PRIVATE CAPITAL MARKETS ASSOCIATION OF CANADA

THE NATIONAL VOICE OF EXEMPT MARKET DEALERS, ISSUERS AND INDUSTRY PROFESSIONALS

VIA E-MAIL

June 30, 2014

Autorité des marchés financiers
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Financial and Consumer Services Commission (New Brunswick)
Nova Scotia Securities Commission
Ontario Securities Commission

Delivered to:

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Dear Sirs and Mesdames:

Re: Draft Regulation 45-108 *respecting Crowdfunding*
Draft Policy Statement to Regulation 45-108 *respecting Crowdfunding*
Draft Blanket Orders in Manitoba, Québec, New Brunswick and Nova Scotia on the Start-Up Crowdfunding Prospectus and Registration Exemption
Draft Amendments to General Order 45-925 – Saskatchewan Equity Crowdfunding Prospectus Exemption, (collectively, the Proposed Exemptions)

This comment letter is submitted by the Private Capital Markets Association of Canada (formerly, the Exempt Market Dealers Association of Canada) (the **PCMA**)) in response to the request for comments published by the Autorité des marchés financiers (the **AMF**), the Financial and Consumer Affairs Authority of Saskatchewan (the **FCAA**), the Financial and Consumer Services Commission of New Brunswick (the **FCNB**), the Manitoba Securities Commission (the **MSC**) and the Nova Scotia Securities

Commission (the **NSSC**) (collectively, the **Participating Jurisdictions**) regarding the Proposed Exemptions.

We thank you for the opportunity to provide our comments on these very important capital raising exemptions in Canada.

We have held Town Hall meetings and solicited feedback from participants n Toronto, Calgary, Vancouver, Saint John and Montreal and have spoken with various members of the Canadian Securities Administrators (the **CSA**) regarding the Proposed Amendments. We thank those CSA members who have engaged in this discussion with us.

WHO IS THE PCMA?

The PCMA is a not-for-profit association founded in 2002 to be the national voice of exempt market dealers (**EMDs**), issuers and industry professionals in the private capital markets across Canada.

PCMA plays a critical role in the private capital markets by:

- assisting its hundreds of dealer and issuer member firms and individuals to understand and implement their regulatory responsibilities;
- providing high-quality and in-depth educational opportunities to private capital markets professionals;
- encouraging the highest standards of business conduct amongst its membership across Canada;
- increasing public and industry awareness of the private capital markets in Canada;
- being the voice of the private capital market to securities regulators, government agencies, other industry associations and the public capital markets;
- providing valuable services and cost-saving opportunities to its member firms and individual dealing representatives; and
- connecting its members across Canada for business and professional networking.

Additional information about the PCMA is available on our website at: www.pcmacanada.com

WHO ARE EXEMPT MARKET DEALERS?

EMDs are fully registered dealers who engage in the business of trading in securities to qualified exempt market clients. EMDs are subject to full dealer registration and compliance requirements and are directly regulated by the provincial securities commissions. The regulatory framework for EMDs is set out in National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* (**NI 31-103**) and it applies in every jurisdiction across Canada.

EMDs must satisfy substantially the same "Know-Your-Client" (**KYC**), "Know-Your-Product", (**KYP**) and trade suitability obligations as other registered dealers who are registered investment dealers and members of the Investment Industry Regulatory Organization of Canada and mutual fund dealers and members of the Mutual Fund Dealers Association of Canada. NI 31-103 sets out a comprehensive dealer regulatory framework (substantially the same for all categories of dealer) which requires EMDs to satisfy a number of regulatory obligations including:

- educational proficiency;
- capital and solvency standards;
- insurance;
- audited financial statements;
- KYC, KYP and trade suitability;
- compliance policies and procedures;
- books and records;
- trade confirmations and client statements;
- disclosure of conflicts of interest and referral arrangements;
- complaint handling;
- dispute resolution;
- maintenance of internal controls and supervision sufficient to manage risks associated with its business;
- prudent business practices requirements;
- registration obligations; and
- submission to regulatory oversight and dealer compliance reviews.

EMDs may focus on certain market sectors (*e.g.,* oil and gas, real estate, mining or minerals, technology, venture financing, etc.) or may have a broad cross-sector business model. EMD clients may be companies, institutional investors, accredited investors or investors who purchase exempt securities pursuant to an offering memorandum or another available prospectus exemption.

EMDs provide many valuable services to small and medium size enterprises (**SMEs**), large businesses, investment funds, merchant banks, financiers, entrepreneurs, and individual investors, through their ability to participate in the promotion, distribution and trading of securities, as either a principal or agent.

PCMA's COMMENTS ON THE PROPOSED AMENDMENTS

Our answers to the questions you have asked in connection with the Proposed Amendments are set out below. We have reproduced the questions for ease of reference.

CROWDFUNDING PROSPECTUS EXEMPTION

Issuer Qualification Criteria

1) Should the availability of the Crowdfunding Prospectus Exemption be restricted to non-reporting issuers?

No, the PCMA feels strongly that the Crowdfunding Prospectus Exemption should be equally accessible to reporting and non-reporting issuers.

2) Is the proposed exclusion of real estate issuers that are not reporting issuers appropriate?

No, the PCMA believes that real estate is an important asset class for both investors and issuers for the reasons set out below:

(a) there are many profitable real estate investments that provide steady yield and cash flow to investors while not relying on speculation or market appreciation to provide returns. Moreover, private real estate is highly uncorrelated to the public markets and therefore provides an alternative and important cash flowing asset class for yield-hungry investors;

(b) investors can be educated on how real estate is valuated. Expenses and budgets can be accurately projected up front so that investors are made aware of the projected costs and revenues before subscribing to an investment. In fact, certain CSA members have published guidance on such matters (*e.g.,* Ontario Securities Commission (**OSC**) Staff Notice 51-721);

(c) many investors understand real estate and want to invest in their communities;

(d) many investors do not have the time, experience or capital to invest in a real estate project on their own. However, they can invest a small amount that forms a part of their individual

portfolio while partnering with an experienced real estate developer/property manager to operate the asset; and

(e) real estate investments create jobs for local small and medium enterprises **(SMEs**). For example, a single $1.5M equity crowdfunding investment can support a real estate development of $5M with the use of a typical real estate mortgage. This project would be injecting roughly $1.5M into labour costs in the local economy, as well as $500,000 to professional trades. Another $600,000 would be transferred to the local municipality through development fees as well as $200,000 to the local utilities. A single project could create over 30 full time jobs at an annual salary of $60,000. To suggest that the Crowdfunding Prospectus Exemption should exclude real estate as an entire asset class since it does not help SMEs is incorrect and misguided.

We understand there are concerns about potential conflicts of interest when a crowdfunding portal raises capital for real estate projects where it has a material interest (*i.e.*, where the issuer and owner of a project is a related issuer of the portal). The PCMA believes that these concerns can be adequately addressed through appropriate existing disclosure requirements under applicable securities law. Moreover, if there is a need for additional structural safeguards, such as independent review committees, we believe this is best addressed outside of a review of the Crowdfunding Prospectus Exemption since such matters would apply to all prospectus exemptions that are relied upon by a dealer that is related to an issuer. We refer the Participating Jurisdictions to the attached **Schedule "A"** where we have included our response to the OSC's proposed prohibition on related issuers under the OM Prospectus Exemption, which equally apply to the Crowdfunding Prospectus Exemption.

The PCMA opposes the exclusion of real estate issuers from using the Crowdfunding Prospectus Exemption and, in particular, we believe that income producing real estate is an important and viable asset class for investors that should not be prohibited by the Participating Jurisdictions.

3) The Crowdfunding Prospectus Exemption would require that a majority of the issuer's directors be resident in Canada. One of the key objectives of our crowdfunding initiative is to facilitate capital raising for Canadian issuers. We also think this requirement would reduce the risk to investors. Would this requirement be appropriate and consistent with these objectives?

Generally, this sort of requirement is contrary to the borderless nature of an online "e-commerce" business. The Canadian start-up and SME community are in fierce competition for talent, markets and capital with US and international companies. If the Crowdfunding Prospectus Exemption for issuers is

too restrictive, Canadian entrepreneurs will simply bypass the Canadian capital markets. Moreover this not a restriction under any other existing prospectus exemption.

Restricting board makeup to be a majority of Canadian residents is a serious barrier to Canadian issuers building the right team (including its board of directors) to compete on a global scale. The proposed regulation is a serious concern to the PCMA. SMEs have a hard enough time attracting great management and board members without putting geographic constraints on an issuer.

Similarly, limiting the use of the Crowdfunding Prospectus Exemption to Canadian domiciled companies severely undermines the market opportunity for Canadian-based Crowdfunding portals to survive and flourish in this burgeoning new global business model. As long as the proper cross-border documents are filed with US and Canadian securities regulators, and the issuer has a registered business location in Canada, there should be no restriction on US companies using the Crowdfunding Prospectus Exemption.

Finally, an equally important consideration in the Crowdfunding movement is allowing the general public to participate in the next Apple, Google, Facebook or Twitter. By limiting US start-ups from accessing the Canadian capital markets (which is what this proposal effectively does) we are limiting the Canadian public's opportunity to participate as an investor in "the next big thing".

Offering Parameters

4) The Crowdfunding Prospectus Exemption would impose a $1.5 million limit on the amount that can be raised under the exemption by the issuer, an affiliate of the issuer, and an issuer engaged in a common enterprise with the issuer or with an affiliate of the issuer, during the period commencing 12 months prior to the issuer's current offering. (a) Is $1.5 million an appropriate limit? (b) Should amounts raised by an affiliate of the issuer or an issuer engaged in a common enterprise with the issuer or with an affiliate of the issuer be subject to the limit? © Is the 12 month period prior to the issuer's current offering an appropriate period of time to which the limit should apply?

(a) Yes, $1.5 million is an appropriate limit, however, if a sunset clause is introduced for this exemption, then it should be revisited in the future. We note there is already concern in the US that its proposed limit of $1 million should be increased to $2-3 million.

(b) Yes, the amounts raised by an affiliate of the issuer or an issuer engaged in a common enterprise with the issuer or with an affiliate of the issuer should be subject to the limit.

(c) Yes, the 12 month period prior to the issuer's current offering is an appropriate period of time to which the limit should apply.

5) Should an issuer be able to extend the length of time a distribution could remain open if subscriptions have not been received for the minimum offering? If so, should this be tied to a minimum percentage of the target offering being achieved?

Yes, the PCMA believes that in many cases 90 days may not be sufficient time to close a crowdfunding transaction. If the concern is that information becomes stale if the offering is open for too long, then we suggest the offering be allowed to remain open for a further 90 days provided that:

- 20% of the offering has been raised; and
- the information about the offering on the portal is still accurate or it is updated to change any stale dated financials or other information.

Restrictions on Solicitation and Advertising

6) Are the proposed restrictions on general solicitation and advertising appropriate?

Yes, the PCMA believes the proposed restrictions on general solicitation are appropriate. However, additional guidance is required in connection with an issuer undertaking a concurrent offering under another prospectus exemption and the advertising that can be done in relation thereto while the issuer is also doing its crowdfunding offering on a portal.

Investment Limits

7) The Crowdfunding Prospectus Exemption would prohibit an investor from investing more than $2,500 in a single investment under the exemption and more than $10,000 in total under the exemption in a calendar year. An accredited investor can invest an unlimited amount in an issuer under the AI Exemption. Should there be separate investment limits for accredited investors who invest through the portal?

The PCMA believes that in the absence of any income or net worth tests to determine eligible or accredited investor status, the proposed funding caps are too low and will make it extremely difficult for issuers to complete a $1.5 million fundraising under the proposed Crowdfunding Prospectus

Exemption. For example, it would take 600 investors each investing $2,500, to raise $1.5 million. This base of investor support is impossible for start-up and early stage companies to achieve.

The PCMA submits that the Participating Jurisdictions should increase the investment limit from $2,500 to $5,000 for non-eligible investors, and also consider allowing the non-eligible investors to "top up" the amount invested in a single offering to the $10,000 annual maximum.

We further submit that the crowdfunding investment limits should be increased for accredited investors (who invest through an equity crowdfunding portal). An increased limit for accredited investors would:

(a) allow issuers to more easily achieve their financing goals by having funding portals attract accredited investors and achieve a certain amount of confidence in their offering by having an accredited investor invest a larger sum of money as a "lead investor"; and

(b) permit funding portals to be fairly compensated in relation to the distribution of securities to an accredited investor. For example, an accredited investor having sourced the transaction on the funding portal, but faced with an investment limit, could otherwise directly approach an issuer for the purchase of its securities and thereby bypass the funding portal.

We suggest that investment limits should be increased for accredited investors participating through a funding portal under the Crowdfunding Prospectus Exemption, without introducing suitability obligations for the portal. We submit a precedent has been set in Ontario and Quebec with the exemptive relief order received by MaRS VX. This order establishes a $25,000 investment limit for accredited investors per transaction and $50,000 limit annually in any and all transactions under this exemption, with a corresponding obligation to verify an investor's status as an accredited investor and without having any obligation to determine whether such an investment is suitable for that accredited investor.

Alternatively, we also refer you to our answer to question 18 below where a registered dealer should be able to raise capital for issuers under the Crowdfunding Prospectus Exemption and raise an unlimited amount of money from an accredited investor, provided that the registered dealer complies with applicable securities law including its obligation to ensure an investment is suitable.

Statutory or Contractual Rights In the Event of a Misrepresentation

8) The Crowdfunding Prospectus Exemption would require that, if a comparable right were not provided by the securities legislation of the jurisdiction in which the investor resides, the issuer must provide the investor with a contractual right of action for rescission or damages if there is a misrepresentation in any written or other materials made available to the investor (including video). (a) Is this the appropriate standard of liability? (b) What impact would this standard of liability have on the length and complexity of offering documents?

(a) No, , this is not the appropriate standard of liability. The PCMA believes that an issuer and a portal must comply with applicable regulatory regimes in the different CSA jurisdictions. Each CSA member imposes or does not impose statutory rights of action for various reasons and the PCMA believes having a Crowdfunding Prospectus Exemption should not change the status quo unless it is changed for all prospectus exemptions.

(b) We are not concerned whether adding rights of action increase the length and complexity of an offering document since it is an important investor protection safeguard.

Provision of Ongoing Disclosure

9) How should the disclosure documents best be made accessible to investors? To whom should the documents be made accessible?

Offering documents should be published online and downloadable. Online disclosure and ongoing communications should be available to all shareholders and can be password protected to protect an issuer's confidential information.

10) (a) Would it be appropriate to require that all non-reporting issuers provide financial statements that are either audited or reviewed by an independent public accounting firm? (b) Are financial statements without this level of assurance adequate for investors? (c) Would an audit or review be too costly for non-reporting issuers?

(a) The PCMA believes that financial statements are essential for the purposes of determining the financial health and historical performance of an issuer. However, the PCMA also believes that a requirement for all non-reporting issuers to provide financial statements that are audited or reviewed by an independent public accounting firm as unwarranted

and too costly for many SMEs, unless they have raised in excess of a certain amount of capital.

The proposed Crowdfunding Prospectus Exemption provides that an issuer that has raised in excess of $500,000 and expended more than $150,000 is required to have audited financial statements. The PCMA submits that a review engagement should be required if both proposed thresholds are triggered, and that an audit requirement only be imposed when $1 million, or more has been raised by an issuer and/or it has expended more than $250,000 since inception. Simply, the PCMA believes the current review engagement and audit triggering thresholds are too low.

(b) In a perfect world, audited financial statements would typically be preferred by investors. However, not all start-ups and SMEs can afford audited financial statements. PCMA submits that investor protection and the level of assurance of financial statements must be balanced against the amount of capital raised and an issuer's financial ability to provide financial statements with a higher level of assurance.

(c) An audit or review would be too costly for many start-ups and should only apply after an issuer has raised and expended a certain amount of money. See also our answer in 10(a) above for our proposed revised thresholds.

11) The proposed financial threshold to determine whether financial statements are required to be audited is based on the amount of capital raised by the issuer and the amount it has expended. Are these appropriate parameters on which to base the financial reporting requirements? Is the dollar amount specified for each parameter appropriate?

No, the PCMA believes the threshold amounts in the proposed Crowdfunding Prospectus Exemption are too low. See above response under question 10 above.

Other

12) Are there other requirements that should be imposed to protect investors?

No, the PCMA believes that the proposed mechanisms relating to investor protection are adequate.

CROWDFUNDING PORTAL REQUIREMENTS

General Registrant Obligations

13) The Crowdfunding Portal Requirements provide that portals will be subject to a minimum net capital requirement of $50,000 and a fidelity bond insurance requirement of at least $50,000. The fidelity bond is intended to protect against the loss of investor funds if, for example, a portal or any of its officers or directors breach the prohibitions on holding, managing, possessing or otherwise handling investor funds or securities. Are these proposed insurance and minimum net capital amounts appropriate?

Yes, the PCMA believes that the proposed requirements are acceptable and consistent with industry standards.

Additional Portal Obligations

14) Do you think an international background check should be required to be performed by the portal on issuers, directors, executive officers, promoters and control persons to verify the qualifications, reputation and track record of the parties involved in the offering?

Yes, but subject to our comments below.

The process involved in conducting an international background check varies widely depending on the applicable jurisdiction (as does the legislation governing privacy law). It could cost thousands of dollars per search, depending on the jurisdiction. Furthermore, translation considerations and the time involved in obtaining credible results may hinder the ability of an issuer to proceed with an offering in a timely manner. For these reasons, the PCMA believes that the obligation to conduct international background checks on the insiders of an issuer would be a complex, burdensome and a costly requirement for both portals and issuers.

The PCMA believes the Participating Jurisdictions should provide additional guidance on what work needs to be done for an international background check. The Participating Jurisdictions should consult with those service providers that currently provide such international background checks for potential directors who seek to be on the board of an issuer listed on a stock exchange. The Participating Jurisdictions need to balance the costs for these international background checks with the need to protect investor from individuals who are bad actors.

Prohibited Activities

15) The Crowdfunding Portal Requirements would allow portal fees to be paid in securities of the issuer so long as the portal's investment in the issuer does not exceed 10%. (a) Is the investment threshold appropriate? (b) In light of the potential conflicts of interest from the portal's ownership of an issuer, should portals be prohibited from receiving fees in the form of securities?

(a) The PCMA believes that the 10% ownership limit for a portal in an issuer is acceptable. PCMA believes any conflicts of interest in obtaining such an equity interest in an issuer is adequately addressed under the Crowdfunding Prospectus Exemption since a portal is prohibited from:

(i) providing specific recommendations or advice to investors about specific securities;

(ii) soliciting purchases or sales of securities offered on its platform (other than through posting an offering on its platform); and

(iii) compensating employees or agents to solicit the sale of securities on their platform, the PCMA does not believe that portals should be prohibited from receiving fees in the form of securities.

Some portals in other parts of the world have raised capital for themselves on their own portal, such as Crowdcube in the United Kingdom. We believe a portal should be able to raise capital on its own portal for itself subject to certain conflicts of interest disclosure. Many investors may want to invest in a portal and a portal should not have to go to a dealer and pay a commission in order to raise capital for itself.

(b) No, a portal should not be prohibited from receiving securities as compensation for its services. Dealers typically receive cash and warrants in connection with an offering.

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?

The PCMA is not clear how a portal cannot hold, manage, possess or otherwise handle investor funds. For example, if an escrow account is set up at a financial institution, is this an account of the portal or

that of the issuer? A third party escrow agent will likely want little to no liability and only take instructions from a third party. It would make sense that this gate-keeper function would be handled by the portal and not the issuer. Investors would also typically expect a portal to be involved in collecting and disseminating any funds. We respectfully request additional clarification on this matter.

Other

17) Are there other requirements that should be imposed on portals to protect the interests of investors?

No, the PCMA believes that the proposed requirements governing portals are acceptable.

18) Will the regulatory framework applicable to portals permit a portal to appropriately carry on business?

We have a few concerns about portal ownership matters as discussed below which we would appreciate if you could clarify.

(a) Existing registered dealers should be able to use the Crowdfunding Prospectus Exemption

The PCMA is concerned that the proposed regulation of crowdfunding portals prohibits EMDs and investment dealers from operating a crowdfunding portal and relying on the Crowdfunding Prospectus Exemption to raise capital. We believe registered dealers should be able to raise capital under the Crowdfunding Prospectus Exemption, or for that matter, any prospectus exemption, adopted in any CSA jurisdiction. Registered dealers understand corporate finance and capital raising and have important exempt market experience new market entrants, such as a restricted portal dealer, may not have.

(b) A holding company should be able to own and operate a restricted portal deal and EMD

The PCMA seeks clarity on whether a holding company can own a restricted dealer, operating as a crowdfunding portal, as well as an EMD. Some groups would like to raise capital through a crowdfunding portal under the Crowdfunding Prospectus Exemption and concurrently under existing prospectus exemptions through an EMD. Moreover, crowdfunding portals may want to refer accredited investors to a related EMD instead of a third party EMD. In such circumstances, these crowdfunding portals would receive a smaller referral fee as opposed to a full transaction commission. Moreover, the accredited investor may invest directly with an issuer without paying any

fee to the portal after becoming aware of the investment opportunity from the portal where it first saw the investment opportunity. Many crowdfunding portals believe their economic viability depends on whether they can also raise capital through a related EMD under other prospectus exemptions.

Based on the foregoing, the PCMA submits that a holding company should be able to own a portal that is registered as a restricted dealer as well as an EMD provided that they are each a separate legal entity that is operating and regulated in two different manners under Canadian securities law. In these scenarios, it is very important that executive oversight, board governance and compliant processes be shared (*e.g.,* shared Chief Compliance Officer) in order to ensure the business viability of the emerging registrants in the crowdfunding portal operator marketplace.

The PCMA submits that this related company ownership model is a viable solution and reduces the risk of any public confusion involving a dually registered firm which we understand is the CSA's concern.

(c) Other Matters

Lastly, we would appreciate if the Participating Jurisdictions could clarify whether a single EMD can act as a registered dealer for more than one unregistered funding portal. We understand certain portals want to work with one EMD who has the necessary infrastructure, experience, knowledge and scale to act as a registered dealer in connection with the on-line sale of securities. These funding portals would prominently display on their website the name of the EMD they are working with. A discussion of this practice and what information would have to be displayed on the funding portal's website would be appreciated.

STARTUP EXEMPTION

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19) Considering that the Start-Up Exemption will be substantially harmonized amongst the Participating Jurisdictions, it is our intention to allow a portal established in one Participating Jurisdiction to post offerings from issuers established in another Participating Jurisdiction. Also, portals established in one Participating Jurisdiction would be allowed to open their offerings to investors from other Participating Jurisdictions. Do you see any problems with this approach?

The PCMA does not see any problem with cross-jurisdictional offerings between the Participating Jurisdictions provided the portal is registered as a restricted dealer under applicable securities law. The Participating Jurisdictions should provide guidance on what type of disclosure should be

provided by a portal to ensure that investors in non-Participating Jurisdictions cannot complete transactions on the portal.

20) One of the major differences between the Crowdfunding Prospectus Exemption and the Start-Up Exemption is that there is no registration requirement for the portal under the Start-Up Exemption. (a) Do you think there are appropriate safeguards to protect investors without the registration of the portal? (b) If not, please indicate what requirements should be imposed to the portal in order to adequately protect investors.

(a) No, the PCMA does not believe having an unregistered funding portal under the Start-Up Exemption adequately protects investors for the following reasons:

i. An unregistered funding portal would have no liability in the event of fraud. If a fraud did occur, the CSA membersin the Participating Jurisdictions would have little or no recourse against the unregistered portal.

ii. It is important to establish trust in capital raising and an unregistered funding portal increases the risk that trust will be lost if fraud does occur on its platform and adversely impact all equity crowdfunding. The media and public will not distinguish between a regulated portal raising capital under the Crowdfunding Prospectus Exemption and an unregulated portal raising capital under the Start-Up Exemption if fraud takes place. The potential damage this could cause to the equity crowdfunding industry is not fair to those regulated portals raising capital under the Crowdfunding Prospectus Exemption.

iii. Unregulated equity crowdfunding portals are akin to unregulated donation or rewards-based non-equity crowdfunding portals. The PCMA is concerned that non-equity rewards-based crowdfunding portals will be actively involved in providing equity crowdfunding under the Start-up Exemption. There is a big difference between regulated and unregulated crowdfunding.

iv. PCMA believes the public will be confused when an unregulated non-equity funding portal is involved in equity crowdfunding. Simply, the PCMA does not believe unregulated non-equity funding portals should also be allowed to engage in equity crowdfunding under the Start-Up Exemption. This is no different than the prohibition

against a restricted dealer being dually registered as an exempt market dealer, as discussed in proposed Multilateral Instrument 45-108 Crowdfunding. Accordingly, we believe a non-equity crowdfunding portal should be prohibited from selling securities on the internet unless it is registered with an applicable Canadian securities regulator. Otherwise, we believe the Participating Jurisdictions would be inviting fraud which is not in the public interest and be generally bad for the capital markets.

v. An unregistered funding portal under the Start-up Exemption is contrary to the "business trigger" test which would ordinarily require a funding portal selling securities on the internet to be registered as a dealer under applicable securities law. We are of the view that a portal distributing securities and posting offering materials on the internet for valuable consideration triggers dealer registration. This would be a fundamental deviation from existing securities laws involving the registration requirement and cause public confusion.

vi. Lastly, the Start-Up Exemption requires an issuer to pre-file its offering document with its principal regulator and for officers, directors and certain other prescribed individuals of an issuer (the **Prescribed Individuals**) to provide its principal regulator with certain background information in order to allow its principal regulator to do background checks.

PCMA believes investors may incorrectly assume a principal regulator's review of an issuer's offering document and background checks will be interpreted as having 'approved' an offering and that the Prescribed Individuals are acceptable to the principal regulator. In addition, the PCMA does not believe any disclaimer by a principal regulator will relieve it of any perceived approval or liability in the eyes of the investing public. We believe this should be the responsibility of the funding portal and not the principal regulator. Accordingly, the PCMA believes that all funding portal should be registered.

(b) The PCMA recommends that the Participating Jurisdictions reconsider this aspect of the Start-up Exemption and require the registration of the funding portal as a restricted dealer, since investments in small businesses may be high risk and some investors will lose money and should be afforded the protections of a registrant when making such investments.

PCMA believes a funding portal under the Start-Up Exemption should be subject to the same requirements as a funding portal under the Crowdfunding Prospectus Exemption in order to adequately protect investors.

21) We are considering imposing a limit per calendar year of 2 capital raises by an issuer of a maximum amount of $150,000 under the exemption ($300,000 per year). Are these limits appropriate? If not, please provide what you would consider acceptable limits given the parameters of the proposed exemption.

The Start-up Exemption, as proposed, is intended to assist start-up and early stage companies. It enables companies to raise relatively small amounts of capital by providing relief from certain disclosure requirements, such as financial statements and a robust offering document, thereby reducing the cost of capital for start-ups.

While we believe the $150,000 limit per capital raise is appropriate, limiting the number of raises per calendar year is problematic. The financing needs of start-ups can be unpredictable, and limiting this to twice per year is unnecessarily restrictive.

Accordingly, the PCMA believes an alternative approach would be to limit the maximum amount of capital that can raised under the exemption during the lifetime of an issuer to a maximum amount of $500,000 (the **Threshold Amount**). Once the Threshold Amount is raised, an issuer could no longer rely on the exemption.

Having a Threshold Amount is consistent with the proposed Crowdfunding Prospectus Exemption, where additional disclosure (*e.g.,* audited financials) is required once an issuer has raised more than $500,000 and expended more than $150,000.

The PCMA submits that the calculation of the Threshold Amount should include all monies raised by the issuer through any other prospectus exemption, such as the private issuer exemption or the family, friends and business associates exemption under NI 45-106.

The PCMA believes that if an issuer raises more than the Threshold Amount, then additional disclosure and investor protection safeguards would be required.

22) The Start-Up Exemption would prohibit an investor from investing more than $1,500 in a single investment under the exemption. (a) Is this limit appropriate? (b) Should there also be a limit on the dollar amount that may be invested on a yearly basis by an investor?

Our answers below assume the portal under the Start-Up Exemption is regulated as a restricted dealer as per our response in question 20 above.

(a) The PCMA agrees with an investment limit, and that this limit should be based on a fixed dollar amount since an investment limit based on a percentage of an investor's net assets or income would add complexity to the Start-up Exemption. PCMA submits that the investment limits should be increased to a maximum $2,500 per investment under the Start-Up Exemption and $5,000 per investment under the Crowdfunding Prospectus Exemption.A higher limit could be introduced after a period of time, following implementation and a review of the investment limits under the Start-Up Exemption.

However, we suggest that limits should be removed or increased for accredited investors participating through a funding portal under the Start-Up Exemption, without introducing suitability obligations for the portal. A reasonable precedent has been set in Ontario and Quebec with the exemptive relief order obtained by MaRS VX, which allows accredited investors to invest up to $25,000 in a single transaction but no more than an aggregate amount of $50,000 per annum, without a suitability obligation imposed on the portal.

Alternatively, we also refer you to our answer to question 18, above, where we submit that a registered dealer should be able to raise capital under the Crowdfunding Prospectus Exemption on behalf of an issuer. In such circumstances, a registered dealer operating a portal under the Start-Up Exemption should be able to raise an unlimited amount of money from an accredited investors, *provided that* the registrant complies with applicable securities law including, its obligation to ensure an investment is suitable.

(b) The PCMA believes there is a need to introduce an annual limit on the dollar amount invested under the Start-Up Exemption which should be similar to the investment cap of $10,000 under the Crowdfunding Prospectus Exemption.

23) Should there be minimal ongoing disclosure that issuers be required to provide to their security holders? If yes, what should it be?

No, the PCMA believes that disclosure requirements for security holders under Canadian corporate law, is adequate.

24) We expect issuers using the Start-Up Exemption to maintain the information provided in the *Issuer Information* form and the *Offering Document* form updated throughout the distribution period. Should there be an obligation for issuers to further update that information outside the distribution period?

No, the PCMA believes that maintaining the issuer and offering forms outside of the distribution period represents an unnecessary requirement and cost to issuers. Refer to question 23) regarding our comments regarding ongoing disclosure.

25) Should investors have the right to withdraw their subscription at least 48 hours prior to the disclosed offering deadline, as proposed under the Crowdfunding Prospectus Exemption?

No, the PCMA believes investors should not have the right to withdraw their subscription at least 48 hours prior to the offering deadline – rather, investors should have a two-day withdrawal right after they commit to an investment. Allowing withdrawal rights at least 48 hours prior to the disclosed offering deadline would allow promoters to 'game the system' and recruit investors to invest intially to give the appearance of a successful capital raise only to have them withdraw prior to the deadline.

26) For Nova Scotia only, should Community Economic Development Investment Funds (CEDIFs) be eligible to use the Crowdfunding Prospectus Exemption and/or Start-Up Exemption? If so, why? If not, why?

Yes, the PCMA believes that CEDIFs should be eligible to use the Crowdfunding Prospectus Exemption and/or the Start-Up Exemption notwithstanding the investment fund prohibition. CEDIFs are a critical part of the capital raising ecosystem in Nova Scotia and tax-incented structures should work hand-in-hand with the Crowdfunding Prospectus Exemption and/or Start-Up Exemption.

27) Are there other requirements that should be imposed to protect investors, taking into account the stage of development of the issuers susceptible to issue securities under the exemption?

No, the PCMA believes the proposed requirements are adequate.

The PCMA submits that the current OM Prospectus Exemption is likely not an appropriate exemption for start-up businesses and that CSA members who are not a Participating Jurisdiction should consider adopting the Start-Up Exemption, provided that the concerns we address above can be addressed.

* * *

We thank you for the opportunity to provide you with our comments on the Proposed Amendments and would be pleased to discuss this with you further.

Yours very truly,

Private Capital Markets Association of Canada

"Brian Koscak"	*"Geoffrey Ritchie"*
Chair	Executive Director

cc: PCMA Canada, Board of Directors

Schedule "A"

Extract from the PCMA response to the OSC involving Question #8 in its March 20, 2014 request for comments on the Proposed OM Exemption involving the related issuer prohibition.

…

Registrants

8) Do you agree with our proposal to prohibit registrants that are "related" to the issuer (as defined in National Instrument 33-105 Underwriting Conflicts) from participating in an OM distribution? We have significant investor protection concerns about the activities of some EMDs that distribute securities of "related" issuers. How would this restriction affect the ability of start-ups and SMEs to raise capital?

The PCMA does not agree with the OSC's proposal to prohibit registrants that are "related" to an issuer from participating in an OM distribution. Having to contract the services of a non-related EMD to undertake a financing transaction will simply increase the cost of capital for issuers who want to distribute their own securities, and unduly restrict capital raising.

We respectfully disagree with the assumption that selling securities of a related issuer is fundamentally unsound and should be prohibited. Conceptually, there are many valid business reasons for an issuer selling its own securities including wanting to pay no or little commissions to third parties and controlling its own distribution channels.

We believe if an issuer is in the "business of trading" securities and must become registered as a dealer, or sell securities through a dealer, the fact that an issuer becomes registered should be seen as a positive outcome from a regulatory and industry perspective. This was a fundamental intention behind NI 31-103. The issuer itself, or through a related entity, is now regulated and subject to the securities laws governing all registrants and its particular category of registration. However, the OSC appears to be taking the view that this situation is somehow worse for investors than when the issuer was unregulated. We strongly disagree.

We believe the public interest is served by having such an issuer registered and subject to the full oversight of a securities regulator. Accordingly, the question should be about what, if any, measures are needed to better regulate a dealer selling securities of a related issuer rather than the imposition of a blanket prohibition. We respectfully submit that the prohibition is an over-reaction to some

dealers apparent disclosure and KYC deficiencies and is not the appropriate approach in these circumstances.

We note that no other CSA member, other than Ontario and New Brunswick, has proposed a prohibition on selling securities of related issuers. In the interest of harmonization and to avoid administrative confusion and complexity, we encourage the OSC to seriously reconsider its views on such matters and work with industry in developing a better way of managing such conflicts that protects investors and provides for fair and efficient capital markets.

The PCMA further submits that an outright prohibition does not recognize the significant work the OSC has already done in the exempt market through its communication and education of EMDs with respect to their obligations of KYP, KYC, and suitability under NI 31-103. We specifically note the work done by the OSC through annual compliance reports, dealer compliance reviews and OSC Outreach education seminars which help registrants understand the requirements for additional disclosure pertaining to related and connected issuer relationships, including those in National Instrument 33-105 – *Underwriting Conflicts*.

The PCMA believes registrants must constantly balance the best interests of the issuer, the investor and their own businesses and are capable of managing any conflicts of interest through commonly accepted industry practices.

Specifically, the PCMA submits that conflicts of interest are best managed through disclosure and a variety of techniques currently employed within the investment industry such as:

1. educating/enforcing the application of appropriate suitability standards, especially when conflicts of interest are involved;
2. providing continuing education for registrants about conflict identification and management techniques;
3. having documented policies and procedures that address KYC/KYP and conflicts of interest and in particular those involving related and connected issuers ;
4. implementing enhanced client disclosures/acknowledgements (*i.e.*, the relationship disclosure documents);
5. introducing independent product reviews by third parties much like an independent review committee involving mutual funds;
6. specific categorization of the relationship such as “principal distributor” (*i.e.,* manufacturer/distributor associated with offering documents) and providing enhanced disclosure related thereto;

7. expanding rights of rescission/withdrawals, and categorization of a transaction as "solicited/not solicited" and providing guidance on specific actions to be taken by a dealing representative and dealer in such circumstances; and
8. providing for enhanced compliance reviews by OSC field staff of dealers that sell securities of related issuers, perhaps through a new risk category for firms distributing related products that applies across all categories of dealers (including IIROC and MFDA dealers).

In addition, we believe that among the most effective tools used for conflict management is client disclosure and acknowledgements. Effective disclosure ensures that the client is fully aware of the conflict and the nature and extent of any conflict of interest prior to a transaction. Conflict disclosure has been successfully used in other segments of the investment industry and it is reasonable to assume that it would be equally successful in the exempt market.

Lastly, other factors the OSC should consider before prohibiting related issuers from availing themselves of the OM Prospectus Exemption are as follows:

1. there are many issuers in the financial services sector that already sell related products to their customers such as banks, insurance companies, investment dealers and mutual fund companies. For example, individuals know they are buying a Ford automobile from a Ford dealership, a State Farm insurance policy from a State Farm insurance agent or an Investor's Group mutual fund from an Investor's Group mutual fund dealer;
2. by allowing issuers to take advantage of their own distribution networks to raise capital without paying a commission or paying a reduced commission, issuers would have more capital to invest on behalf of investors;
3. by having the issuer as a registrant, the trades would be required to pass the same scrutiny for KYC, KYP and suitability as through any other registrant; and
4. issuers are currently able to do a non-brokered private placement directly to investors where these investor protections are completely circumvented.

We remind the OSC of the work that was done in the mutual fund industry in dealing with conflicts of interest, which resulted in, among other things, the creation of independent review committees under NI 81-107 and continuous disclosure requirements under National Instrument 81-106. We believe there are a number of existing regulatory tools available for regulators to address situations where related party products are sold by providing the necessary disclosures and other steps to manage and control potential conflicts of interest.

We are aware that the OSC is concerned with certain EMDs selling securities of related issuers and support further work in this area rather than invoking a complete prohibition.