

September 9, 2016

To: Alberta Securities Commission  
Superintendent of Securities, Nunavut

C/O: Jessie Gill  
Legal Counsel, Corporate Finance  
Alberta Securities Commission  
Suite 600, 250 – 5th Street SW  
Calgary, AB, T2P 0R4  
Fax : 514-864-6381  
E-mail: Jessie.gill@asc.ca

**Re: Response to Proposed Adoption of Multilateral Instrument 45-108 Crowdfunding Exemption in Alberta**

Dear Sirs and Madams,

Please accept this letter as our response on behalf of the National Crowdfunding Association of Canada (“**NCFA Canada**”) with respect to the **Request for Comments on the Proposed Adoption of Multilateral Instrument 45-108 Crowdfunding Exemption in Alberta** (the “**Integrated Crowdfunding Exemption**”), as released on July 26, 2016.

We are pleased the Alberta Securities Commission is considering joining the other provinces who have already adopted the Integrated Crowdfunding Exemption. NCFA Canada and its members also thank the Alberta Securities Commission for the opportunity to participate in the consultation process.

NCFA Canada is a cross-Canada non-profit actively engaged with both social and investment crowdfunding stakeholders across the country. NCFA Canada provides education, research, leadership, support and networking opportunities to over 1300+ members and works closely with industry, government, academia, community, and eco-system partners and affiliates, to create a strong and vibrant crowdfunding industry in Canada.

We support innovation, small businesses and entrepreneurs seeking to make a difference, and believe that crowdfunding markets and the eco-systems around them can play a significant role in mobilizing start-up capital and resources to early stage projects and businesses in an efficient and cost effective manner.

More detailed information about our organization is attached as a schedule to this response letter.

## **Our Comments on Adoption of the Integrated Crowdfunding Exemption**

### ***General***

We support the adoption of the Integrated Crowdfunding Exemption in Alberta. It is our opinion, however, that the Alberta Securities Commission should be adopting the Saskatchewan and Manitoba version of the Integrated Crowdfunding Exemption and not the Ontario version of the exemption.

The Integrated Crowdfunding Exemption came into effect January 25, 2016 in the provinces of Manitoba, Nova Scotia, New Brunswick, Ontario, and Quebec. It will come into effect in Saskatchewan on ministerial approval which has not yet been obtained. Alberta will be the seventh jurisdiction in Canada to adopt the Integrated Crowdfunding Exemption.

It is our opinion that the harmonization of the capital-raising exemptions in Canada should be a top priority of all Canadian securities regulators. Ideally, the Integrated Crowdfunding Exemption and the Start-Up Crowdfunding Exemption, as set-out in Multi-lateral CSA Notice 45-316, should be available to issuers in every province and territory in Canada. The requirements and application of both these exemptions should also be identical and not have nuanced differences as they do now.

### ***Slow Start to Use of Canadian Crowdfunding Specific Exemptions***

As of today's date, no portal has registered under the Integrated Crowdfunding Exemption. We are also unaware of any registered dealers who have amended their registration to include sales under the Integrated Crowdfunding Exemption through a portal. As a result, no issuers have conducted a financing using the Integrated Crowdfunding Exemption in Canada since it became effective in January 2016.

The Start-Up Crowdfunding Exemption, available in British Columbia, Manitoba, New Brunswick, Nova Scotia, Quebec and Saskatchewan, has also had a slow start in Canada but is starting to gain traction. There are now eight portals registered under the Start-Up Crowdfunding Exemption and one exempt market dealer who is registered to include sales under this exemption through their portal. Issuers have closed financing on a number of these portals in British Columbia and Quebec.

There are also eight funding portals run by exempt market dealers and one portal registered as a restricted dealer utilizing the accredited investor and offering memorandum exemption. These portals have been more active in closing financings than the portals utilizing the Start-Up Crowdfunding Exemption.

In the United States Title III Crowdfunding rules became effective May 16, 2016. [Fifteen portals have registered](#) under the exemption and [ninety-nine issuers](#) have launched crowdfunding campaigns under the exemption. As of July 18, 2016, [35 states have approved an intrastate crowdfunding exemption](#). Portals have registered across the United States under these various intrastate exemptions. [Texas](#) alone has over ten portals registered under its intrastate crowdfunding exemption and portal rules. Over one-hundred and sixty-six issuers have launched crowdfunding campaigns utilizing these various intrastate crowdfunding exemptions. The Title III Crowdfunding rules and the various intrastate crowdfunding rules are similar to the Integrated Crowdfunding Exemption but vary in ways that has made these rules more attractive to portal operators and issuers.

Although we are disappointed the Integrated Crowdfunding Exemption has not been utilized, we believe it is too early to determine whether the Integrated Crowdfunding Exemption is of no interest to private or public issuers who may rely on this exemption to issue securities.

Other jurisdictions such as the UK, Europe and the US also had a slow start to the use of their funding portals. The use of these portals however have doubled or tripled year after year over the past four years in these jurisdictions. We expect a similar evolution of the use of funding portals will occur in Canada as investors and issuers become aware of and educated about this form of raising capital and investing, and the rules are adjusted to fall more in line with those in other jurisdictions.

***Suggestions for Improvements to the Integrated Crowdfunding Exemption***

We provide the following suggestions and comments for the purpose of encouraging you and other regulators in the participating jurisdictions to discuss how the Integrated Crowdfunding Exemption can be revised to be more palatable to potential portal operators and private small and medium enterprises (SMEs). We certainly do not want to encourage the Alberta Securities Commission to adopt its own twists to the Integrated Crowdfunding Exemption at this time. The majority of the suggested changes below are for future consideration.

**Too Many Subtle Variations in to the Integrated Crowdfunding Exemption**

One of the perceived issues of the Integrated Crowdfunding Exemption concerns the variations of the exemption adopted in different participating jurisdictions. A securities exemption that is identical in every jurisdiction across Canada is the ideal that Canadian securities regulators should actively pursue as a goal any time a new rule is adopted. The feedback we have received is that issuers and their advisors believe the Integrated Crowdfunding Exemption has too many variations from jurisdiction to jurisdiction which makes the rule difficult to understand and use. The chart below sets-out the main differences.

<b>Jurisdictional Differences in MI 45-108 Crowdfunding</b>						
	<b>Ontario</b>	<b>New Brunswick</b>	<b>Nova Scotia</b>	<b>Manitoba</b>	<b>Saskatchewan</b>	<b>Quebec</b>
<b>Investment Limits</b>  Non-accredited investors have a cap of \$2,500 per distribution.  Accredited investors have a cap of \$25,000 per distribution.	Non-accredited investors capped at \$10,000 per year for all CF investments.	No aggregate cap for CF investments per year.				
	Accredited investors capped at \$50,000 per year for all CF investments, unless permitted					

<b>Jurisdictional Differences in MI 45-108 Crowdfunding</b>						
	<b>Ontario</b>	<b>New Brunswick</b>	<b>Nova Scotia</b>	<b>Manitoba</b>	<b>Saskatchewan</b>	<b>Quebec</b>
	client. No limits apply to permitted client.					
<b>Document Requirements</b>	Confirmation of investment limit Form 45-108F3 from investors required.	No investment limit form required.				
	No accredited investor confirmation or validation required, but portal required to obtain additional information to determine if investor meets accredited or permitted client definition.	Accredited investor confirmation and validation if investing over \$2,500.				
	Offering documents considered an offering memorandum with rights available under s. 130.1 of ON securities act.	N/A	Offering documents considered an offering memorandum with rights available under s. 138 of NS securities act.	N/A	N/A	Offering documents and material considered authorized in lieu of prospectus with rights of action in s. 217 to 221 of QU securities act.
	No direction regarding language.					Documents must be in French only or in French and English.
<b>Ongoing Disclosure Obligations</b>	Notice of specified key events if a non-reporting issuer.			No key event notice.		
<b>Portal</b>	A restricted dealer funding portal must not be an affiliate of another registered dealer, registered adviser, or	No restriction on affiliation. A restricted dealer funding portal that is affiliated with another registered firm must establish internal controls and appropriate policies and procedures to manage the risks associated with operating an affiliated restricted dealer funding portal.				

Jurisdictional Differences in MI 45-108 Crowdfunding						
	Ontario	New Brunswick	Nova Scotia	Manitoba	Saskatchewan	Quebec
	registered investment fund manager.					
	Substitution of NI 31-103 requirements for similar (but not identical) Ontario Securities Act registration requirements.	No local rule substitutions.				
	Issuer access agreement must include confirmation funding portal is agent of issuer for purposes of a distribution under the CF exemption.	No confirmation of agent requirement.				
	Restricted dealer can only act for a distribution under CF Exemption.	Restricted dealer portal may act for a distribution under CF Exemption and Start-Up CF Exemption.				

The proposed version of the Integrated Crowdfunding Exemption to be adopted in Alberta mirrors the Ontario version other than: (1) there is no requirement for a notice of specified key events if a private issuer; (2) the offering documents are considered an offering memorandum with rights available under the Alberta Securities Act; and (3) restricted dealers may also sell securities under the *Alberta Securities Commission Rule 45-517 Prospectus Exemption for Start-up Businesses* (the “**Start-up Business Exemption**”). If adopted in Alberta as proposed, Canada will have yet another version of the Integrated Crowdfunding Exemption.

**There should be no Caps on Accredited Investors under the Rule**

There appears to be no logical reason to impose distribution caps or aggregate yearly investment caps on accredited investors under this exemption.

Under the existing accredited investor exemption there are no caps on the amount someone who is qualified as an accredited investor can invest in a distribution, or yearly limit as to how much they may invest in public or private issuers. The accredited investor exemption is based on the premise that someone who is an accredited

investor has the financial sophistication and ability to sustain the risk of loss of investment or the ability to protect themselves which render the protections of the securities act's registration process unnecessary. It is unclear why accredited investors now need protection from investing in securities offered under the Integrated Crowdfunding Exemption or should be discouraged from participating in these offerings.

Issuers are forced to run two concurrent offerings (one utilizing the Integrated Crowdfunding Exemption and another utilizing the accredited investor exemption) if an accredited investor wishes to invest more than \$25,000 or the issuer or investor is located in Alberta and Ontario and the investor has maxed out his yearly investment cap of \$50,000. Not only does this add complexity, it removes valuable information about who is interested in investing in an issuer and the benefits accredited investors bring to the due diligence process of a crowdfunding investment.

Non-accredited investors benefit when accredited investors (angels, venture capitalists, and market professionals) participate in a crowdfunding offering as they often have the means and ability to evaluate the merits of the business and offering. If accredited investors are restricted or absent from these offerings, non-accredited investors cannot take advantage of the knowledge base accredited investors can bring to the shared evaluation process. Limiting and discouraging the participation of accredited investors removes a potentially important investor protection mechanism in equity crowdfunding.

We strongly encourage Alberta to not adopt the Ontario version of the Integrated Crowdfunding Exemption which imposes an aggregate yearly investment cap on accredited investors and instead to join the other participating jurisdictions in adopting a version of the exemption with no yearly investment caps. We also encourage Alberta and the other participating jurisdictions to eliminate the per distribution cap currently in place for accredited investors.

### **Accredited Investor Confirmation and Validation**

Except in Ontario (and Alberta), issuers and portals are required to confirm and validate if an investor is an accredited investor if the acquisition cost is greater than \$2,500. In all jurisdictions, if an investor indicates they are an accredited investor or a permitted client, the portal is required to obtain further information from the purchaser in order to determine whether the purchaser has the requisite income or assets to meet the terms of the accredited investor or permitted client definition.

Portals and issuers struggle with what is required of them to confirm and validate that someone is an accredited investor. Ideally, they would like to be able to rely on self-declarations by investors or use a check-the-box approach, however, regulatory actions across Canada and guidelines issued by various regulators have indicated these actions are not sufficient to determine if someone is an accredited investor.

It appears Ontario's (and Alberta's) *Form 45-108F3 - Confirmation of Investment Limits* not only serves to provide information about investment limits but also confirms for issuers (but not portals) an investor is an accredited investor. If this is true we encourage all participating jurisdictions to adopt an accredited investor confirmation and validation form that issuers and portals can rely on to determine if someone is an accredited

investor. Alternatively, we ask the regulators to provide further guidance given that it is not clear how confirmation and validation of accredited investor status can be streamlined to meet the requirements of the regulators and at the same time not put-off potential investors or be a costly exercise.

### **Allow Advertising**

The Integrated Crowdfunding Exemption should be amended to allow advertising and general solicitation. Issuers and registered dealers have been allowed to use advertising and general solicitation when utilizing the accredited investor exemption and the offering memorandum exemption for over ten years. During this period there has been very little abuse attributed to advertising and general solicitation. Abuse that has been identified in this area has gone hand in hand with fraud, material misrepresentations, and a flagrant disregard for securities laws all together.

Allowing advertising and general solicitation increases investor protection. In donation, pre-sale and perk crowdfunding campaigns advertising and general solicitation draws in hundreds of people who review and provide their opinion and knowledge about the issuer, founders, business, product and perk. Allowing advertising and general solicitation creates transparency, and unlike online bulletin boards and chat rooms, potential investors and commenters cannot hide their identity behind multiple aliases. Fraud is rare and quickly uncovered in this type of environment. You want equity crowdfunding campaigns to be seen by as many people as possible.

Not allowing advertising, and requiring or allowing portals to put information about an offering behind a wall, creates a private room environment where issuers and portal operators have a greater ability to hide what is being said to potential investors and what communication regulators can see as well. It is equivalent to creating a “private pitch dinner” or “timeshare presentation” environment which can breed high-pressure sales tactics, falsified information, and empty promises. Regulators cannot police everything and the crowd will alert you to issuers and founders who are not who they say they are or who are not abiding by the rules which would otherwise be missed if only a few people are aware of an issuer’s equity crowdfunding campaign.

Advertising and general solicitation is allowed under the equity crowdfunding rules in the United Kingdom. We believe this is one of the reason equity crowdfunding has been so successful for issuers raising capital in the United Kingdom. In the United States, twenty-one states have explicitly allowed for advertising and general solicitation in their intrastate crowdfunding exemption rules. The remaining states who have adopted an intrastate crowdfunding exemption are silent on the issue, and no state bans advertising and general solicitation in its intrastate crowdfunding exemption rules.

### **Eliminate or Provide a Reasonable Sunset Clause to Ongoing Disclosure Requirements**

Under the Integrated Crowdfunding Exemption non-reporting issuers must provide investors and file with regulators annual financial statements and an annual statement of use of proceeds, and in Ontario, New Brunswick and Nova Scotia, notices of significant events. Financial statements are required to be:

- audited or reviewed by a public accounting firm if the cumulative amount an issuer has raised under any securities exemption since its formation is \$250,000 or more but is less than \$750,000, or
- audited if the cumulative amount an issuer has raised under any securities exemptions since its formation is \$750,000 or more.

Using a cumulative threshold pretty much guarantees most non-reporting issuers considering using the exemption will be required to file audited financial statements at some point in time. This is a very expensive proposition to non-reporting issuers as these statements must be prepared in accordance to *National Instrument 51-102 Continuous Disclosure Obligations*, *National Instrument 52-107 Acceptable Accounting Principles and Auditing Standards* and International Financial Reporting Standards (IFRS), versus Canadian GAAP for Private Enterprises.

These ongoing disclosure requirements continue until a non-reporting issuer becomes a reporting issuer, winds-up or dissolves its business, or has fewer than 51 security holders worldwide.

If an issuer raises \$150,000 under the Integrated Crowdfunding Exemption and all investors put in \$2,500, the maximum allowed by non-accredited investors, that issuer will have 60 new security holders. If they had previously raised \$600,000 through friends and family or accredited investors they would be required to provide audited financial statements indefinitely. The cost of meeting this ongoing disclosure requirement far outweighs the advantage or interest any non-reporting issuer may have in using this exemption.

An indefinite ongoing disclosure requirement only makes sense if a non-reporting issuer is continually raising capital, planning to go public in the near term, or has a definite life span like a limited partnership.

Ongoing disclosure requirements do not apply when an issuer raises capital under the private issuer exemption, the accredited investor exemption, the Start-up Crowdfunding Exemption or the Start-up Business Exemption. It should not exist here either unless it has a reasonable sunset clause such as one year after a non-reporting issuer raises capital under the Integrated Crowdfunding Exemption.

### **Increase Amount that May be Raised under the Integrated Crowdfunding Exemption**

The maximum an issuer group can raise under the Integrated Crowdfunding Exemption in a twelve month period is \$1.5 million.

We believe this limit should be \$5 million or higher in order to make this exemption attractive to issuers. It is our understanding that this limit was previously selected based on the U.S. \$1,000,000 limit set out under Title III of the *JOBS Act* and the proposed, now effective, U.S. Securities and Exchange Commission crowdfunding rules. Several House and Senate members in the United States have proposed the cap be raised for offerings under Title III Crowdfunding under various bills, none of which have yet been adopted. Under the intrastate crowdfunding exemptions offering caps vary from \$100,000 to \$5 million per year. Other than in Oregon, there has been no activity under the intrastate crowdfunding exemptions in states where the offering cap is less than US \$1 million.

This yearly cap should be considered in context of the markets you are trying to encourage and support in Canada, and the cost and burden imposed on issuers who wish to use the Integrated Crowdfunding Exemption.

Two years ago data from equity crowdfunding portals in Europe and accredited investor equity crowdfunding portals in the U.S. seemed to indicate the mean offering size of existing campaigns were under \$1.5 million. Data from 2015 and 2016, however, indicates these portals are now regularly helping issuers raise over \$1.5 million for early stage companies. A higher limit would support a wider variety of issuers and make the cost of undertaking such an offering worthwhile.

We also believe an issuer's raise should not be aggregated with 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. A parent or subsidiary company may be involved in a completely different line of business or be the research arm of the organization. New developments and opportunities may be stifled by treating these entities as one for the purpose of this exemption.

#### **Increase Threshold for the Requirement for Review and Audited Financial Statements**

Issuers are required to provide financial statements as part of their offering material which have:

- been approved by management if the cumulative amount an issuer has raised under any securities exemption since its formation is under \$250,000;
- audited or reviewed by a public accounting firm if the cumulative amount an issuer has raised under any securities exemption since its formation is \$250,000 or more but is less than \$750,000, or
- audited if the cumulative amount an issuer has raised under any securities exemptions since its formation is \$750,000 or more.

As discussed previously, it is extremely expensive and burdensome for non-reporting issuers to obtain reviewed and audited financial statements. It is not uncommon for review engagements to cost \$20,000 or more. Audited financial statements can cost a lot more for non-reporting issuers who have active businesses.

Regulation A in the United States is similar to our offering memorandum exemption in Canada. Under Tier 1, Canadian and United States resident issuers can raise up to US \$20 million dollars under the exemption with no audited financial statements required.

The majority of the intrastate crowdfunding exemptions do not require reviewed or audited financial statements until an issuer raises \$1 million or more. Title III Crowdfunding in the United States does not require reviewed or audited financial statements by first time users of the exemption unless they are otherwise available. Canadian non-reporting issuers are placed at a serious disadvantage to the issuers located elsewhere in the world by requiring they have reviewed or audited financial statement under the current threshold amounts.

The Integrated Crowdfunding Exemption is the only exemption we are aware of that uses a cumulative amount raised over the life of the issuer to determine if reviewed or audited financial statements are required. As a result, almost all high growth companies that have been around longer than three years will be required to provide audited financial statements if using the Integrated Crowdfunding Exemption.

Non-reporting issuers should not be required to provide audited financial statements unless they are planning to raise over \$1.5 million. A per distribution approach should be applied to this requirement and not a cumulative approach.

### **Eliminate Requirement for Personal Information Forms and Criminal Record and Background Checks**

Requiring personal information forms from management of issuers looking to raise capital is intrusive and not required when using other capital raising exemptions in Canada. Requiring portals to conduct criminal record and background checks is also not required when raising capital using other exemptions in Canada. These checks are also incredibly time consuming and expensive for a portal to undertake. These requirements increase the cost of raising capital under the Integrated Crowdfunding Exemption and make its use unattractive to both issuers and potential portal operators. These requirements should be eliminated.

### **Require Portals to Keep all Campaign Materials Online and Open to the Public**

Section 31 of the Integrated Crowdfunding Exemption requires portals to remove the distribution materials of an issuer's crowdfunding campaign at the end of the distribution period. We believe this is a mistake.

Regulators should require issuers and portal operators to keep all campaign materials on the portal and available to the public to access post campaign. This information provides historical transparency which will allow the public, regulators, professionals and other third parties to track issuers and their founders' performance and their capital raising history. This type of transparency will encourage issuer and founder accountability for their statements and financial stewardship of investors' funds. It will also encourage portals to curate quality companies versus being solely fee driven in terms of who they allow to raise capital through their portal. Erasing or allowing portals to hide this information behind a paywall eliminates a valuable tool for investor protection. This also would bring the requirements and practice of Canadian portals in line with portals operating in the Asia, Europe, New Zealand, the United Kingdom and the United States.

### **Simplify Registration Process of Restricted Dealers**

Feedback we have received from groups who have investigated whether they should pursue becoming a restricted dealer under the Integrated Crowdfunding Exemption is that the process is confusing and complicated. These rules should be simplified and all of the rules should be found in one place and not refer to substitution of *National Instrument 31-103* requirements for similar (but not identical) Ontario *Securities Act* registration requirements. They are also concerned about their liability exposure and ability to streamline the process sufficiently to meet the regulatory requirements and make a profit.

It is our opinion that the requirements under the Start-up Crowdfunding Exemption struck the appropriate balance of what should be required of groups wanting to become a portal operator and operate a portal. As a result, eight portals are now operating under the Start-up crowdfunding exemption. No portals are currently operating as a restricted dealer under the Integrated Crowdfunding Exemption.

Ontario (and Alberta) should eliminate the requirement that a restricted dealer funding portal not be an affiliate of another registered dealer, registered adviser, or registered investment fund manager. We believe this may encourage some existing dealers to consider running a portal under the Integrated Crowdfunding Exemption.

### **Marketplace Lenders**

The Integrated Crowdfunding Exemption and restricted dealer registration as currently adopted do not work for the majority of marketplace lending platforms successfully operating outside of Canada. The rules do not take into consideration multi-party participation of public, private and government blended funding models which have developed in the United Kingdom and Europe. They also do not allow for a financial institution to either operate a marketplace lending portal or heavily participate in each funding event (a number of successful portals have the crowd raise 25% and the portal/institution loan 75%). Requiring marketplace lending portals to do a suitability analysis of each lender (investor) when their loan (investment) is capped and a participating institution or party is involved ignores the fact these lenders may have extensive experience with small business loans. The rules also do not allow for the implementation of membership marketplace lending models.

Regulators should revisit the Integrated Crowdfunding Exemption and make changes or accommodations that allow for the exemption to be relied on by marketplace lenders. We also encourage you to implement a regulatory sandbox project which provides a class-wide licensing waiver for new businesses to run early-stage tests and trials in the fintech area. The dynamics of this sandbox should encourage dialogue versus suspicion between the private market innovators and regulators. Any action Canadian Securities Administrators implement in this area should be undertaken in conjunction and in association with other interested regulatory bodies.

The regulatory sandbox approach has had good success in the [United Kingdom](#) and was formalized earlier this year. The [Australian Securities & Investment Commission](#) just recently issued an update on its Innovation Hub for fintech companies. In the United States, the Consumer Financial Protection Bureau formed Project Catalyst to engage with companies developing innovative consumer financial products and serves and provides as an established process for obtaining a [no-action letter](#) (equivalent to an exempt application in Canada) concerning innovative financial products.

Marketplace lending platforms are having a significant impact on SMEs in the United Kingdom, as set out in the Cambridge University 2015 [UK Alternative Finance Industry Report](#), and in the United States, as illustrated in report prepared by the [Milken Institute Center for Financial Markets](#) which profiled 70 of the [United States based online non-bank fintech businesses](#). Canada is at risk to be left behind in the fintech revolution if our regulatory environment thwarts innovation and change.

**Closing Comments**

We encourage the Alberta Securities Commission to adopt the Integrated Crowdfunding Exemption (preferably in the form adopted by Saskatchewan and Manitoba). We also encourage Alberta to undertake community outreach to educate Albertans about the exemption and to support its use by private and public issuers. In other jurisdictions, this type of participation has worked to foster portals and issuers using those jurisdiction's equity crowdfunding exemption.

Please feel free to contact us at any time to discuss further.

Sincerely,

Craig Asano  
Founder and Executive Director  
NCFA Canada  
+1 (416) 618-0254

Enclosure

# The National Crowdfunding Association



**Education, Advocacy, Networking, Growth**

*Fostering a dynamic, vibrant and inclusive Crowdfunding industry in Canada*

## **Proposed Multilateral Instrument 45-108 Crowdfunding**

NCFCA Canada Board  
September 9, 2016

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## About NCFA Canada

- The National Crowdfunding Association of Canada (**NCFA Canada**) is a cross-Canada non-profit organization with a mandate to be inclusive in providing **education, awareness** and **advocacy** in the rapidly evolving crowdfunding industry.
- NCFA Canada is a community-based and membership-driven non-profit entity that was founded at a grass roots level to fill a national need in the marketplace.
- Members and prospective members are industry stakeholders (e.g., portals, experts, service providers and enablers), small businesses using crowdfunding to fund their initiatives and investors seeking to learn more and get connected with a relevant and national membership peer network.

## Overview

### The Importance of SMEs to the Canadian Economy

- Small to mid-sized enterprise businesses (**SMEs**) are the lifeblood of the Canadian economy. From the corner laundry mat to the emerging high tech software company there were a total of 1,105,972 SMEs in 2012 according to Industry Canada. By definition, SMEs include micro-enterprises (1-4 employees), small businesses (5-100) and medium sized businesses (101-500).
- In 2012, SMEs hired 89.9% of the entire workforce. Stated differently, almost nine in every ten persons is directly affected and reliant on the SMEs for their livelihood. In 2011, SMEs represented 27% of Canada's total GDP and also accounted for \$150 billion in exports, or 40.1% of Canada's total export value.<sup>1</sup>
- SMEs play a significant role as a feeder system. Successful smaller companies may grow, acquire other businesses or assets, and possibly become larger public companies.

### SME's Funding Challenge

- A funding gap exists for Canadian start-ups and SMEs to raise small amounts of capital (e.g., estimated by various industry professionals to be \$1 to \$5 million) that is not currently being satisfied by friends and family networks, angels, incubator/accelerator programs and venture capital (**VC**) groups.
- Traditional institutions and alternative lenders have strict lending requirements that most start-ups do not qualify for. Many small businesses cannot get a line of credit approved by their bank (or revive credit lines) due to poor sales or insufficient collateral to support their loan requests.
- Many small businesses are asked to front money to initiate a funding process or are advised to pay expensive financial and legal planners to develop detailed business plans and prospectus documents that exceed the budget and viability of many start-ups and SMEs.
- Incubators and accelerators are excellent options, however there are only a limited number of placements available (e.g., most programs are operating at maximum capacity) and they generally focus on a niche industry. VC has been on the decline. In 2000, \$5.9 billion was invested in 1,007 Canadian start-ups, according to Thomson Reuters, compared to just \$1.1 billion in 2010 that was raised by 357 Canadian firms representing an alarming decreasing trend in a ten year period. In 2014, Canadian start-ups received \$2.36 B in funding, nearly double the amount invested five years ago but this was primarily due to four exceptionally large financing.<sup>2</sup> VCs are incentivized to participate in larger funding transactions and the average deal sizes are mismatched with the needs of SME issuers.<sup>3</sup>

### What's at Stake?

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<sup>1</sup> Key Small Business Statistics - August 2013 Edition, Innovation, Science and Economic Development Canada, Industry Canada  
[http://www.ic.gc.ca/eic/site/061.nsf/eng/h\\_02800.html](http://www.ic.gc.ca/eic/site/061.nsf/eng/h_02800.html)

<sup>2</sup> <http://www.reuters.com/article/canada-investment-idUSL1N0VK2MW20150210>

<sup>3</sup> <http://www.theglobeandmail.com/report-on-business/streetwise/canadian-venture-capital-stuck-in-deep-rut/article616668/>

- Fundamentally there's a strong need to ensure SMEs have the proper access to capital to innovate and develop competitive products/services to bring to Canadian and global markets.
- Without a clear funding roadmap for small businesses or an efficient and legally viable capital formation process many valid business ideas will not get funded in Canada.
- Crowdfunding has gained a lot of momentum in North America and Europe. Equity crowdfunding is currently legally permitted in many countries, such as Australia, United Kingdom ("UK"), Netherlands and the United States ("US"). will soon be added to the growing list with the passing of the [\*Jumpstart Our Business Start-ups Act \(JOBS Act\)\*](#)<sup>4</sup> last April 2012.
- Canada needs to review its securities laws to ensure they are current and suitable to meet the needs of SME issuers and their ability to connect with prospective investors (funders) and successfully raise early stage capital from online market places.
- Canada risks losing its Canadian funded ideas and best entrepreneurs to countries with more supportive funding environments and access to capital (e.g., US) that are keen to commercialize on Canadian start-up ventures.
- Canada will continue to slide down global innovation rankings and the economy will suffer as a result negatively impacting job creation and Canada's strategic social-economic advantages.<sup>5</sup>

### **NCFA Canada 2015 Conferences and Outreach**

In 2015, NCFA Canada held five events across Canada (Toronto: March 3, 2015, July 28, 2015, and October 15, 2015, Vancouver: September 29, 2015, and Calgary: December 3, 2015) to educate and receive feedback from various constituent groups interested in start-up capital in their communities. All of these events were held in association with strong government, academic, industry and community supporters such as the Dec 3rd event held in Calgary that involved participants from Government of Alberta (Innovation and Access to Capital; and Alberta Securities Commission), ATB Financial, VA Angels, LendingArch, Business Link and SeedUps Canada. NCFA Canada and all in attendance appreciated the participation by local securities regulators in each jurisdiction at these events.

In addition to holding conferences, NCFA Canada has fielded questions from aspiring crowdfunding portal operators, issuers, and investors by telephone and email. We have published an equity crowdfunding FAQ on our website and provided articles summarizing the key elements of the proposed crowdfunding exemptions. We are also in the process of finalizing an e-book of a larger array of questions and answers on equity crowdfunding and investing in general, and an industry led whitepaper on the topic of Online Lending in Canada.

### **National Crowdfunding Surveys in Canada**

In 2013, NCFA Canada collaborated with the Exempt Market Dealers Association of Canada to develop and host the National Canadian Crowdfunding Survey in Canada ([link to survey](#)) ("2013 Survey"). The purpose of the survey was to obtain a better understanding of the various stakeholder opinions on legalizing equity Crowdfunding in Canada and to provide Canadian securities regulators with feedback on many of the issues Canadian securities regulators were seeking input into on online capital raising options for SMEs.

NCFA Canada has joined Cambridge Centre for Alternative Finance at Cambridge Judge Business School and the Polsky Center for Entrepreneurship and Innovation at Chicago Booth School of Business in launching the 2015 Americas Alternative Finance Benchmarking Survey.

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<sup>4</sup> [http://en.wikipedia.org/wiki/Jumpstart\\_Our\\_Business\\_Startups\\_Act](http://en.wikipedia.org/wiki/Jumpstart_Our_Business_Startups_Act)

<sup>5</sup> <http://www.ncfacanada.org/poor-innovation-ranking-dims-the-lights-on-canadas-competitiveness-and-prosperity/>

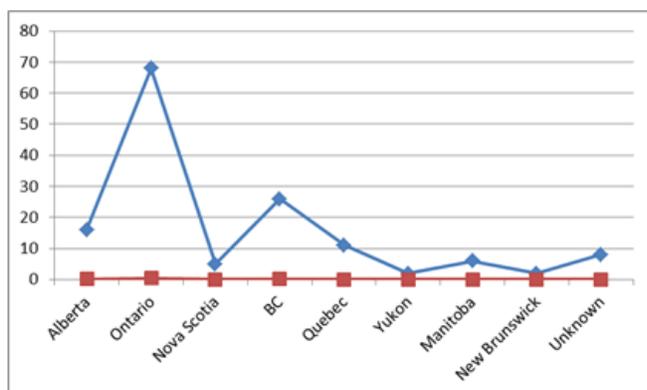
Additionally, NCFA Canada is in the process of completing a 2015 Canadian Crowdfunding Platform Survey that attempts to measure the size and make-up of the Canadian market. The survey is expected to be completed in time for release in the first quarter of 2016. There is also discussion about administrating a follow-up survey to the original 2013 Survey to gage how opinions of various stakeholders has changed or evolved since 2013.

We believe the results of our 2013 Survey, although focused on an equity crowdfunding specific exemption, is equally relevant to the Participating Regulators as they consider the Start-Up Business Exemption.

### Overview of 2013 Survey Responders

We received a total of 144 survey responders from NCFA Canada’s crowd:

- 100% of responders represented start-up and/or SME issuer views
- Almost 75% were a planned portal or service provider
- 70% / 25% identified themselves as non-accredited / accredited investors
- 12 self-identified as registrants including exempt market dealers, investment dealers, or portfolio managers



**Responders by Province**

Alberta	16	11.1%
Ontario	68	47.2%
Nova Scotia	5	3.5%
BC	26	18.1%
Quebec	11	7.6%
Yukon	2	1.4%
Manitoba	6	4.2%
New Brunswick	2	1.4%
Unknown	8	5.6%
<b>total</b>	<b>144</b>	<b>100.0%</b>

### Preliminary Survey Results

In addition to the raw data survey responses below, NCFA Canada Advisory Board member, Douglas Cumming, Professor and Ontario Research Chair, York University – Schulich School of Business, and his research team, conducted further analysis of the data: [Demand Driven Securities Regulation: Evidence from Crowdfunding](#) (Apr 2013); and [Crowdfunding and Prosperity In Ontario](#) (Mar 2014).

### **Should we Adopt a Crowdfunding Exemption?**

- 95.7% of responders voted that Canada should adopt a crowdfunding exemption under applicable securities laws.
- 74.8% of survey participants were moderately to extremely familiar with crowdfunding.
- Overall, approximately 90% of survey responders agreed or strongly agreed that there would be significant benefits for both SME issuers and investors by adopting a crowdfunding exemption.

### **Investor Motivations to Make an Investment through Crowdfunding (Ranked in Order):**

1. Innovation and entrepreneurship
2. Financial incentives
3. Non-financial incentives
4. Direct access to entrepreneurs
5. Diversification
6. Networking

### **Should Canada Move Ahead or Follow the SEC and FINRA?**

- 60.6% of survey responders agreed or strongly agreed that Canada should move ahead and finalize crowdfunding rules and regulations (23.1% were undecided).

### **Pilot Project**

- 73.7% of survey responders believed that Canada should approve a crowdfunding exemption on a trial or limited basis initially.
- 43.3% or the majority of survey responders answered that the trial should be based on a limited period of time.
- A very low 5.6% clearly indicated that a crowdfunding pilot project should not be restricted to a particular industry or sector.

### **Investor Limits and Restrictions**

- 72.9% of the responders voted that the investment cap should be \$10,000-\$15,000 or more per investor in a 12-month period.
- 64.2% of responders indicated that there should not be any further caps on the funds that can be invested with a single crowdfunding issuer within a 12 month period.

### **Issuer Limits**

- 45% of responders voted that the aggregate amount of capital that an issuer should be able to raise in a 12 month period is up to \$2,000,000.
- 45% of responders indicated that there should not be a limit.

### **Secondary Market**

- 64.4% of survey responders believed that securities should be free-trading after a period of time.
- 83.7% of survey respondents indicated that crowdfunding securities should be eligible for second market trading after 12-24 months of the original purchase.
- Note, by way of comparison and under the USJOBS Act there is a moratorium on transferring shares within one year from the date of issuance, unless the transfer is to an accredited investor or back to the company.

### **Prospective Crowdfunding Exemption**

NCFA Canada advocates that a crowdfunding exemption in Canada will increase the awareness of Canadian start-ups, support innovation and entrepreneurship, create jobs and contribute to the total GDP and export base of the economy.

### Proposed Implementation Principles

To cultivate the benefits of investment crowdfunding frameworks, regulators must strike the right balance between protecting investors while ensuring efficient capital formation for SMEs. To assist with this task, NCFA Canada has developed eight (8) high-level implementation principles to be used as guidelines when considering the costs and benefits of a prospective crowdfunding exemption in Canada. (These considerations apply equally to the Start-Up Business Exemption.)

Principle	Concept	Description
1. Harmonious	Collaborative development	The collaborative development of a harmonized set of crowdfunding regulations to benefit Canada as a whole.
2. Inclusive	All sectors and industries	To be as inclusive as possible to a broad-based range of sectors and industries to encourage balanced growth in communities across the country.
3. Transparent	Disclosure rules and crowd intelligence	Support transparent disclosure and crowd intelligence as a means to help government and industry prevent, identify and report potential fraud and abuse to authorities within a timely manner.
4. Adaptive	Innovative market adaptation	To ensure crowdfunding regulations support market evolution enabling innovation to flourish.
5. Robust	Efficient capital formation	A regulatory framework that gives SME issuers and investors (funders) the confidence that there is a robust framework in place capable of efficient capital formation, and one that is collectively supported by the eco-system.
6. Open	No jurisdictional restrictions	Enable a vehicle to allow businesses to accept investment (and funding) from other jurisdictions on a limited basis encouraging competitiveness, collaboration and cross border participation.
7. Additive	New channels and source of funds	Ensure crowdfunding regulations are designed to open up largely a new source and channel of funds by minimizing the impact and overlap with existing exempt market exemptions.
8. Protective	Investment caps and reasonable due diligence	Protect investors by limiting investment exposure, promoting education, fraud detection and implementing a fair and reasonable amount of due diligence and compliance without overly burdening the process.

### Contact Information

Craig Asano  
 Founder and Executive Director  
 NCFA Canada  
 +1 (416) 618-0254