



# Backgrounder

Ontario  
Securities  
Commission

Commission des  
valeurs mobilières  
de l'Ontario

FOR IMMEDIATE RELEASE

February 19, 2015

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## EXEMPT MARKET REVIEW

As part of its exempt market review, the Ontario Securities Commission (the OSC or we) is involved in several initiatives of the Canadian Securities Administrators (CSA) as well as local initiatives:

- Prospectus exemptions – We have considered whether the existing minimum amount investment and accredited investor prospectus exemptions remain appropriate and have published amendments to these exemptions. We have also proposed new prospectus exemptions intended to facilitate capital raising by businesses at different stages of development, including start-ups and small and medium-sized enterprises, while maintaining an appropriate level of investor protection. We have also published amendments that would modify the existing short-term debt prospectus exemption relating to distributions of commercial paper, and have introduced a new prospectus exemption for distributions of short-term securitized products, primarily asset-backed commercial paper (ABCP).
- Report of exempt distribution – We have proposed changes to the report of exempt distribution to enable us to obtain better information on exempt market activity than is presently reported. We are now considering the report of exempt distribution as a separate CSA initiative and are working with the CSA to harmonize reporting requirements across all jurisdictions.

The purpose of this backgrounder is to provide an update on the current status of each of these initiatives.

### 1. Final amendments to prospectus exemptions published today

Today we published final amendments that would introduce or modify several prospectus exemptions:

Exemption	Description
Introduction by the OSC of family, friends and business associates prospectus exemption	<ul style="list-style-type: none"><li>• The exemption will allow businesses to raise capital from investors who are principals of the business or within the personal networks of the principals of the business. It is intended to enable early stage businesses to access capital.</li><li>• The exemption identifies the relationship an investor must have with the business to qualify to invest under the exemption. Further guidance is provided on determining whether an investor qualifies as a close personal friend or close business associate of a principal of the business.</li><li>• In addition, there is a requirement for investors to be given a risk acknowledgement form highlighting the key risks associated with the investment.</li><li>• Subject to Ministerial approval, the exemption will come into force on May 5, 2015.</li></ul>

Exemption	Description
CSA initiative regarding amendments to existing accredited investor prospectus exemption	<ul style="list-style-type: none"> <li>• The amendments require those persons relying on the exemption to obtain a signed risk acknowledgment from individual accredited investors (who are not permitted clients) and provide additional guidance on steps sellers could take to verify the status of purchasers who acquire securities under certain prospectus exemptions, including the accredited investor exemption. The amendments are intended to address investor protection concerns as well as concerns regarding compliance.</li> <li>• The amendments do <u>not</u> include changes to the net income, net financial asset or net asset thresholds that must be satisfied for an individual to qualify as an accredited investor.</li> <li>• The amendments change the definition of accredited investor in Ontario to allow fully managed accounts to purchase investment fund securities using the managed account category of the exemption, as is currently permitted in other CSA jurisdictions.</li> <li>• The amendments also introduce family trusts as a category of accredited investor.</li> <li>• In Ontario, the amendments will come into force on the later of May 5, 2015 and the date certain provisions of the <i>Budget Measures Act, 2009</i> are proclaimed into force.</li> </ul>
CSA initiative regarding amendments to existing minimum amount investment prospectus exemption	<ul style="list-style-type: none"> <li>• The amendments restrict the exemption to distributions to non-individual investors in order to address investor protection concerns.</li> <li>• In Ontario, the amendments will come into force on the later of May 5, 2015 and the date certain provisions of the <i>Budget Measures Act, 2009</i> are proclaimed into force.</li> </ul>
CSA initiative regarding amendments to existing short-term debt prospectus exemption relating to distributions of commercial paper	<ul style="list-style-type: none"> <li>• The amendments modify the credit rating requirements of the exemption to: <ul style="list-style-type: none"> <li>○ remove a regulatory disincentive for some commercial paper issuers to obtain an additional credit rating,</li> <li>○ provide consistent treatment of commercial paper issuers with similar credit risk, and</li> <li>○ maintain the current credit quality of commercial paper distributed under the exemption.</li> </ul> </li> <li>• Subject to Ministerial approval, the amendments will come into force on May 5, 2015.</li> </ul>
CSA initiative regarding short-term securitized products prospectus exemption	<ul style="list-style-type: none"> <li>• The amendments remove the availability of the existing short-term debt prospectus exemption and certain other prospectus exemptions for the issuance of ABCP and other short-term securitized products.</li> <li>• The amendments introduce a new prospectus exemption that is limited to conventional or traditional ABCP. The new exemption has conditions relating to credit ratings, liquidity, underlying asset pools and initial and ongoing disclosure.</li> <li>• Subject to Ministerial approval, the exemption will come into force on May 5, 2015.</li> </ul>

For further information, please see the Notice of Amendments published on February 19, 2015:

[http://www.osc.gov.on.ca/en/SecuritiesLaw\\_ni\\_20150219\\_45-106\\_amendments.htm](http://www.osc.gov.on.ca/en/SecuritiesLaw_ni_20150219_45-106_amendments.htm)

## **2. Update on other prospectus exemptions**

### **Existing security holder prospectus exemption**

A new prospectus exemption that allows public companies listed on the Toronto Stock Exchange, TSX Venture Exchange, Canadian Securities Exchange or Aequitas NEO Exchange to raise capital on a cost effective basis from existing investors in reliance on a company's public disclosure record became effective in Ontario on February 11, 2015. The exemption incorporates important investor protection measures, including, most significantly, an investment limit of \$15,000 in the previous 12 months under the exemption, if advice regarding the suitability of the investment has not been obtained.

The exemption is substantially harmonized with a similar exemption adopted by other CSA jurisdictions.

For further information, please see the Notice of Amendments published on November 27, 2014:

[http://www.osc.gov.on.ca/documents/en/Securities-Category4/ni\\_20141127\\_45-106\\_pro-amend.pdf](http://www.osc.gov.on.ca/documents/en/Securities-Category4/ni_20141127_45-106_pro-amend.pdf)

### **Offering memorandum and crowdfunding prospectus exemptions**

On March 20, 2014, we published for comment amendments that would introduce two other new capital raising prospectus exemptions in Ontario:

- an offering memorandum prospectus exemption (the OM exemption), and
- a crowdfunding prospectus exemption along with regulatory requirements applicable to an online crowdfunding portal described in proposed Multilateral Instrument 45-108 *Crowdfunding* (collectively, the crowdfunding regime).

Each is described in greater detail in the table below.

We have worked closely with staff in other CSA jurisdictions in formulating the OM exemption and the crowdfunding regime. The securities regulatory authorities in Alberta, New Brunswick, Quebec and Saskatchewan published for comment proposed amendments to the OM exemption that were similar to the OM exemption that we published for comment. The securities regulatory authorities in Manitoba, New Brunswick, Nova Scotia, Quebec and Saskatchewan also published for comment the crowdfunding regime.

The comment period ended on June 18, 2014 and the participating CSA jurisdictions collectively received approximately 916 comment letters regarding the OM exemption and approximately 45 comment letters regarding the crowdfunding regime. We are reviewing the comments and our goal is to publish the OM exemption and the crowdfunding regime either in final form or, if warranted, for a second comment period, in summer 2015.

<b>Exemption</b>	<b>Description</b>
Proposed OM exemption	<ul style="list-style-type: none"><li>• The proposed OM exemption would allow businesses to raise capital based on an offering memorandum being made available to investors. The exemption would be available for a wide range of businesses at different stages of development.</li><li>• The proposed OM exemption incorporates important investor protection measures, including:<ul style="list-style-type: none"><li>○ requirement that a comprehensive disclosure document, that is subject to statutory liability if it contains a misrepresentation, be delivered to investors at the point of sale,</li><li>○ investment limits for individual investors who do not qualify as accredited investors (\$10,000 or \$30,000 under the exemption in a 12 month period depending on the circumstances of the investor),</li><li>○ requirements to provide investors with certain limited disclosures on an ongoing basis, and</li></ul></li></ul>

Exemption	Description
	<ul style="list-style-type: none"> <li>○ requirement for investors to be given a risk acknowledgement form highlighting the key risks associated with the investment.</li> </ul>
Proposed crowdfunding regime	<ul style="list-style-type: none"> <li>● The proposed crowdfunding regime would allow businesses to raise capital from a potentially large number of investors through an online portal registered with the securities regulatory authorities. Businesses could raise up to \$1.5 million during a 12 month period. The proposed crowdfunding regime is aimed primarily at start-ups and small and medium-sized enterprises based in Canada.</li> <li>● The proposed crowdfunding regime incorporates important investor protection measures, including: <ul style="list-style-type: none"> <li>○ small investment limits (\$2,500 in a single investment and \$10,000 under the exemption in a calendar year),</li> <li>○ requirements to provide investors with certain limited disclosures at the point of sale and on an ongoing basis,</li> <li>○ requirement for investors to be given a risk acknowledgement form highlighting the key risks associated with the investment, and</li> <li>○ requirement that all investments be made through a registered crowdfunding portal.</li> </ul> </li> </ul>

#### Rights offering prospectus exemption

On November 27, 2014, the CSA published proposed amendments intended to streamline the existing rights offering prospectus exemption for non-investment fund reporting issuers. The proposed amendments address investor protection concerns as well as concerns regarding compliance. The proposed amendments include:

- updating requirements,
- removing the current regulatory review process prior to the use of the exemption,
- increasing investor protection through the addition of civil liability for secondary market disclosure,
- introducing a user-friendly form of rights offering circular, and
- allowing an increase of up to 100% in the number of outstanding securities of the class to be issued.

The proposed amendments would also repeal the exemption for non-reporting issuers. The comment period ends on February 25, 2015.

For further information, please see the Notice and Request for Comment published on November 27, 2014:  
[http://www.osc.gov.on.ca/documents/en/Securities-Category4/ni\\_2014127\\_45-106\\_pro-amend.pdf](http://www.osc.gov.on.ca/documents/en/Securities-Category4/ni_2014127_45-106_pro-amend.pdf)

#### 3. Proposed reports of exempt distribution

On March 20, 2014, we published two proposed new reports of exempt distribution for use in Ontario and certain other jurisdictions:

- Form 45-106F10 *Report of Exempt Distribution for Investment Fund Issuers (Alberta, New Brunswick, Ontario and Saskatchewan)*, and
- Form 45-106F11 *Report of Exempt Distribution for Issuers Other Than Investment Funds (Alberta, New Brunswick, Ontario and Saskatchewan)*.

The comment period ended on June 18, 2014. We received several comments regarding the need to harmonize the reports of exempt distribution across the CSA. The reports of exempt distribution are now being considered as

a separate CSA initiative and we are working with CSA members to harmonize reporting obligations to the extent possible. This initiative aims to:

- reduce the compliance burden for issuers and underwriters related to their exempt distribution reporting requirements, and
- provide regulators with the information necessary to more effectively oversee the exempt market and develop policy accordingly.

As part of this CSA initiative, we anticipate publishing for a second comment period in spring 2015.

We continue to require issuers to file a Form 45-106F1 *Report of Exempt Distribution*, as is currently required for distributions in CSA jurisdictions other than British Columbia. In British Columbia, issuers are generally required to file Form 45-106F6 *British Columbia Report of Exempt Distribution*.

#### 4. Consultation

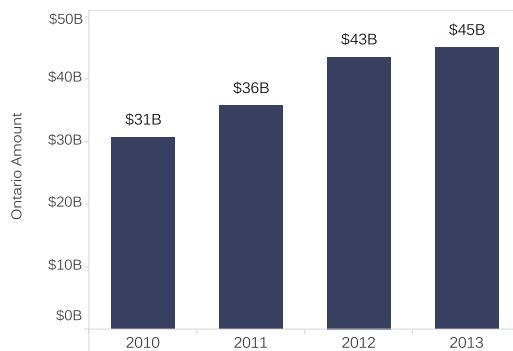
In addition to reviewing the comment letters we received on our published proposals, we have undertaken the following to obtain feedback on our proposals:

- Creation of advisory committee – We established an ad hoc committee, the OSC Exempt Market Advisory Committee, to advise on possible regulatory approaches to the exempt market. We have also consulted with other OSC advisory committees to obtain feedback on certain aspects of our exempt market review.
- Stakeholder consultations – We conducted extensive public consultations and stakeholder outreach, including hosting town hall meetings and participating in various other discussion panels and stakeholder forums. We also held one-on-one meetings with stakeholders, including:
  - TMX Group Limited advisory committees,
  - exchanges and other self-regulatory organizations,
  - foreign regulators,
  - investor advocates,
  - industry associations,
  - existing crowdfunding portals in other jurisdictions,
  - crowdfunding associations, and
  - academics.
- Investor survey – We commissioned research to gauge retail investor interest in investing in start-ups and small and medium-sized enterprises, including through crowdfunding.
- Comparative analysis – We considered the experience of other Canadian jurisdictions with prospectus exemptions not currently available in Ontario, as well as international developments relevant to capital raising in the exempt market.

## 5. Exempt market activity in Ontario

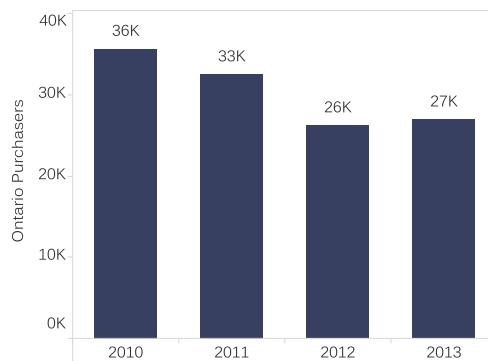
The exempt market continues to be an important part of Ontario's capital markets. In 2013, non-investment fund issuers raised approximately \$45 billion through prospectus-exempt distributions in Ontario.<sup>1</sup>

**Figure 1: Ontario amount raised by non-investment fund issuers**



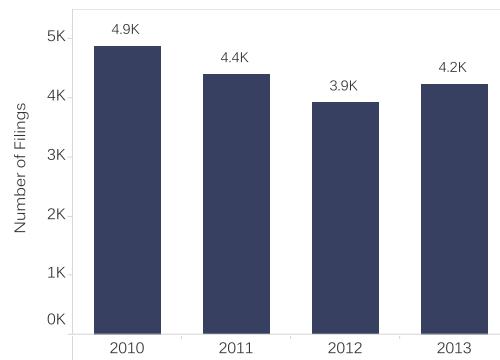
Non-investment fund issuers raised capital through approximately 27,000 purchases made by Ontario residents in 2013.

**Figure 2: Ontario purchasers in non-investment fund issuers**



Total filing activity also increased in 2013 compared to the previous year but remains below 5,000 filings per year.

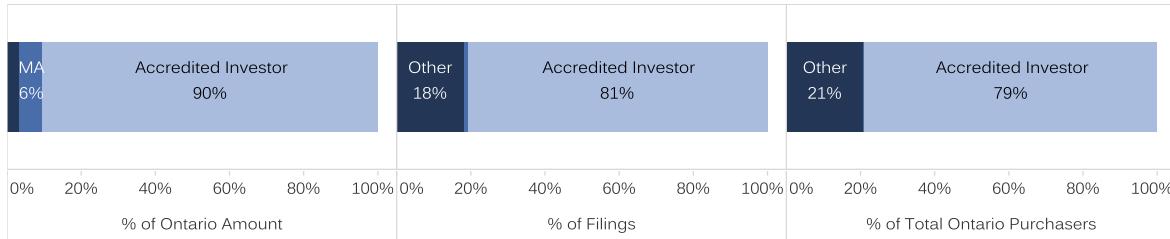
**Figure 3: Number of filings by non-investment fund issuers**



<sup>1</sup> Pre-2013 statistics from previous publications have been updated to reflect amended and late submissions.

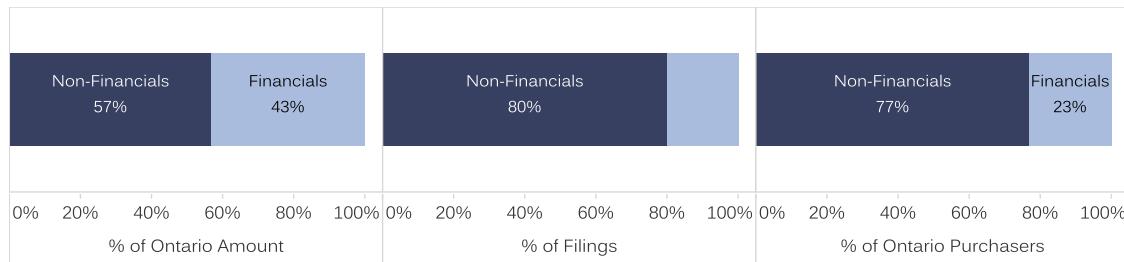
The accredited investor prospectus exemption is the most widely used prospectus exemption in Ontario by amount of capital raised (90%), number of filings (81%) and purchases (79%). The minimum amount investment prospectus exemption is the second most used prospectus exemption by amount of capital raised (6%).

**Figure 4: Use of prospectus exemptions in 2013 by non-investment fund issuers<sup>2</sup>**



Financial issuers represent 43% of the capital raised by non-investment fund issuers but only accounted for approximately 20% of filings and purchases in 2013. Examples of financial issuers are private equity firms, consumer credit securitizations, banks, mortgage investment entities and insurance firms.

**Figure 5: Types of non-investment fund issuers in 2013**



The top three non-financial sectors (technology, media and telecommunications (TMT), natural resources and real estate) accounted for over 50% of the total capital raised by non-financial issuers.

**Figure 6: Amount raised by non-financial issuers in 2013**



<sup>2</sup> The “Other” category represents instances where multiple prospectus exemptions including the minimum amount investment prospectus exemption or the accredited investor prospectus exemption were used in a single distribution.