THE CANADIAN BAR ASSOCIATION
L'ASSOCIATION DU BARREAU CANADIEN

Cooperative Capital Markets Regulatory System – Draft Prospectus and Related Registration Exemptions

CANADIAN BAR ASSOCIATION
BUSINESS LAW SECTION

August 2018

500–865 Carling Avenue, Ottawa, ON, Canada K1S 5S8
tel/tél. 613 237-2925 • **tf/sans frais** 1-800 267-8860 • **fax/téléc**. 613 237-0185 • cba.org • info@cba.org

PREFACE

The Canadian Bar Association is a national association representing 36,000 jurists, including lawyers, notaries, law teachers and students across Canada. The Association's primary objectives include improvement in the law and in the administration of justice.

This submission was prepared by the Business Law Section, with assistance from the Legislation and Law Reform Directorate at the CBA office. The submission has been reviewed by the Law Reform Subcommittee and approved as a public statement of the Business Law Section.

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Cooperative Capital Markets Regulatory System – Draft Prospectus and Related Registration Exemptions

I. INTRODUCTION

The Business Law Section of the Canadian Bar Association (CBA Section) is pleased to comment on the Cooperative Capital Markets Regulatory System's draft prospectus and related registration exemptions under the *Capital Markets Act* published on May 8, 2018.

The CBA is a national association representing over 36,000 jurists, including lawyers, Quebec notaries, law teachers and students across Canada. Its primary objectives include improvement to the law and the administration of justice. The CBA Section comprise lawyers from across Canada who are experts in all areas of securities law including securities filings, initial public offerings, corporate governance, continuous disclosure, registrants, and other financial instruments including both transactional and regulatory practice and litigation.

II. NATIONAL INSTRUMENT 45-106 PROSPECTUS EXEMPTIONS

Generally, we are pleased to see that most of the revisions eliminate Ontario-specific exceptions, as this will simplify the instrument's application.

Specifically, section 2.6.1, which currently applies only in Ontario, will apply in all CMR jurisdictions. This is a positive step because it establishes consistency on the type of disclosure issuers should obtain to ascertain that a subscriber is a family, friend or business associate. However, the corresponding risk acknowledgement form and its requirement that certain sections be created (and signed) before the subscriber signs should be reconsidered. This approach makes it cumbersome to complete the form, and therefore a subscription agreement, in the proper order.

This instrument still contains inconsistent approaches between Canadian jurisdictions (including CMR jurisdictions) on "distributions outside of the jurisdictions" rules. For example, British Columbia and Ontario have different rules. Without a consistent approach, the analysis to determine if a prospectus exemption is available in a particular jurisdiction is uncertain. Determining if a prospectus exemption is required by an issuer in the local jurisdiction for distributions outside the local jurisdiction is often complex and uncertain.

Adopting a harmonized approach (at least in CMR jurisdictions) or offering additional guidance (including similar examples to the ones in Companion Policy 45-102CP) would significantly benefit capital market participants in Canada

III. CAPITAL MARKETS REGULATORY AUTHORITY (CMRA) REGULATION 45-501 PROSPECTUS AND REGISTRATION EXEMPTIONS

Part 1, Division 4 – Start-up Crowdfunding

The definition of "funding portal" in section 12 includes the phrase "*proposes* to facilitate online start-up crowdfunding distribution". The notion of *proposing* to facilitate is unclear and doesn't accord with the rest of the provisions – where the notion of *proposing* isn't contemplated. We suggest deleting "proposes to facilitate" from the definition of *funding portal*.

In section 13, the lead-in language refers to a trade "*in connection with* a start-up crowdfunding distribution". We suggest using more direct language such as "*that is* a start-up crowdfunding distribution".

In subsection 13(a), the negative tense construction is not consistent with other subsections of section 13. We suggest that this provision be stated in the positive to read "receives, prior to its first start-up crowdfunding distribution, confirmation in writing from the Chief Regulator of the following:"

In subsection 13(f), the reference to "client transactions" is unclear and should be defined.

In subsection 13(n), we question if "participating jurisdiction" is the appropriate reference, or whether this should be a reference to "CMR Jurisdiction", given the expanded jurisdictional scope by virtue of the definition "corresponding start-up crowdfunding exemption". This comment also applies to subsection 14(d).

In subsection 13(o), we suggest the reference to "risk warnings" should be stated in the singular rather than plural to reflect that there is a singular risk warning document (Form 45-501F3).

In subsection 13(q), we suggest adding "as soon as practicable", similar to subsections 13(b) and 14(i).

In subsection 13(r), we suggest adding "or causes to return", similar to subsection 13(s)(i)(A).

We suggest adding "or" at the end of subsection 13(s)(i)(B).

In subsections 13(s)(ii)(A), 13(s)(ii)(B) and 14(j), we suggest replacing the references to "distribution" with "start-up crowdfunding distribution" to be consistent with other provisions of this division.

In subsection 14(b)(ii), we suggest defining "Canadian securities legislation" as this term has no standardized meaning.

We suggest revising subsection 14(f) to state that the issuer group does not complete more than two start-up crowdfunding distributions in a calendar year, rather than stating as a restriction on the issuer group (where the source of the restriction is unclear).

In subsections 14(g) and (h), clause (h) should be listed before clause (g).

In subsection 14(i), we suggest a materiality qualification be added to the phrase "is no longer true" to align with analogous securities law requirements.

We suggest adding "and" at the end of subsection 14(p)(iii).

We suggest adding a final provision in section 14, similar to subsection 13(s)(i).

Part 1, Division 2 – Bonus or Finder's Fees

We suggest that the discussion of this exemption in the Companion Policy to Regulation 45-501 include a reference to the *Northwest Exemption* (e.g. BC Instrument 32-513 and Saskatchewan General Order 45-918 *Registration Exemption for Trades in Connection with Certain Prospectus-Exempt Distributions*) in light of the linkage between that registration exemption and the prospectus exemption set out in this division.

Part 2, Prospectus and Registration Exemptions Related to Provincial and Territorial Legislation

We wonder if a time frame is associated with the phrase "to be reviewed at a later date" (e.g. on the potential future adoption of the "investment dealer exemption"). If so, we suggest stating it. If no time frame exists, we suggest adding "during the next two years".

Similarly, we wonder if a time frame on whether to adopt the "financial institutions exemption" could be stated.

Part 3, Offering Memorandum Requirements

We note the following on the "voluntarily provided offering memorandum" provisions.

Section 98 of proposed Regulation 45-501 states that a voluntarily provided offering memorandum must be delivered to the Chief Regulator. As the Commentary document notes, this is a new requirement in British Columbia. It would be useful to clarify (either in the regulation or its companion policy), that these documents will not be made public as a result of delivery to the Chief Regulator, or at least that they will be kept confidential subject to access-to-information regimes. This confidentiality is particularly important for non-reporting issuers, who may be less likely to include full disclosure in their offering materials if the documents will be made public.

We recognize the term "delivered" (as opposed to "filed") may imply that the document will not be publicly available, making an assurance of confidentiality less relevant. However, British Columbia has historically made offering memoranda (used in exemptions) available on its website, irrespective of whether the issuer is a reporting issuer. Therefore, British Columbia issuers – and in particular non-reporting issuers – may have cause for concern that offering materials will be publicly available, absent an assurance to the contrary.

We are also concerned with section 100 of proposed Regulation 45-501, which states:

Description of rights in offering memorandum. If a seller delivers an offering memorandum to a prospective purchaser in connection with a distribution to which the rights referred to in section 122 of the Act apply, the rights must be described in the offering memorandum.

The Commentary document explains that this provision "requires a person who voluntarily delivers an offering memorandum to disclose that the investor has a right of action under the CMA if there is a misrepresentation in that offering memorandum", and that it is based on the applicable provision in OSC Rule 45-501.

However, section 122 of the draft *Capital Markets Act* does not appear to contemplate a "voluntarily filed offering memorandum". Rather, it refers only to a "prescribed disclosure document", which is not defined in the draft 45-501. Another proposed regulation may designate a voluntarily provided offering memorandum as a prescribed disclosure document, but this approach is unnecessarily circuitous and opaque. In contrast, the applicable section of OSC Rule 45-501 (5.2) clearly states that "the rights of action referred to in section 130.1 of the Act apply in respect of an offering memorandum delivered to a prospective purchaser."

We recommend amending section 100 to clarify that (pursuant to draft revised Regulation 11-501) the requirements of subsection 122(1)(a)(i) and 122(1)(b) of the *Capital Markets Act* apply

to a voluntarily provided offering memorandum (other than exemptions noted in the proposed new subsection 15(5) of Regulation 11-501). This appears to be the intent of Part V of the Commentary document.

Related Consequential Amendments to CMRA Regulation 11-501 Definitions, Procedure, Civil Liability and Related Matters

The Commentary document explains the revised section 15(1) of Regulation 11-501, and refers to the section's additional subsections. There does not appear to be a revised draft of Regulation 11-501 (since the original 2015 version which does not contain any subsections to section 15). We urge the Capital Markets Authority Implementation Organization to publish these for comment as soon as possible to have a complete understanding of Regulation 45-501, including section 122 discussed above. We are also interested to see what the undescribed provisions of a revised Regulation 11-501 will offer.

In part V of the Commentary document, a description of the future subsection 15(1) of Regulation 11-501 will exclude a "specified term sheet" from the definition of "offering memorandum", which appears to refer to voluntarily provided offering memoranda. This may not be necessary, given that section 98 of proposed Regulation 45-501 excludes "a specified term sheet" (as later defined) from the definition of "offering memorandum".

IV. CONCLUSION

We are grateful for the opportunity to participate in the consultation process on recent draft prospectus and related registration exemptions. We hope that our comments will contribute to the review of these important issues.