum.	Two-day right of withdrawal. Statutory right of action against issuer if misrepresentation in offering document.	None. 48 hour right of withdrawal after subscription and after notification of a material amendment to the offering.	None. 48 hour right of withdrawal after subscription and after notification of a material amendment to the offering. Contractual right of action against reporting issuer if misrepresentation in offering docu-	Two-day right of withdrawal. Statutory right of action against issuer if misrepresentation in offering document. 48 hour right of withdrawal after subscription and after notification of a material amendment to the offering.

					ment. Statutory right of action against private issuer if misrepresentation in offering document.	
Post Offering Requirements	File Form 45-106F1 (Form 45-106F6 in BC) within 10 days of closing offering. No annual report or other continuous disclosure requirements because of offering.	File Form 45-106F1 (Form 45-106F6 in BC) and offering memorandum within 10 days of closing offering. If a mining company must also file a Form 43-101 Technical Report. If an oil and gas company must also file a Form 51-101F1 or Form 51-101F2 statement or report. If offering made in AB, SK, ON, QU, NB, or NS[8] subject to continuous disclosure requirements: (1) annual audited financial statements within 120 days from fiscal year end; (2) annual disclosure of use of proceeds; (3) material change like reports in NB, NS and ON; and (4) deemed to be a market participant in ON and NB subject to record-keeping requirements and compliance review.	File Form 45-106F1 and offering memorandum within 10 days of closing offering. If a mining company must also file a Form 43-101 Technical Report. If an oil and gas company must also file a Form 51-101F1 or Form 51-101F2 statement or report. No annual report or other continuous disclosure requirements as a result of offering. Not clear if on April 30, 2016, issuers will be subject to continuous disclosure requirements,	File Form 45-106F1 (Form 45-106F6 in BC) and offering document within 30 days of closing offering.	File Form 45-106F1 and offering document within 10 days of closing offering. Subject to continuous disclosure requirements: (1) annual financial statements within 120 days from fiscal year end review report or auditor's report if amount raised under exemption is $250,000 or more but less than $750,000 and audited report if amount raised is more than $750,000; (2) annual disclosure of use of proceeds; (3) material change like reports in NB, NS and ON; and (4) must maintain books and records available for inspection by investors and ON and NB regulators.	File Form 45-106F1 (Form 45-106F6 in BC) and offering document within 30 days of closing offering.
Portal Requirements	Direct sales by issuer on their website or offline, or portal operator needs to be registered as an exempt market dealer, investment dealer or a restricted market	Direct sales by issuer on their website or offline, or portal operator needs to be registered as an exempt market dealer, investment dealer or a restricted market dealer	Direct sales by issuer on their website or offline, or portal operator needs to be registered as an exempt market dealer, investment dealer or a restricted market dealer	Portal operator must provide 30 days advance notice of intent to act as a Start-up Crowdfunding portal. Cannot be related to an	Portal operator needs to be registered as an exempt market dealer, investment dealer or a restricted market dealer	Direct sales by issuer on their website or offline, or portal operator needs to be registered as an exempt market dealer, investment dealer or a restricted market dealer.

	dealer.			issuer of securities on portal. OR: Registered as an exempt market dealer, investment dealer or a restricted market dealer.[9]		
Advantages	(1) No limit to offering size; (2) Available across Canada; (3) No financial statement requirement; (4) No offering document obligation; (5) Available to all issuers; (6) No annual report or other continuous disclosure requirements as a result of offering; (7) All types of securities may be sold; and (8) No statutory or contractual right of action.	(1) No limit to offering size; (2) Available across Canada; (3) Available to all issuers but investment funds in certain jurisdictions; (4) No annual report or other continuous disclosure requirements because of offering in BC, MB, PEI, NFL, NU, YK and NWT ; and (5) All types of securities may be sold other than securitized products and in AB, SK, ON, QU, NB and NS[8] specified derivatives and structured finance products.	(1) Can sell to anyone resident in AB and SK; (2) Unaudited financial statement prepared using PE-GAAP allowed; and (3) No annual report or other continuous disclosure requirements as a result of offering.	(1) Can sell to anyone in participating jurisdictions; (2) Limited offering document obligation; (3) No financial statement requirement; (4) No annual report or other continuous disclosure requirements as a result of offering; and (5) No statutory or contractual right of action.	(1) Can sell to anyone in participating jurisdictions; (2) Limited offering document obligation; and (3) Unaudited financial statements allowed if non-reporting issuer and total amount raised under all prospectus exemptions to date less than $750,000 (audit review letter required if amount raised is more than $250,000).	(1) Can sell to anyone in participating jurisdictions; (2) Limited offering document obligation; (3) No financial statement requirement; and (4) No annual report or other continuous disclosure requirements as a result of offering.
Disadvantages	(1) Accredited investors only; and (2) Must confirm accredited investor status.	(1) Rule is complicated; (2) Requires IFRS audited financial statements; (3) Must provide detailed offering memorandum; (4) Not available to investment funds in AB, NS, SK, NB, ON and QU[8], unless if offering is in AB, NS, SK issuer is a non-redeemable investment fund or mutual fund that is a reporting issuer; (5) $10,000 investment	(1) Offering size limited to $500,000 every 12 month period; (2) Must provide detailed offering memorandum; (3) Only available in AB and SK; (4) Not available if a reporting issuer, investment fund, mortgage investment entity or an issuer engaged in real estate as a business; (5) No derivative type securities allowed; (6)	(1) Offering size limited to $250,000 per offering to a maximum of $500,000 in two offerings every 12 month period; (2) Only available to participating jurisdiction resident issuers and investors; (3) Not available if a reporting issuer or investment fund; (4) No derivative type securities allowed; and (5) Offering	(1) Offering size limited to maximum of $1,500,000 every 12 month period; (2) Only available to participating jurisdiction resident issuers and investors; (3) Not available if an investment fund; (4) No derivative type securities allowed; (5) Offering must be made through a funding portal; (6) 12-month investment cap of $2,500 per	(1) Offering lifetime limit of $1,000,000; (2) Only available to issuers and investors in AB, NU and in participating jurisdictions of the Start-up Crowdfunding Exemption; (3) Not available if a reporting issuer or investment fund; and (4) No derivative type securities allowed.

		limit per 12 month period by investors in MB, PEI, NU, YK or NWT unless accredited investors, friends, family or business associate, or receives suitability advice from eligibility advisor. $30,000investment limit per 12 month period by investors in AB, NB, NS, ON, QU or SK unless eligible investor obtains suitability advice than $100,000 cap for all investments under exemption in 12 month period; (6) Statutory or contractual right of action attached; (7) Continuous disclosure requirements including audited financial statements indefinitely if offering securities in AB, NB, NS, ON, QU or SK.	12 month investment cap of $2,000 in all securities of issuer group; and (7) Statutory or contractual right of action attached.	must be made through a funding portal.	distribution and $10,000 for all distributions under exemption, unless an accredited investor who is not a permitted client, than $25,000 per distribution and $50,000 for all distributions under exemption; and (7) Statutory right of action attached.	
Active Portal Examples	**Exempt Market Dealer**: FrontFundr (AB, BC, MB, SK, QU, MB, NS, NB); NexusCrowd (AB, BC, ON); Optimize Capital Markets (AB, BC, MB, QU) InvestX (AB, BC, ON, QU) **Restricted Market Dealer**: Social Venture Connexion/MaRs SVX (ON, QU)	**Exempt Market Dealer**: FrontFundr (AB, BC, MB, SK, QU, MB, NS, NB) **Exempt Market Dealers Through Registered 3rd Party**: SeedUps Canada (AB, BC, ON, QU via Waverley)	**Exempt Market Dealer**: FrontFundr (AB, BC, MB, SK, QU, MB, NS, NB) **Exempt Market Dealers Through Registered 3rd Party**: SeedUps Canada (AB, BC, ON, QU via Waverley)	**Exempt Market Dealer**: FrontFundr (BC, SK, QU, MB, NS, NB) **Start-up Crowdfunding Portals**: GoTroo (BC, QU, NS, NB); InvestLocal (BC); SmallStarter (BC, SK, MB, QU, NS, NB); StellaNova (QU, NS, NB); Vested (BC)	No Portals.	No Portals.

Appendix 2: Prohibitions on advertising and soliciting

The Integrated Crowdfunding Exemption MI 45-108 prohibits issuers from directly or indirectly advertising their crowdfunding offering, although an issuer may inform prospective "purchasers" that it intends to conduct an offering and may direct purchasers to the portal. Contrast this with the U.K. where the Financial Promotion Rules simply require issuers to consider the nature and risks of the investment and the information needs of the customers, then to ensure that investors have the information they need to make informed investment decisions and that all communications are fair, clear and not misleading.

The FCA considers that these high level requirements are appropriate and proportionate for this market. In the FCA's view, it is generally not appropriate to mandate specific disclosures since business models and risks vary considerably. The high level approach puts the onus on firms to provide appropriate, useful information and not to burden consumers with too much detail. [13]

Under Title II of the U.S. Jobs Act, a company may use "general solicitation" to market securities offerings if it follows the rules and guidelines of Rule 506 of Regulation D. Under this relatively new exemption, companies can use the internet or other media to advertise their offerings. This gives companies the chance to attract a large number of new investors in a short period of time, but limits the type of investor who can purchase the securities to "accredited" investors.

The Act defines an accredited investor as one who has a net worth of $1,000,000 (not including the principal residence), or who earned more than $200,000 a year for the three years before the securities purchase. Companies must take "reasonable steps" to verify that they are accredited. There is no cap on the number of investors or the amount of money that can be raised.

Title III of the Act allows securities offerings to non-accredited investors but capped at $1,000,000 raised in a 12-month period. There are some additional restrictions on portals, but a company is essentially free to advertise and solicit off portal about its business and prospects via social media, webinars, live events, etc. [Bend Law Group - http://www.bendlawoffice.com/2016/01/03/crowdfunding-and-the-important-distinctionsbetween-title-ii-and-title-iii-of-the-jobs-act/]

The prohibition on advertising and soliciting in Ontario appears to the NCFA to be another example of unjustified regulation. While consumer protection is a key objective, and high level requirements along the lines of those in the UK are appropriate, we are not aware of evidence of abuse or a degree of risk that would justify a complete prohibition, let alone a prohibition as costly to the market as this one.

13 https://www.fca.org.uk/publication/policy/ps14-04.pdf.

Appendix 3: Frequency of reporting requirements

In Ontario, entrepreneurs who are non-reporting issuers who have distributed securities under the crowdfunding exemption must deliver financial statements to the regulator within 120 days of their financial year end. This requirement is commonly imposed globally and is entirely appropriate.

However, in Ontario, the statements must be accompanied by: (i) a review report or auditor's report if the amount raised by the issuer under one or more prospectus exemptions from the date of the formation of the issuer until the end of its most recently completed financial year, is $250,000 or more but is less than $750,000, or (ii) an auditor's report if the amount raised by the issuer under one or more prospectus exemptions from the date of the formation of the issuer until the end of its most recently completed financial year, is $750,000 or more. (MI 45-108, s.16)

Contrast this with U.K. requirements where an audit is generally not required at all if a company is "small" and an audit is not otherwise required under companies legislation (i.e. at least two of the following must apply for at least two consecutive years: Turnover < £10.2 million; Balance sheet total (fixed assets plus current assets) <£5.1 million; Number of employees < 50).

While the U.K. audit threshold is probably the highest of comparable jurisdictions, Ontario's appears to be one of the lowest. The cost of an audit plus the company time associated with the process can be a very significant burden for small firms. In addition, for data reporting other than financial statements, other regulators (e.g., U.K. FCA) commonly require quarterly reporting. Data may be required in Ontario as frequently as every 10 days. These burdens are exacerbated by the fact that Ontario entrepreneurs must also comply with different (non-harmonized) reporting requirements in other Canadian jurisdictions.

In the absence of any explanation or analysis from the regulators, these requirements appear to the NCFA to be examples of unjustified regulatory burden. While consumer protection is a key objective here, and regular reporting is appropriate, it is accepted best practice for regulators that NO requirement is imposed unless it can be shown on good evidence that the requirement is the best alternative to achieve the regulatory objective or solve a market problem, and that the demonstrated benefit will exceed the costs. Compare this to the extensive cost/benefit analysis in the FCA's Consultation Paper 13/3. [14]

[14] "The FCA's regulatory approach to crowdfunding (and similar activities)" Oct 2013 - https://www.fca.org.uk/publication/consultation/cp13-13.pdf.

Appendix 4 - Regulatory approach

In a submission on regulatory burden, FAIR "cautioned against reducing regulatory burden in the absence of empirical support that it will be beneficial to the capital markets including investors, a key stakeholder in our capital markets".

While the NCFA is 100% behind the consumer protection objective, the NCFA strongly takes issue with this approach. The statement should be turned on its head (and the onus reversed) – i.e. No regulatory burden should be imposed unless a risk to regulatory objectives (e.g. consumer protection) has been identified by the regulator and the regulatory solution selected (if any) is the most cost-effective to mitigate the risk. (The regulator's analysis should also be fully transparent so stakeholders can comment effectively.)

Apart from the fact that FAIR's approach does not support the equally important objective of efficient and competitive markets, it makes any argument for reducing burdens much more difficult. How does the NCFA provide empirical support for a lower trigger for an audit, for example? How can it show that reducing this burden is "beneficial" for investors?

NCFA supports the approach of successful regulators such as the FCA – https://www.fca.org.uk/publication/consultation/cp13-13.pdf.

Speech (Getting regulation right) – https://www.fca.org.uk/news/speeches/getting-regulation-right.

FCA's regulatory principles – https://www.fca.org.uk/about/principles-good-regulation.

For ASIC (Australian regulator of equity crowdfunding) see - http://asic.gov.au/regulatory-resources/financial-services/crowd-sourced-funding/ and podcast – https://asic.podbean.com/e/episode-25-crowd-sourced-funding/.

Appendix 5: Peer-to-Peer lending in Canada

P2P lending, also known as marketplace lending, is the practice of lending money to individuals or businesses through online services that match lenders directly with borrowers. Since P2P lending companies operate entirely online, they can run with lower overhead and provide the service more cheaply than traditional financial institutions. As a result, lenders often earn higher returns compared to savings and investment products offered by banks, while borrowers can borrow money at lower interest rates, even after the P2P lending company has taken a fee for providing the match-making platform and evaluating the borrower's creditworthiness.

Since more companies have been seeking debt financing since the financial crisis, the P2P lending market is now about 10 times larger than the investment crowdfunding market in the U.K. and other developed markets. Unfortunately, in Canada exemptions such as the Integrated Crowdfunding Exemption and restricted dealer registration do not work for most marketplace lending platforms. For example, they do not allow the multi-party participation of public, private, and government blended funding models which have developed in the U.K. and elsewhere, or membership marketplace lending models. They also prevent financial institutions from operating a marketplace lending portal or from heavily participating in funding events. (A number of successful portals in other countries may raise 25% from the crowd and 75% from an institution.)

To provide another example, requiring marketplace lending portals to do a full suitability analysis of each lender/investor, especially when their loan/investment is capped at the low end (so that the downside risk is low), or when the investor is an institution, is not risked based. (So far as we are aware, only Canada imposes caps on P2P lending.) Due to the significant costs of tasks such as determining suitability, the requirements have kept the sector from making any headway in Canada.

Marketplace lending platforms are having a significant positive impact on SMEs in the U.K. as shown in the Cambridge University 2015 UK Alternative Finance Industry Report, and in the U.S. as illustrated by a report prepared by the Milken Institute Center for Financial Markets (which profiled 70 U.S. based online non-bank fintech businesses). Loan based crowdfunding generally presents somewhat different risks than investment based crowdfunding. The NCFA suggests that it should therefore be regulated somewhat differently, more in line with the U.K. [15]

Case Study: Funding Circle, a UK P2P Lending Platform

The Centre for Economics and Business Research assessed the impact of Funding Circle on the U.K. economy. They found that from 2010 to mid-2016, Funding Circle boosted the U.K. economy by £2.7 billion by: supporting the creation of over 40,000 new jobs; helping businesses in regions that have faced economic hardship (such as the North); helping small housebuilders to build more than 2,200 homes; and helping more than 15,000 SMEs to access finance. [16]

15 See – https://www.fca.org.uk/publication/thematicreviews/crowdfunding-review.pdf.

16 https://static.fundingcircle.com/files/uk/information-packs/small-business-big-impact-cebrreport-315de033.pdf.

Appendix 6: Specific recommendations for regulatory change

The changes that the NCFA proposes here would remove much of the undue burden for small companies and licensed portals, and encourage wider participation by all stakeholders. Some recommendations would simply bring Ontario into line with lighter regulatory regimes elsewhere.

The NCFA considers that its recommendations are positive or neutral for investor protection. Higher compliance costs when there is no net benefit to mitigate downside risk only serve to increase costs for consumers or to push businesses to other jurisdictions for cheaper capital.

See Appendix 5 for changes that would better enable and support marketplace (P2P) lenders.

1. Harmonize crowdfunding requirements

The Integrated Crowdfunding Exemption (MI 45-108) came into effect January 25, 2016 in the provinces of Manitoba, Nova Scotia, New Brunswick, Ontario, and Quebec. Saskatchewan and Alberta have since adopted the Integrated Crowdfunding Exemption. Ideally, the Integrated Crowdfunding Exemption and BC's Start-Up Crowdfunding Exemption (amended as we propose) should be available to issuers in every province and territory in Canada. The requirements and application of these exemptions should also be identical in each jurisdiction; the differences that currently exist should be eliminated. Some of the differences among crowdfunding regimes are documented in at Appendix 1.

2. Allow advertising and general solicitation

A company trying to raise capital for the first time probably does not have a list of willing investors to draw from so the ability to use the internet could increase the likelihood of a successful capital raising dramatically. Issuers and registered dealers have been allowed to use advertising and general solicitation under the accredited investor exemption and the offering memorandum exemption for over 10 years.

During this period, so far as we are aware, there has been very little abuse. Not allowing advertising, and requiring portals to put information about an offering behind a wall, creates a private room environment where issuers and portal operators have a greater ability to hide what is being said to potential investors. It is equivalent to creating a "private pitch dinner" or "timeshare presentation" which can breed high-pressure sales tactics, false information, and empty promises.

Regulators cannot police everything. With more visibility, the crowd will alert regulators and potential investors to issuers and founders who are not who they say they are or who are not abiding by the rules. Allowing advertising and general solicitation creates transparency and with this approach fraud is less likely and quickly uncovered. See Appendix 2: Prohibitions on Advertising and Soliciting.

3. Increase thresholds for required review and audit of financial statements

In Ontario, entrepreneurs who are non-reporting issuers who have distributed securities under the crowdfunding prospectus exemption must deliver financial statements to the regulator within 120 days of their financial year end. This requirement is commonly imposed globally and is entirely appropriate. However, in Ontario, the statements must be accompanied by:

- a review report or auditor's report if the amount raised by the issuer under one or more prospectus exemptions from the date of the formation of the issuer until the end of its most recently completed financial year, is $250,000 or more but is less than $750,000, or;
- an auditor's report if the amount raised by the issuer under one or more prospectus exemptions from the date of the formation of the issuer until the end of its most recently completed financial year, is $750,000 or more. (MI 45-108, s.16)

The cost of an audit plus the company time associated with the process can be a significant burden for small firms. It is not uncommon for reviews of financial statements to cost $20,000 or more, as well as additional management time. Audited financial statements can cost substantially more. These burdens are exacerbated by the fact that Ontario entrepreneurs must comply with different reporting requirements in other Canadian jurisdictions.

"There is an advertising and marketing restriction and yet on top of that there is an audited financial statement required even though you only get half a million dollars of capital. And anybody who is doing the audited financial statements knows that they can cost anywhere from twenty-five to fifty thousand dollars. So, you can imagine you're trying to raise half a million bucks and you're spending 25 to 50 thousand dollars on audited statements alone per year."

In comparison, the majority of the intra-state crowdfunding exemptions in the US do not require reviewed or audited financial statements until an issuer raises $1 million or more per year. Canadian non-reporting issuers are at a disadvantage compared to issuers located elsewhere. (And see Appendix 3)

4. Remove caps on accredited investors (to allow them to fully participate)

In all jurisdictions, if an investor indicates they are an accredited investor or a permitted client, the portal is required to obtain further information from the purchaser in order to be satisfied that the purchaser has the requisite income or assets to meet the definition of accredited investor or permitted client. This imposes additional administrative costs on small start-up companies.

Portals and issuers struggle with what is required of them to confirm and validate that someone is an accredited investor. They would like to be able to rely on self-declarations by investors or use a check-the-box approach, however, regulators across Canada have indicated that this would not be sufficient.

Our understanding is that Ontario's and Alberta's Form 45-108F3 - Confirmation of Investment Limits not only serves to provide information about investment limits but also confirms for issuers if an investor is an accredited investor. If this is true, we encourage all participating jurisdictions to adopt a uniform accredited investor confirmation and validation form that issuers and portals can rely on to determine if someone is an accredited investor.

5. Increase amount issuers may raise to $5 million

The maximum amount an issuer group can raise under the Integrated Crowdfunding Exemption in a 12-month period is $1.5 million. The NCFA is aware of no reason why this limit should not be $5 million or higher. We understand that the $1.5 million limit was based on the (then) US $1 million limit under Title III of the JOBS Act and in the U.S. Securities and Exchange Commission crowdfunding rules. Prominent leaders in the U.S. have proposed that the crowdfunding threshold be raised to US$20 million. [17] Under the intrastate crowdfunding exemptions,

[17] https://www.crowdfundinsider.com/2018/07/136823-prominent-group-of-fintech-leaders-send-letter-to-sec-chair-jay-clayton-demanding-an-increase-in-regulation-crowdfunding-to-20-million/.

caps vary from $100,000 to $5 million per year. A higher cap means greater use.

6. Eliminate caps on retail investors and investment

Under the current cap of $2,500 per retail investor or per investment, a start-up would have to crowdfund from 600 retail investors to generate the maximum $1.5 million investment. This requirement for so many individual investors is very difficult for a start-up to manage, especially if many of the investors are inexperienced with investing. Documenting all those investments in the company's investment ownership record or "cap table" is onerous and off-putting for angel investors or venture capitalists looking for a simpler capital base. It would also be challenging for companies to round up investors' approvals on the future direction of the company.

While we understand the intent to protect retail investors by limiting their investments, caps also limit the ability of the same retail investors to achieve returns or allocations that suit their investment goals and risk profile. Many retail investors are 'repeat participants' or are comfortable with the process and want to be able to increase their participation or expand their portfolio.

In the U.K. there are no caps (except for the indirect issuer cap set under the EU Prospectus Regulation of 8 million Euro).

In Australia, "both private and unlisted public companies may raise up to A$5 million (about USD $3.6 million) in any given 12-month period. Smaller (retail) investors may invest up to A$10,000 in any single crowdfunded company." [18]

7. Provide a reasonable sunset clause for ongoing disclosure requirements

An indefinite ongoing disclosure requirement only makes sense if a non-reporting issuer is continually raising capital, is planning to go public in the near term or has a finite life span. Certain ongoing disclosure requirements should not apply when an issuer has finished raising capital under the exemption. We suggest a sunset clause of one year after a non-reporting issuer finishes a capital raising exercise.

8. Less frequent filing of the distribution report

The offering memorandum and the MI 45-108 exemption distribution report must be filed every 10 days. This is an onerous (and so far as we are aware unprecedented) burden for a small exempt market dealer. In addition, the report must to be inputted multiple times since British Columbia, Ontario and others have different forms. We strongly recommend that this form be filed monthly or quarterly (as in the U.K.) and that input forms be harmonized. See Appendix 3: Frequency of reporting requirements.

Appendix 7: Submission Contributors

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[18] https://www.crowdfundinsider.com/2018/09/138943-finally-parliament-of-australia-approves-proprietary-firms-to-utilize-investment-crowdfunding/.

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