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Investor Crowdfunding Coming to Ontario

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The Ontario Securities Commission (“OSC”) announced last month (November 5, 2015) that it will join Saskatchewan, Manitoba, Quebec, New Brunswick and Nova Scotia in allowing businesses to participate in equity crowdfunding regulations. Provided all necessary Ministerial approvals are obtained, investor crowdfunding will finally come into force in Ontario and other jurisdictions on January 25, 2016.

Although accredited investors have been allowed to participate in equity crowdfunding since 2013, the new regulations will allow all investors to participate, with restrictions on how much they can invest, as well as limits on what the company can raise in order to limit risk. Under the OSC’s new rules, businesses will be required to offer such equity stakes through registered crowdfunding platforms. These crowdfunding platforms will be responsible for background checks and other due diligence on companies and investors.

Other key conditions of the new OSC regulations include offering non-complex securities such as common shares and non-convertible preference shares as well as issuers will be required to complete a Risk Acknowledgement Form and an offering document. In addition, businesses will have a limit of \$1,500,000 in capital they can raise and investment limits for investors will be \$2,500 per investment and in Ontario, \$10,000 total in a calendar year per investor. Accredited investors are limited to \$25,000 per investment and in Ontario, \$50,000 in total per calendar year.

Although crowdfunding has many benefits including faster access to funding for start-ups and businesses, there are a few issues a business should consider prior to using the crowdfunding exemption.

Some of the issues to consider are:

- **Will there be too many shareholders?** Crowdfunding allows access to capital by raising money through many small subscribers. Consequently, businesses using this exemption quickly acquire a large number of shareholders which can have several implications. For example, a potential buyer may not be able to rely on the take-over bid exemptions contained in Canadian Securities law for non-reporting issuers. Therefore, such business may become a less appealing acquisition target. Other implications include the requirement of a proxy circular if over a certain number of shareholders, difficulty passing written shareholders’ resolutions and a more onerous day to day administrative burden as a result of the large number of shareholders (securities transfers, notices, inquiries and other investor relations matters).
- **What are the costs of crowdfunding?** As portals will be necessary to use this exemption, the costs of funding the portals will likely be passed on to the businesses using these portals.



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- **What are some other concerns of crowdfunding?** The regulations contemplate that investors will have a statutory right of damages or rescission in the event of misrepresentation in the required information statement. Further, Canadian securities regulators will be able to review all disclosure provided by an issuer and as a result the issuer may spend significant amounts of time dealing with issues raised by regulators instead of focusing that time on building their business. Also, audited financial statements may be required and could result in significant additional costs for such businesses.
- **What about future financings?** Use of crowdfunding could potentially make future financings more challenging. Future investors will be concerned about the business' compliance with securities law. As a result, due diligence for such financings may be more costly and time consuming.

Crowdfunding has many benefits but also has costs and obligations. Each business will have to weigh the pros and cons of the crowdfunding exemption in order to determine if this method of raising capital is best suited for them.

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