

June 18, 2014

DELIVERED BY E-MAIL

comments@osc.gov.on.ca

Secretary
Ontario Securities Commission "OSC"
20 Queen Street West
19th Floor, Box 55
Toronto, ON M5H 3S8

Dear Sir or Madam,

**RE: Proposed Multilateral Instrument 45-108 (the proposed Instrument)
Crowdfunding Prospectus Exemption and Crowdfunding Portal Requirements
(for Ontario only)**

Thank you for the opportunity to provide comments on the proposed Instrument on both the Crowdfunding Prospectus Exemption and Crowdfunding Portal Requirements.

It is clear that the OSC has invested a lot of thought and effort in drafting the proposed Instrument. In particular, the OSC should be commended for its efforts in the following areas:

- providing retail investors with access to private markets while ensuring investor protection
- considering the operational implications on funding portals

As you work towards finalising these rules, I would encourage you to continue to engage industry participants in a dialogue to get an end-to-end view of the payment processing, clearing, settlement and custodial processes, and a more detailed picture of how each service provider interacts with funding portals. Regulations that are clear, practical and easy to implement would enable registrants to:

- structure their operations and service agreements in an effective and efficient manner
- contain the cost of capital raising activities, benefitting small to medium businesses.

My answers to the questions below are based on over 25 years experience in financial services. These answers come from the vantage point of helping registrants to

- implement OSC regulations
- structure their business operations and processes so that they meet their compliance obligations

Question 16: The Crowdfunding Portal Requirements restrict portals from holding, handling or dealing with client funds. Is this requirement appropriate? How will this impact the portal's business operations? Should alternatives be considered?

In my view, the requirement that prohibits portals from holding, handling or dealing with client funds is restrictive.

How will this impact the portal's business operations?

The proposed requirements may present an operational challenge for portals to fulfill their compliance obligations under the proposed Instrument. For example:

(a) A portal must arrange for a Canadian financial institution to hold client funds in trust, and thus it must be empowered to give instruction to the financial institution to move money in the following limited instances:

- to return the subscription monies to subscribers if a subscriber exercises his/her right to withdraw
- to refund all subscription monies raised if the conditions of closing are not met
- to transfer the proceeds raised to the issuer once the offering is completed

(b) Payment processing and settlement is integral to capital raising. If a portal is restricted from handling, holding and dealing in client funds, it must use the services of a third party. Some of these parties may not be registrants, e.g. on-line payment providers. In addition, portals may accept a variety of payment methods and from an investment viewpoint, some of the payment methods would be considered "non-traditional", e.g. on-line payment providers or even credit cards. These circumstances give rise to a number of questions:

- is there also a client relationship between the subscriber and the service provider
- would the portal have access to client information of the service provider
- where a portal is prohibited from performing certain functions, is a portal required to monitor the compliance activities of their service providers under paragraph (a) of

subsection 11.1 of National Instrument 31-103 *Conditions of Registration, Exemptions and Ongoing Registrant Obligations*

(c) Under the proposed Crowdfunding Exemption, before a distribution can be completed, a portal must confirm that the minimum amount of funds to be raised has been subscribed for (ref: subsection 43(2)). Please clarify whether you mean subscribed and fully paid for. To fulfill this obligation, a portal would need access to payment and cash deposit information (including chargebacks) in order to reconcile, by issuer, the sum of all subscriptions received from each individual purchaser with the total cash position on deposit with, or held by, a custodian. The proposed Instrument is silent on the banking arrangements to be used to temporarily hold client funds and whether it would be appropriate to commingle client funds across a number of issuers, e.g. a portal may have multiple deals in the pipelines. I can appreciate the desire to not be overly prescriptive in drafting the Instrument. However, it is worthy to note that reconciliations of client cash are more difficult when omnibus accounts are used and there is also a risk that client debit balances may result (see answer to Question 17 below). For these reasons, I would suggest that the Instrument address the issue of commingling client funds across issuers. I would also suggest that portals not commingle client cash across issuers.

Should alternatives be considered?

Yes. Portals should be allowed to hold, handle or deal with clients funds under specific circumstances. However, they should also

- have appropriate systems, processes and controls over client funds
- be required to have adequate capital and insurance coverage.

Question 17: Are there other requirements that should be imposed on portals to protect the interest of investors?

Additional disclosures

Subscribers have a right to know

- the identity of the custodian or deposit taking institution who holds their funds, since portals are required to arrange for a custodian to hold client funds temporarily
- whether their subscription proceeds are insured while on deposit with or held by the custodian. The context for this suggestion comes from the fact that the proposed Instrument does not specify the type of account used to temporarily hold subscriber funds (e.g. omnibus or individual). In addition, the account arrangement chosen by the portal and the administration of such arrangements might affect the amount of the deposit that is insured, recognizing of course that increased protection comes at a cost

- whether there is also a client relationship between a third party service provider and the subscriber as a result of an arrangement in a servicing agreement

For ease of reference, I would suggest these disclosures form part of the Offering Memorandum.

Client Debit Balances

A portal may receive payment from a subscriber and see cash credited to the bank account but the cash may not, in fact, be available. As a result, if cash is transferred to the issuer before the following items occur, it would give rise to client debit balances:

- the hold period for fund availability required by an on-line payment processor
- chargebacks on credit card payments
- stop payments on cheques

To resolve any issues around client debit balances, portals should have the following additional requirements:

- ensure that at least the minimum amount of the capital raised is available for transfer as a condition of closing, i.e., before any proceeds are transferred to the issuer
- disclose to subscribers the time period to effect a refund in the event of a withdrawal request or if the offering is not completed

Thank you again for the opportunity to comment on these matters. I would be happy to meet with you to discuss these comments.

Yours truly,



Merici Young
Managing Director