



**Remarks by Howard Wetston**

**Chair, Ontario Securities Commission**

**Private Capital Markets Association Annual Conference**

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**Check against delivery**

Good morning - and thank you for inviting me back to speak at your conference again this year. Last year, when I was here, we were in the middle of reviewing the extensive feedback we received on our consultation paper on prospectus exemptions.

At that time I indicated that regulatory obstacles to capital formation in Ontario needed to be addressed.

The issuance of the consultation paper demonstrated how the markets and our thinking have evolved. A year later I can safely say things are moving forward.

I see that things are also moving forward for the PCMA and not just in name only. I note the release of your new magazine, “Private Capital Markets”.

When I joined the Commission over three years ago, your publication was in a newspaper format. Now it’s a sophisticated glossy.

This symbolizes the importance of private capital markets in Ontario and Canada, as well as the evolving role of the PCMA in supporting its members on understanding their regulatory responsibilities and ensuring diligent standards of business conduct.

The latest edition of your publication is about “unlocking capital raising” and, at the OSC, we’re committed to doing our part.

How are we doing it? By being responsive. Changes in technology, innovations in the markets, a plethora of new products, cost pressures, changing attitudes of entrepreneurs and investors - these are all factors that are informing the OSC's approach to capital formation.

I'm sure you're familiar with our four proposed new prospectus exemptions.

Just to remind you, I'm talking about

- 1) Introducing an offering memorandum exemption in Ontario.
- 2) Raising capital from family, friends and business associates.
- 3) Rights offerings, based on a company's public disclosure record.
- 4) Crowdfunding through registered online platforms.

As you know, while some of these exemptions have existed in other provinces, these are game-changing proposals for Ontario.

Why are we doing this?

⇒ To reduce obstacles to capital formation in the face of a difficult environment for SMEs and entrepreneurs to raise funds. That's important for industry and investors alike.

⇒ To recognize that the balance between public and private markets is changing.

When we talk about capital formation, we need to consider the entire market – both public and private. Historically the regulatory system has exhibited a focus towards public markets and reliance on “full true and plain disclosure”. Access to private markets by both issuers and investors has been carefully limited through regulation considered necessary for investor protection.

The traditional model has been that investor protection and market efficiency required issuers to comply with public company disclosure standards if they wanted to raise funds from more than a few select investors. That continues to be true in many instances.

However, that conventional approach is now giving way to a continuum of methods for issuers to raise funds from a broad range of investors in both the public and the private markets.

While it is important for securities regulators to mandate effective standards to protect investors and foster efficiency in private markets, we are also seeing the development of innovative mechanisms to address the concerns traditionally dealt with by detailed regulatory requirements.

For instance:

- 1) Crowdfunding sites and other internet-based matching systems are emerging around the world -- and are requiring regulators to respond.
- 2) Exchanges are entering the private market space by offering secure portals for approved issuers and investors to find information and opportunities to match buyers and sellers. I refer to initiatives like TSX Private Markets, the proposed Aequitas private market platform, and the Nasdaq Private Market in the US.
- 3) Dealers are offering online access to exempt offerings posted by private companies that can be accessed directly by qualified investors.
- 4) Seeing opportunities on both the supply and demand side, intermediaries, including PCMA's members, are offering an increasing range of products in the private markets. As the market becomes more competitive, dealers are becoming more efficient at identifying and bringing together clients on both the buy and sell sides.

These developments are creating ways to raise capital faster, more efficiently and at lower cost – not to mention the private market can provide capital to businesses that can't get it from other sources. Regulators need to respond to these developments – so we have.

When you combine new technological capabilities to support capital raising, new private sector initiatives to match buyers and sellers, and our new regulatory proposals, I think we're on the cusp of a major change in the structure and performance of our capital markets.

### **Role of the regulatory system**

The efficiency of capital formation is primarily a function of the capital needs of companies creating investment opportunities, investor demand at varying levels of risk, and the process that matches the two. Our goal is to enable efficient means of matching buyers and sellers of capital and at the same time to protect investors by promoting capital markets that are fair and honest. That means:

- Relevant facts are fully disclosed and accessible to investors.
- Risks are understood and accepted by investors.
- Fraud, misrepresentations and abuses are prevented.

We recognize that investors have different risk appetites, levels of sophistication and ability to withstand loss. We therefore need to create a regulatory framework for the exempt market that balances the interests of those investors that are willing, and able, to make high risk investments with the risks to those for whom such investments would be inappropriate.

Obviously, this is a difficult balance to achieve, but one that is essential to ensure that the needs of both companies and investors are met.

The bottom line is we have to get it right. We cannot afford changes that backfire, and lead to unsuspecting people suffering major losses. People who didn't understand the risks, and were never advised of them.

I believe that means our interests must be aligned with yours as we work towards implementing these changes. As the new tools to develop and access private markets become available, we need to be prudent in introducing them. As private market dealers, you have strong incentives to make the new system work well. But not only that – you have a responsibility to make it work well.

We all know there are weaknesses in financial knowledge among many investors in Canada. At the same time, the OSC's compliance examinations have shown that procedures to address KYC and suitability of investments

must to be strengthened at some dealers who participate in the private markets. In fact our 2012 sweep found that a majority of EMDs needed to improve their KYC procedures, and suitability assessments were inadequate at approximately 25% of the dealers.

Dealers have also sold product to investors who did not qualify for any prospectus exemption. To assist dealers in addressing these issues, in January the CSA issued guidance on KYC, KYP and suitability obligations. Those obligations are central to the duty to deal fairly and honestly with your clients.

All of that means that the OSC plans to deliver sound supervision of the new private market mechanisms and the use of the new exemptions. We are currently working on oversight procedures in anticipation of finalizing our rule proposals. Those procedures will include review of filings on exempt offers, random sampling of disclosures and continued inspections of dealers. We will focus on the compliance issues identified as concerns. We don't want anyone to ask later, "Where were the regulators?" Confidence and trust in the private markets is critical.

**Let me address a couple of the issues that the PCMA and others are raising about the rule proposals.**

First, people are asking for the CSA to fully harmonize the rules across Canada, particularly on the OM exemption. That makes sense, and we are striving for the highest possible degree of uniformity and consistency.

But as you know institutional and regional structures can make this process more difficult. Our proposal does contain a number of restrictions, which the Commission felt was needed. The comment period closes on June 18, 2014 and it is our duty to review and consider all comments received.

That leads me directly to the second issue: the proposed limits on the size of investments made by retail investors using crowdfunding and the OM exemption, as well as limits on the amounts raised by issuers. Many industry comments are advocating that the limits be removed or raised substantially. As I indicated earlier we must achieve a balanced approach. As such the specific amounts of the limits and other matters will be considered after the comment period closes.

## **Where do we go from here?**

As indicated, our proposals are out for comment until June 18. We've already received a large number of comments, so clearly the proposals have sparked lots of interest.

Over the summer OSC staff will review the comments and propose any changes to the rule proposals that we consider appropriate. The Commission then aims to finalize the rules, and to implement them in the first quarter of 2015. That is our goal.

The landscape in this industry will be significantly different next year. I believe that a powerful combination of regulatory reforms, technological tools and market initiatives are about to bring important changes to our markets, especially for small companies, entrepreneurs and investors who are comfortable with the risk involved in participating in new ideas. This is an exciting time to be involved in private markets, whether as a buyer, seller, intermediary or regulator. We must all work together to realize the great potential of these changes in a way that is positive for all participants.

Thank you and enjoy your conference.