

Consulting on the Securities Law Framework for Fintech Regulation (BC Notice 2018/1)
Response of the National Crowdfunding & Fintech Association of Canada (NCFA)

The NCFA is a national non-profit organization engaged with both social and investment crowdfunding and fintech stakeholders across the country. It provides education, research, leadership, support, and networking opportunities to over 1600 members and works with the private sector, government, academia, and community and eco-system partners and affiliates to create a strong and vibrant crowdfunding and fintech industry in Canada. The NCFA supports 'innovation finance' - aiming to make the financial ecosystem more accessible and inclusive and to enhance the use of technology for smarter, faster, and more secure decisions and services.

Introduction

Thank you for the opportunity to comment. We appreciate the active steps that BCSC is taking to better understand a fast moving ecosystem and to adapt accordingly.

The NCFA provided both oral and written input on many of the issues below to the BCSC in 2017. Except in response to the questions posed by the BCSC, the NCFA does not repeat those submissions here.

The consultation questions

1 (a) Although we are limited by a serious absence of data in Canada, the limited data we do have, supplemented by anecdotal evidence from our members, supports our assertion that moving to a lifetime raise of **\$1 million** would increase the effectiveness of the start-up crowdfunding exemption. The \$250k cap per 6 month subscription is unduly limiting for most types of businesses that could rely on the exemption.

However, we have argued previously for no caps (or at least a higher limit of \$5 million over the fund-raising lifetime but ideally possible in one financing). This would be more in line with other (successful) jurisdictions. In the UK, for example, there is no cap on the total amount an issuer can raise in any given year and no limit on the amount an investor can invest - <https://www.wealthforge.com/insights/crowdfunding-gaining-traction-in-the-uk-but-what-about-the-us>. Assuming other appropriate requirements (such as for disclosure and KYC), there is no significant risk to consumer protection of which we are aware that should prevent this.

We wonder how the higher cap is working in Alberta?

(b) The BCSC will know from our earlier submissions that the NCFA is strongly in favour of removing the requirement for "**eligible securities**" or expanding the definition to allow for eg convertible securities.

(c) We continue to propose other changes to the crowdfunding exemptions across Canada. We argue that many restrictions are not justified by the risks. Their only effect is to restrict or prevent start-ups in Canada. (To the extent that the BCSC continues to

be of the view that those prescriptive requirements are justified by the risks, we ask that the analysis be made public so that we can more effectively respond.)

Our main recommendations for regulatory change across Canada remain:

- harmonize crowdfunding/start-up requirements across Canada
- permit advertising and general solicitation (or make it easier)
- increase the threshold for required review or audited financial statements
- allow accredited investors to fully participate (without caps)
- eliminate retail investor caps (or at least increase them)
- provide a reasonable sunset clause for audited financial statements
- increase the period for filing of the distribution reports.

Online lending

Although the staff of securities regulators in Canada, including the BCSC, have supported the development of peer to peer (P2P) lending platforms such as Lending Loop, there are fundamental aspects of the securities regime that are not well suited to regulating what is in substance a loan brokerage activity linking lenders (investors) with small and medium sized business (SME) borrowers under a simple loan agreement.

We call for the establishment of a regulatory regime that recognizes and accepts that the activities of P2P lenders (and simple loan agreements) are inherently different from equity investments and should be regulated differently.

We ask that CSA examine and adopt the regulatory models in other jurisdictions such as the UK and New Zealand where frameworks were developed specifically for P2P lending (see <https://fma.govt.nz/compliance/role/peer-to-peer-lending-providers/>). Securities regulators should exempt P2P lenders from securities legislation on the condition that they comply with provisions designed for P2P lenders.

A new regulatory paradigm should improve a lower rate of adoption in Canada than seen in other jurisdictions where P2P and B2B have provided significant economic stimulus by supporting the growth of the SME sector.

2. The BCSC asks whether it should make changes to the regime that would increase differences with other jurisdictions. Since the changes would (presumably) reduce burden, the answer has to be, in principle, yes. The benefit should outweigh the cost (if any).

3. What is the likely impact of ICOs on existing crowdfunding opportunities? There are similarities and differences between traditional crowdfunding and ICOs in terms of models, regulations, ownership, usage, and liquidity to name but a few. However, they both seek to use technology to raise early stage capital for new products/services and ventures while allowing a wider pool of investors to participate.

We view ICOs and tokens as the next generation of crowdfunding using DLT and decentralized models that improve liquidity and contract reliability in ways that traditional

crowdfunding platforms cannot achieve. For example, ICOs can reduce or eliminate the need for transactions to be verified by third parties via decentralized networks that are in a way self-regulating. Blockchain allows smart contracts/tokenization that can automate and execute pre-agreed conditions once they are met.

All stakeholders are assessing ICOs and the risks associated with them in a rapidly evolving market that has unfortunately also attracted the interest of many speculators whose primary concern is not necessarily compliance or honest behaviour. This has not been a major concern with traditional crowdfunding. Nevertheless we are seeing the emergence of best practices from KYC and AML processes to governance and transparency standards. We expect this trend to continue. See the recent ICO best practice document from the Hong Kong FinTech Association.

On the one hand we urge regulators not to over-react to risks of financial crime and poor operating behaviour by ICOs (but to deal firmly and expeditiously with either under existing laws). It would be a mistake to substitute over-regulation for (for example) inadequate criminal enforcement. On the other hand, we urge ICOs to improve their self-regulation so regulators can be less concerned about the risks. We recognize that if ICOs do not themselves improve, then they can expect regulators to tighten up.

Meanwhile, regulators should strive not to unduly delay applications for exemption by existing dealer licensees who have built up appropriate operating practices and who would like to manage the distribution of ICOs across all jurisdictions.

If ICOs are regulated appropriately and a vibrant market develops, then they will likely supersede many of the investment crowdfunding models in the market today.

As with traditional crowdfunding, if ICO regulation is too costly, then companies, investors, and infrastructure providers will move to foreign markets and jurisdictions that offer more facilitative and supportive capital raising. Lack of certainty is also driving ICOs to other markets. Canadian issuers and investors both need more guidance, soon, on the regulatory approach(es) in Canada.

4. What kind of educational/awareness outreach opportunities or mechanisms should BCSC be considering?

The Financial Consumer Agency of Canada has taken the lead on financial literacy with good results. They may be best placed to take the lead on education and awareness of crowdfunding and innovation finance. One body should be working with regulators, the private sector, and others for consistent online/offline educational programs, developing and tracking key metrics, benchmarking, and participating in research initiatives. We should be working together to do more and not wasting resources by re-inventing the wheel.

Part 4 - Online advisers

We leave this section for response by our members.

Part 5 - Cryptocurrency funds

Given the present uncertainties, we advocate a wait and see approach (as in the UK - <https://www.coindesk.com/uks-fca-chief-warns-bitcoin-investors-be-prepared-to-lose-your-money/>). Regulators should not hastily impose more requirements where they quite possibly are not needed. We commend BCSC for its more open attitude to cryptocurrencies.

NCFA also supports the creation of a Canadian crypto task force - <https://cointelegraph.com/news/britain-introduces-crypto-task-force-to-foster-fintech-innovation>. It is extremely important that stakeholders collaborate, that Canada remain in synch with important jurisdictions, and that regulation is essentially global.

Part 6 - ICOs and cryptocurrencies

26. At this point in the evolution of the ICO markets, we think that the exemption power is sufficient, along with general warnings to investors about the risks of both regulated and unregulated ICOs. It is not obvious to us that new regulatory requirements are needed. What is obvious is the need for close collaboration among regulators and the industry across Canada and globally, and firm enforcement of existing laws.

27. We do not comment on the variables listed. The main point here that Canada must remain broadly in synch with important jurisdictions such as the USA , Australia, New Zealand, Singapore, and the UK.

Part 7 - Fintech regulation in the future

34/35. The NCFA supports a 12-month exemption similar to the ASIC exemption, with similar safeguards.

36. The NCFA has already provided its views to the BCSC on regulatory requirements or approaches that stifle innovation and how they should be removed or changed.

39 to 42. We support the risk-based approach of the UK Financial Conduct Authority where data collection and analysis are also a priority.

Regulators, governments, and other stakeholders in Canada should be closely following what more advanced regulators (and markets such as the UK, Australia, New Zealand, China, and Singapore are doing). These jurisdictions are well ahead of us.

Most studies of fintech around the world assert that collaboration among regulators, governments, and with the private sector needs to improve. Without improved collaboration, and without an over-arching strategy for innovation, both regulation and the markets in Canada (overall) will remain sub-standard.

Other points

The BCSC Notice states that BC's start-up ecosystem has been ranked among the strongest in the world. Although we agree that the regime is more supportive of start-

ups than in other Canadian jurisdictions, it would be helpful to know who has provided this ranking (and to see the data that supports it).

It is a constant struggle in the start-up ecosystems in Canada to gain access to data and analysis about what is going on the markets of the provinces and across Canada as a whole. Smart regulation and meaningful cost/benefit analysis is impossible without it.

We lag far behind the UK and others in data collection and analysis. To provide one example of how this is problematic, the BCSC Notice states that “respondents noted the limited risk appetite among BC investors and pool of available capital in BC as significant non-regulatory barriers to growth and development”. We wonder whether better data would support that conclusion. Our members do not perceive that BC investors are inherently risk averse. Rather they may lack education or awareness about investing in innovation and fintech, but are keen once they learn and feel more comfortable with the ecosystem. (We have explained in earlier submissions that certain regulatory changes would actually help investors to manage/spread their risks.)

At Globe Forum 2018 in March, Canadian capital providers noted that their Canadian investments in innovation were limited less by the lack of capital and more by the lack of good projects coming up through the system. This suggests to us that start-ups are blocked by the costs of start-up in Canada, rather than lack of capital as such. But we do not have the hard data to back this up.

We very much support the creation of the BCSC Tech Team and have been impressed by the team’s willingness to learn, to talk openly with our members, and to provide guidance to entrepreneurs where appropriate. The BCSC has become an increasingly valuable sponsor and participant at NCFAs conferences such as VanFunding.

We are encouraged by BCSC and OSC collaboration with other regulators to improve the sandbox in a way that is consistent with other jurisdictions such as the UK and Australia, and by efforts to harmonize regulatory *approaches* to licensing and guidance across CSA. However, we repeat the NCFAs recent submission to Finance Canada where we said -

The NCFAs urges the federal and provincial governments, as well as the provincial and territorial securities regulators, to work together with the private sector on a strategy:

- to reduce regulatory burden,
- to champion innovation,
- to make good use of proven tax and other incentives, and
- to ensure adequate data collection and analysis, as well as education and awareness.

3 April 2018