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June 18, 2014

Via email to comments@osc.gov.on.ca;
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Autorité des marchés financiers
British Columbia Securities Commission
Financial and Consumer Affairs Authority of Saskatchewan
Financial and Consumer Services Commission (New Brunswick)
Manitoba Securities Commission
Nova Scotia Securities Commission
Ontario Securities Commission
Securities Commission of Newfoundland and Labrador
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island
Superintendent of Securities, Northwest Territories
Superintendent of Securities, Nunavut
Superintendent of Securities, Yukon

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Re: Comments on the Ontario Securities Commission's proposed amendments to National Instrument 45-106 *Prospectus and Registration Exemptions*, and on its proposed Multilateral Instrument 45-108 *Crowdfunding* and Companion Policy 45-108CP *Crowdfunding*, published March 20, 2014

Dear Sirs/Mesdames:

AUM Law is a corporate and securities law firm providing regulatory compliance, fund formation, corporate finance and corporate secretarial services. Our approach is to deliver the most practical, forward-thinking advice and services to our clients, who primarily consist of portfolio managers, investment dealers, hedge funds, and private and public companies.

Our comments represent the views of Erez Blumberger, Pierre-Yves Châtillon, Soma Choudhury, Ron Kugan and Adam Braun, who are lawyers at AUM Law, and are submitted without prejudice to any position that has or may in the future be taken by AUM Law on its behalf or on behalf of its clients.

Unless otherwise defined, capitalized terms used in this letter have the same meaning as in the above-captioned proposals.

A. Proposed OM Prospectus Exemption and the FFBA Prospectus Exemption

Please Harmonize

We appreciate the policy rationale underlying the proposed OM Prospectus Exemption and FFBA Prospectus Exemption in Ontario. However, in our respectful view, the failure to fully harmonize these proposals with the existing OM Prospectus Exemption and FFBA Prospectus Exemption available in other CSA jurisdictions serves to diminish the potential capital-raising benefits of these proposed exempt distribution channels.

Certainly, the CSA framework has inherent harmonization challenges, which we appreciate. But we cannot overstate the import of a uniform set of exemptions. In our view, lack of harmonization, particularly vis-à-vis the OM exemption, will result in inadvertent non-compliance by SMEs and dealers distributing their product. Conversely, harmonization will result in ease of application of the OM exemption, reduction of legal and (non-) compliance costs, and reduction of the resulting cost of capital for SMEs.

Why Exclude Investment Funds?

While the existing OM Prospectus Exemption is available to all investment funds in certain jurisdictions like British Columbia, the existing exemption may only be relied upon by non-redeemable investment funds and prospectus mutual funds in certain other jurisdictions, like Alberta. By excluding all types of investment funds, the proposed OM Prospectus Exemption in Ontario increases the divide among the exemptions across various jurisdictions. This lack of harmonization is particularly troubling in light of the somewhat ambiguous rationale underlying the exclusion of investment funds in Ontario.

Additionally, the OSC plans to recommend repealing the current section 2.7, *Founder, control person and family exemption*, which is currently available to investment funds in Ontario. To repeal section 2.7 without allowing investment funds to avail themselves of the new proposed exemptions would unjustifiably restrict investment funds from accessing the exempt market in Ontario. Relatively speaking, it is likely to be far less risky for investors to invest in a portfolio offered by an investment fund that includes SMEs than to invest directly in start-ups and SMEs.

Moreover, the exclusion of investment funds from the proposed exemptions continues to put small to mid-size investment fund managers at a significant disadvantage in the Ontario market.

In our view, as long as investors understand the risks of investing, and registrants ensure that know-your-client, know-your-product and suitability obligations are being met, there is no

reason for a particular exemption to be available to a segment of investors in one CSA jurisdiction and unavailable in another.

Our Recommendation

We respectfully submit that the proposals be fully harmonized with the existing OM Prospectus Exemption and FFBA Prospectus Exemption available in other CSA jurisdictions.

We respectfully submit that issuers, intermediaries, and investors would be better served if both the proposed OM Prospectus Exemption and the FFBA Prospectus Exemption were made available to investment funds in Ontario, provided that:

- investors have read and acknowledged the risks of investing by executing a risk acknowledgment form; and
- know-your-client, know-your-product and suitability obligations are fulfilled.

Existing Securityholder Exemption

Unlike the current Existing Securityholder Exemption, which has been available to investment funds since March 13, 2014 in most CSA jurisdictions (pursuant to Multilateral CSA Notice 45-313 *Prospectus Exemption for Distributions to Existing Securityholders*), the proposed Existing Securityholder Exemption will not be made available to investment funds in Ontario. The policy rationale in the 45-313 CSA Jurisdictions is to facilitate capital raising for listed issuers, and to promote fairness by giving investors who do not meet the criteria under other capital-raising exemptions the opportunity to participate in private placements.

This opportunity should be equally applicable to all listed issuers in Ontario regardless of whether they are investment funds. Instead, this exclusion disproportionately prejudices closed-end funds that are listed issuers vis-à-vis other listed issuers in Ontario from capital raising in the exempt market. Public closed-end funds provide timely disclosure, similar to other listed issuers. In the absence of the proposed exemption, closed-end funds will need to rely upon a rights offering or a secondary market offering to raise capital in Ontario, at a much greater expense and time than other listed issuers.

Further, given that under the proposed Existing Securityholder Exemption, (i) registrants will need to meet know-your-client, know-your-product and suitability obligations, and (ii) an investor can only invest a maximum of $15,000 per issuer in a 12-month period, appropriate investor protection rationales will be met even if this proposed prospectus exemption is made available to closed-end funds that are listed issuers in Ontario. In our respectful submission, the Ontario market is not so different from the 45-313 CSA jurisdictions to justify such a radically distinctive approach of excluding investment funds from relying on this exemption.

Our Recommendation

We suggest that the same rationale for capital raising and investor protection apply equally to all listed issuers including closed-end funds. Accordingly, we recommend that the proposed existing Securityholder Exemption in Ontario be harmonized with the exemption currently available in the 45-313 CSA Jurisdictions.

B. Reporting Requirements

Pursuant to the proposed amendments, investment funds will be required to use a combination of different reporting forms, depending on the prospectus exemption relied upon for distribution in a particular jurisdiction. For example,

- Form 45-106F1 will be required in all jurisdictions except Alberta, British Columbia, New Brunswick, Ontario and Saskatchewan;
- Form 45-106F6 will be required in British Columbia; and
- Form 45-106F10 will be required in Alberta, New Brunswick, Ontario and Saskatchewan.

Investment funds could therefore be required to complete and file concurrently *three separate forms with different information requirements*. In addition, in Ontario, the filing of the required form of report must be done via an electronic portal, whereas most other jurisdictions require paper form reporting.

Furthermore, in Alberta, New Brunswick, Ontario and Saskatchewan, investment funds that currently file reports annually within 30 days of the financial year-end of the investment fund will be required to make quarterly filings.

In our respectful submission, the regulatory burden (particularly for smaller fund managers) of more frequent quarterly reporting does not justify the theoretical additional benefit to the capital markets arising from the CSA obtaining the data more quickly. Quarterly reporting simply increases registrants' reporting and financial burden, and risk of non-compliance.

Our Recommendation

As the original purpose of annual reporting was to remove the frequency of the filing burden on investment funds due to the frequency of subscriptions and redemptions characterizing these funds, we recommend that the CSA retain its annual reporting regime for investment funds. Additionally, we seek clarification as to whether each quarterly filing will result in increased fees.

At a minimum, if more frequent reporting is absolutely necessary then we recommend that the CSA harmonize the form and timing of reporting exempt trades across all CSA jurisdictions. Alternatively, investment funds should be made to file their reports only with the principal regulator, in one format.

C. Crowdfunding Prospectus Exemption and Crowdfunding Portal Requirements

We are pleased to provide members of the CSA with certain specific comments on MI 45-108 and CP 45-108.

i. Harmonized Crowdfunding and Start-Up Exemptions

Our primary concern is that the CSA will implement the Proposed Exemptions inconsistently, resulting in further increases to the compliance cost and burden for issuers, while depriving investors in certain jurisdictions from lower-cost investment opportunities.

This is particularly true with the Proposed Exemptions because they are based on the ease and wide availability of Internet access. The Internet is not a medium that can be easily divided and restricted by jurisdiction. Under the Crowdfunding Exemption, a portal must be registered as a "restricted dealer" in every jurisdiction where it will potentially distribute securities of issuers. Since portals will be exempted from the "know-your-client" obligation, we are concerned that prospective purchasers resident in non-participating jurisdictions will be able to misrepresent their residency on a portal website, since no proof of residency would be required.

MI 45-108 does appear to provide guidance for portals on how they should police their users to ensure that only residents in jurisdictions that have adopted the Crowdfunding Exemption can participate in a distribution.

Our Recommendation

Inconsistent adoption of the Proposed Exemptions would be a serious setback to the efforts of the CSA to reduce interprovincial barriers to greater capital markets efficiency. Notwithstanding the inherent jurisdiction of the CSA members to make local rules and policies, we urge the CSA to consider harmonizing the Proposed Exemptions across all CSA jurisdictions to create a level playing field for investors and issuers.

Additionally, guidance or a safe-harbour should be provided for portals to address potential for misrepresentation of residency on portal websites and ensure that only residents can participate in a distribution.

ii. Harmonized Report of Exempt Distribution

As discussed in our comments to the amendments to NI 45-106 above, under MI 45-108, issuers will also be required to use a combination of different reporting forms, depending on the particular jurisdictions in which a distribution is made under the Crowdfunding exemption. Under the proposed instrument, issuers will be required to use the following required forms of report, depending on the jurisdictions of distribution:

- Form 45-106F11 in Saskatchewan, Ontario and New Brunswick, and
- Form 45-106F1 in Manitoba, Nova Scotia and Québec.

If the BCSC adopts a similar regime, it may also require issuers to file Form 45-106F6. Issuers could therefore be required to complete and file concurrently *three separate forms with different information requirements*. In addition, the filing in Ontario of the required form of report will presumably be done via an electronic portal, while other jurisdictions may require paper form of reporting.

The enhancement of the CSA members' understanding of exempt market activity through the proposed reporting requirements should not add to SME issuers' regulatory burden and compliance costs. This would be contrary to the purpose of the Proposed Exemptions, which are intended to reduce this load.

Our Recommendation

A key objective of the CSA is its ability to harmonize securities legislation across Canada to lessen the burdens of issuers and registrants dealing with the provincial regulatory authorities. We do not see this objective being met with the requirement to file multiple reports through inconsistent means. We respectfully submit that harmonization of reporting requirements should be a priority of the CSA.

Alternatively, we would suggest that until all jurisdictions have harmonized their reporting requirements, issuers and portals should only be required to file with their principal regulator.

iii. Offering Limit

We have concerns about the proposed offering parameters of the Crowdfunding Exemption. Specifically, notwithstanding the policy focus on SMEs, we are concerned that an arbitrary offering limit of $1.5 million per 12-month period is overly restrictive in light of the other proposed investor protection measures.

Imposing an offering limit may lead to perverse effects. It may influence issuers to develop written business plans as a way to fit within the offering limit, rather than develop business plans based on sound economic and business factors. An offering limit may also hinder issuers' ability to react in a timely manner to available business opportunities, if there is no room for them under the offering limit. This could have the effect of requiring such issuers to avail themselves of other more time-consuming and expensive prospectus exemptions, while not necessarily providing additional disclosure to prospective investors. The end result is that the Crowdfunding Exemption may have a very limited appeal to issuers for whom the $1.5 million limit is not a sufficient solution to their funding gap.

Our Recommendation

It is not clear that investor protection would be enhanced by an issuer offering limit, especially at the proposed amount. We respectfully submit that the proposed investment limit, disclosure requirements and restriction of type of securities that could be offered, and the statutory or contractual rights that would be available to investors, more than adequately address investor protection concerns.

Alternatively, we recommend that the CSA up the offering limit in line with the $3 million cap that existed as part of the now repealed closely-held issuer exemption in Ontario.

iv. Enforcement of Investment Limits

We submit that the proposed investment limits may make it overly difficult for portal operators to ensure compliance with the proposed investment limits. For example, an investor may choose to invest additional amounts in a single issuer through other family members or personal holding companies. There is no proposed guidance as to the measures portals should take to ensure investors do not breach the proposed investment limits.

Further, an investor may invest more than $10,000 in a single calendar year by investing through multiple portals.

We also note that the proposed investment limits appears to be arbitrarily low, given that the Investor Survey indicated that only 20% of those surveyed would consider an investment of $5,000 or more in an offering.

Additionally, we would suggest that consideration be given to balancing the convenience of a uniform limit with the fact that investors with higher incomes or net worth may have higher risk tolerances. The proposed investment limits would restrict diversification through the Crowdfunding Exemption to four SME issuers in a calendar year. For certain investors, this could prevent prudent diversification of their overall portfolios.

Our Recommendation

Notwithstanding the requirement to educate portal investors on the investment limits, we respectfully submit that further guidance should be provided to portal operators on the standard to which they would be held accountable for enforcing the proposed investment limits and on the measures they would be expected to implement.

We also think that even if the proposed investment limits are deemed necessary, greater efficiency would be achieved with fixed limits, rather than periodically adjusted limits to account for inflation. As has been observed in the proposed amendments to National Instrument 45-106, fixed dollar amounts will become more or less restrictive over time, and those relying on dollar-based exemptions will be left waiting for a regulatory response. Such a regulatory model is both inefficient and unfair to market participants.

Lastly, we recommend guidance or a safe-harbour to address the steps that would be viewed as adequate with respect to the limits set out in the exemption.

v. Ongoing Disclosure

As a result of the ongoing disclosure requirements being proposed, the Crowdfunding Exemption would entail significantly higher compliance costs for non-reporting issuers. In light of the offering and investment limits, some SME issuers may view the Crowdfunding Exemption as an unappealing option, as they would have to assume the cost of audited financial statements if the relatively low thresholds in MI 45-108 are exceeded – defeating the purpose of having an alternative exemption.

Our Recommendation

We believe the requirement for audited financial statements should remain applicable to reporting issuers only. We respectfully submit that such a requirement should not be included in MI 45-108. Unaudited or review-level financial statements that are prepared and delivered to shareholders in accordance with applicable corporate law should be sufficient.

vi. Investor Education and Screening

We agree with the requirement to provide prospective investors with prescribed issuer disclosure and risk acknowledgement. However, the screening of investors to ensure that they understand the nature of their investment places an unfair burden on portals and SME issuers in light of the other investor protection measures. Moreover, we believe it would be difficult to ensure that the investor education and screening is meaningful or genuine thereby further calling into question the utility of this obligation. For example, a prospective portal investor could rely on someone else to complete an online quiz.

Our Recommendation

We respectfully submit that the requirement to provide prospective investors with prescribed issuer disclosure and risk acknowledgement is sufficient as a way to ensure that investors have an understanding of the investment proposition.

Alternatively, we believe further guidance or a safe-harbour should be provided to ensure that the investor education and screening process is genuine.

vii. Prohibition on Portal Dual Registration

While we recognize the regulatory concern underpinning the proposal that portals not be dual-registered, we respectfully submit that the potential mischief should be addressed by other means, such as through conflict of interest policies, procedures and disclosure. It is unclear to us why dual registration could necessarily lead to the misuse of portals for distributions under exemptions other than the Proposed Exemptions.

We realize that a currently registered dealer could create an affiliate entity that may register as a restricted dealer, in order to operate a portal and request exemptive relief from section 4.1 of National Instrument 31-103 to allow dealing representatives to work for both firms. But this is an unnecessary hurdle and cost for firms.

Our Recommendation

We contend that firms that are already registered may be better equipped to develop and administer the compliance systems necessary to operate a portal as a distinct line of business. We submit, as an alternative, that registered dealers that wish to operate a portal should be permitted to register as a "restricted dealer" and receive terms and conditions that would include an exemption from the provisions of National Instrument 31-103 listed at section 29(1) of MI 45-108 in the course of operating their portal when dealing with the Crowdfunding exemption. We believe that a firm could maintain appropriate books and records to demonstrate it is meeting its obligations under both business lines, and should not need to create a separate entity to act as an artificial barrier.

viii. Lack of Clarity on Proficiency Requirements

A dealing representative for a portal has no specific proficiency requirement, except for a requirement that the individual has the "education, training and experience that a reasonable person would consider necessary to perform the activity competently, including understanding the structure, features and risks of each security distributed."

Our Recommendation

Further guidance should be provided to portal operators about the education, training and experience required for an individual or firm to be appropriately registered. Uncertainty about what proficiency requirements would be satisfactory will inevitably lead to unnecessary complexity, uncertainty and delays for both the regulators and registrants.

ix. Prohibition on Real Estate Issuers That Are Not Reporting Issuers

We respectfully disagree with the exclusion from the Crowdfunding Exemption of real estate issuers that are not reporting issuers. SMEs that wish to operate a business that primarily invests in or develops real estate, or derives its revenues primarily from investments in real estate, have the same capital concerns and considerations as issuers in other industries. We are troubled by this distinction concerning real estate. The exclusion of real estate appears to presume, without apparent justification, that this industry is more speculative and risky than other industries. As with the offering limit, the investment limits and disclosure requirements already impose significant limitations on the harm that could be caused to prospective investors.

Our Recommendation

We agree in general that issuers whose business is primarily conducted in certain industries should be subject to enhanced disclosure. But we submit that the exclusion of real estate is overly restrictive. The exclusion also has not been explained. We respectfully suggest that consideration should be given to whether the business plan requirement should be tailored to real estate issuers so they can access the Proposed Exemptions.

x. Marketing Restriction for Issuers and Portals

We are generally supportive of placing reasonable restrictions on advertising and promotion by portals and the issuers relying on the Crowdfunding Exemption. We do have concerns about the practical realities that confront issuers in raising awareness of proposed distributions. Generally, we believe that there is no harm in advertising the fact that an issuer is making an offering, along with the location where potential purchasers may access information about the offering and the relevant documents.

In our view, it would be helpful for MI 45-108 to provide greater clarity about where and how to promote the fact that an issuer is undertaking a Crowdfunding Exemption offering. We note that while subsection 18(3) of MI 45-108 allows for advertising, the relevant section of CP 45-108 refers only to advising potential purchasers of the Crowdfunding Exemption offering. One reading of the relevant companion policy provision is that the advertising has to be direct rather than general in nature. The reference in CP 45-108 to "potential purchasers, including the issuer's customers and clients" may also suggest targeted notice rather than general notice, such as with a news release.

Guidance should also be provided as to what, if anything, issuers and portals should do regarding general discussion or promotion of a Crowdfunding Exemption in the media or by persons not associated with the portal or issuer. For example, can an issuer respond to media enquiries or discussions regarding is offering? Should an issuer take steps to restrain unaffiliated persons

who post its offering documents on websites other than the portal? The Internet is difficult to police. Should there be some degree of recognition that documents made available on a website may be disseminated widely – against the issuer's intentions?

Our Recommendation

In our view, it would be helpful for MI 45-108 to provide greater clarity about where and how to promote the fact that an issuer is undertaking a Crowdfunding Exemption offering.

Thank you for this opportunity to provide comments. Please do not hesitate to contact me if you have any questions.

Sincerely,

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