

Crowdfunding For Securities Offerings Comes to Ontario (Finally!)



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Beginning on January 25, 2016 Multilateral Instrument 45-108 (“MI 45-108”) will enable corporations and other entities to sell their securities in Ontario via online equity ‘crowdfunding’. Ontario’s new equity crowdfunding prospectus exemption (the “**Crowdfunding Exemption**”) is designed to facilitate online capital-raising from a large number of investors through an Internet funding portal which is registered with securities regulatory authorities. The following Q&A explains key aspects of the new crowdfunding regime.

Q: Who can use the Crowdfunding Exemption?

The Crowdfunding Exemption may be used only by an issuer incorporated or organized in Canada, the head office of which is located in Canada, and a majority of the directors of which are resident in Canada. If the issuer has a principal operating subsidiary, that subsidiary must be incorporated or organized in Canada or in the U.S. The Crowdfunding Exemption is available for both reporting issuers and non-reporting issuers however it is not available for investment funds, if the issuer would use the proceeds to invest in, merge with or acquire a business which is not specified at the time of the crowdfunding offering, for issuers who are not in compliance with certain securities

law requirements, or for issuers who already have an active crowdfunding offering underway.

Q: What Kinds of Securities May be Sold Using the Crowdfunding Exemption?

Only common shares, non-convertible preference shares, securities convertible into common shares or non-convertible preference shares, non-convertible debt securities linked to fixed or floating interest rates, units of a limited partnership or flow-through shares may be sold under the Crowdfunding Exemption.

Q: How Much Can an Entity Raise Using the Crowdfunding Exemption?

An issuer may raise up to \$1,500,000 in any 12 month period under the

Crowdfunding Exemption.

Q: How Long May a Crowdfunding Offering Take?

A crowdfunding offering may remain open for no more than 90 days and closing must occur within 30 days of the end of the offering.

Q: Are there Investor Limits Under the Crowdfunding Exemption?

Yes, purchasers who are not 'accredited investors' cannot invest more than \$2,500 in any single crowdfunding offering nor more than \$10,000 in any number of crowdfunding offerings in any calendar year. An 'accredited investor' who is not a 'permitted client' may not invest more than \$25,000 in any one crowdfunding offering nor more than \$50,000 in any number of crowdfunding offerings in any calendar year. A 'permitted client', which includes among other things certain institutional investors and individual investors whose net financial assets exceed \$5 million, may invest an unlimited amount under the Crowdfunding Exemption.

Q: What Kind of Information Must Be Provided by the Issuer to Crowdfunding Investors?

An issuer which uses the Crowdfunding Exemption must provide investors, via the online portal, with a crowdfunding offering document in a prescribed form which includes certain detailed information relating to the issuer and the securities being issued. If the issuer is a reporting issuer it must attach to the crowdfunding offering

document its most recent annual audited and interim unaudited financial statements. If the issuer is a non-reporting issuer it must attach to the crowdfunding offering document its most recent annual financial statements which must be accompanied by a review report or an audit report if the issuer has raised between \$250,000 and \$750,000 and by an audit report if the issuer has raised \$750,000 or more under any prospectus exemptions from the date of its formation to the date which is not less than 90 days before the date of the crowdfunding offering document. Investors will have certain rights to rescind or sue for damages if there is a misrepresentation in the information provided in the crowdfunding offering document. The issuer may also make available to investors, via the online portal, a term sheet, a video and other materials summarizing the information in the crowdfunding offering document. The crowdfunding offering document including the financials and, if applicable, the term sheet and other materials summarizing the information in the crowdfunding offering document must be filed with the Ontario Securities Commission within 10 days of closing the crowdfunding offering and will be publicly accessible via the SEDAR web site.

Q: Will Investors Be Required to Sign a Risk Acknowledgment Form?

Yes, investors will be required to complete and sign a form 45-

108F2 Risk Acknowledgement which describes certain risks associated with investing under the Crowdfunding Exemption. Investors must also complete a schedule to confirm their investment limits.

Q: Can an Issuer Advertise their Crowdfunding Offering?

No, issuers may not directly or indirectly advertise their crowdfunding offering however an issuer can inform purchasers that it intends to conduct a crowdfunding offering and can direct purchasers to the online portal through which the crowdfunding offering will be conducted.

Q: What is the Role of the Portal?

A crowdfunding offering may only be conducted through a single online portal which will host all of the issuer's disclosure documents, the subscription agreement, risk acknowledgment form and confirmation of investment limits form. Closing of the crowdfunding offering, including payment for the securities purchased, is effected through the portal acting as agent for the issuer. The portal is required to conduct certain due diligence on the issuer including obtaining personal information forms from, and conducting criminal record and background checks on, each director, executive officer and promoter of the issuer and must also conduct background checks on the issuer. A portal is also required to review the issuer's crowdfunding offering document and its other marketing materials and is required to deny an issuer access to the portal if the portal determines that

the business of the issuer may not be conducted with integrity, the issuer is not complying with the crowdfunding legislation, if the crowdfunding offering document or other marketing materials include a misrepresentation which the issuer has not corrected or if the issuer or any of its directors, executive officers or promoters has been guilty of an offence or has entered into a settlement agreement in a matter that involved fraud or securities violations. Portals are prohibited from advertising or soliciting purchasers for a crowdfunding offering and must ensure that information about the issuer and the crowdfunding offering are presented on the portal in a fair, balanced and reasonable manner.

Q: Are there Ongoing Obligations Triggered by Using the Crowdfunding Exemption?

Yes, entities which are not reporting issuers and which use the Crowdfunding Exemption are required to provide investors with annual financial statements which must be accompanied by a review report or an audit report if the issuer has raised between \$250,000 and \$750,000 and by an audit report if the issuer has raised \$750,000 or more under any prospectus exemptions from the date of its formation to the end of its most recent financial year. Reporting issuers and non-reporting issuers which use the Crowdfunding Exemption must also include with their annual financials a notice that describes

how the funds raised under the Crowdfunding Exemption have been used. The annual financials and the use-of-funds notice will be publicly accessible via the SEDAR web site. Non-reporting issuers which have used the Crowdfunding Exemption must also notify investors within 10 days of a discontinuation of the entity's business, a change in the entity's industry, and a change of control of the entity. The requirement to provide aforementioned financial statements and additional notifications continues until the issuer becomes a reporting issuer, the issuer has completed a windup or dissolution, or the securities of the issuer are beneficially owned by fewer than 51 security holders, whichever occurs first.

Q: Is the Ontario Crowdfunding Exemption the Same as Crowdfunding Prospectus Exemptions in Other Canadian Jurisdictions?

No. Among the provinces which have approved MI 45-108 (Manitoba, Ontario, Quebec, New Brunswick, Nova Scotia) Ontario has imposed some additional annual aggregate investment limits and Ontario, New Brunswick and Nova Scotia have imposed notice requirements for certain corporate events which are not required in other provinces. Also, in May, 2015 British Columbia, Saskatchewan, Manitoba, Quebec, New Brunswick and Nova Scotia (but not Ontario) implemented separate 'start-up crowdfunding' exemptions which are available for non-reporting

issuers only and which include, among other things, lower investor limits and lower amounts that issuers can raise than those under MI 45-108, no requirement for the provision of financial statements and no registration requirement for the portal. These start-up crowdfunding exemptions will continue in those jurisdictions following the implementation of MI 45-108 however there is no present intention to implement the start-up crowdfunding exemptions in Ontario. British Columbia has implemented the start-up crowdfunding exemptions but has not approved MI 45-108 and Alberta has not approved nor has it implemented the start-up crowdfunding exemptions or MI 45-108.

Commentary

The Crowdfunding Exemption can profoundly expand an early stage entity's fundraising opportunities by allowing access to any member of the public via the online world. However investor protections in the form of registered portals and costs of using them, requirements for non-reporting issuers to prepare audited annual financials, and the impact on start-ups of having to manage potentially hundreds of shareholders could inhibit some early stage entities from taking advantage of the Crowdfunding Exemption.

For more information about this topic or matters relating to corporate finance, please call me.