

CSA Notice of Consultation

Amendments Relating to the Offering Memorandum Prospectus Exemption

Draft Regulation to amend Regulation 45-106 respecting Prospectus Exemptions

Draft Amendments to Policy Statement to Regulation 45-106 respecting Prospectus Exemptions

September 17, 2020

Introduction

The Canadian Securities Administrators (the **CSA** or **we**) are publishing for a 90-day comment period Draft *Regulation to amend Regulation 45-106 respecting Prospectus Exemptions* (**Regulation 45-106**) and Draft Amendments to *Policy Statement to Regulation 45-106 respecting Prospectus Exemptions* (the **Draft Amendments**).

The Draft Amendments are published with this notice. This notice will be available on the websites of CSA jurisdictions including:

www.bsc.bc.ca
www.albertasecurities.com
www.fcaa.gov.sk.ca
www.mbsecurities.ca
www.osc.gov.on.ca
www.lautorite.qc.ca
www.fcnb.ca
nssc.novascotia.ca

Substance and Purpose

The Draft Amendments set out new disclosure requirements for issuers that are engaged in “real estate activities” and those issuers that are “collective investment vehicles”. Both terms are new definitions in Regulation 45-106. As further discussed below, many issuers utilizing the OM Exemption (as defined below) are issuers that meet these definitions. The new requirements are intended to set out a clear disclosure framework for these issuers, giving them greater certainty as to what they must disclose, and resulting in better information for investors.

In addition, the Draft Amendments include a number of proposed general amendments (the **General Amendments**), which are meant to clarify or streamline parts of Regulation 45-106 or improve disclosure for investors.

Where the Draft Amendments are to a form for an offering memorandum, they are to Form 45-106F2 *Offering Memorandum for Non-Qualifying Issuers* (**Form 45-106F2**).

Background

The offering memorandum prospectus exemption found in section 2.9 of Regulation 45-106 (the **OM Exemption**) was originally designed as a small business financing tool to help early stage and small businesses raise capital from a large pool of investors without having to comply with the more costly prospectus regime. It was expected to be used by relatively simple issuers for relatively small amounts of capital, prior to issuers becoming reporting issuers.

In practice, the use of the OM Exemption has evolved differently. To a significant extent, larger and more complex issuers than those originally envisioned are using it. In addition, issuers using the OM Exemption are often engaged in specific activities, such as real estate ownership or development, or acting as a type of collective investment vehicle carrying out mortgage lending or making other investments.

Based on an analysis by CSA staff of Canada-wide data from reports of exempt distribution for issuers using the OM Exemption in 2017, approximately 40% of the issuers had total assets of \$100 million or more. In addition, 17% of issuers reported their industry as real estate, and approximately 43% were issuers that might, depending on their purpose and investment objectives, be collective investment vehicles under the Draft Amendments.

Compliance reviews have also indicated that under the current OM Exemption requirements, it can be unclear to issuers what disclosure is required in order to provide investors with sufficient information. By tailoring the disclosure to the issuer's industry, and clarifying other requirements, issuers should be able to more easily determine what is required to be included in their offering memorandum.

Summary of the Draft Amendments

Issuers Engaged in Real Estate Activities

The Draft Amendments include the new defined term “real estate activities”. Issuers engaged in real estate activities would be subject to new requirements, including:

- Providing an independent appraisal of an interest in real property to the purchaser if
 - the issuer has acquired or proposes to acquire an interest in real property from a related party (**Related Party**), as that term is defined in Regulation 45-106,
 - a value for an interest in real property is disclosed in the offering memorandum, or
 - the issuer intends to spend a material amount of the proceeds of the offering on an interest in real property.

- Completing new Schedule 1 *Additional Disclosure Requirements for an Issuer Engaged in Real Estate Activities* (**Schedule 1**) to Form 45-106F2, which includes:
 - Disclosure relevant to issuers that are developing real property, such as a description of the approvals or permissions required, and milestones of the project.
 - Disclosure relevant to issuers that own and operate developed real property, such as the age, condition and occupancy level of the real property.
 - Disclosure of penalties, sanctions, bankruptcy, insolvency and criminal or quasi-criminal convictions for parties other than the issuer, such as a party acting as developer.
 - Disclosure of any purchase and sale history of the issuer's real property with a Related Party, so investors can better evaluate transactions involving Related Parties.

We note that Schedule 1 would not apply to real property that when taken together would not be significant to a reasonable investor. This exception is intended to ensure that issuers are not subject to an undue disclosure burden.

We think the Draft Amendments as they relate to issuers engaged in real estate activities are necessary because as noted, research indicates that a significant proportion of issuers utilizing the OM Exemption are engaged in real estate activities. We think more specific disclosure about the real property or development plans for the real property is needed for investors, and we also think that these issuers will benefit from the greater certainty provided by a disclosure framework tailored for them.

Issuers that are Collective Investment Vehicles

The Draft Amendments also include the new defined term “collective investment vehicle”. A collective investment vehicle is defined as an issuer whose primary purpose is to invest money provided by its security holders in a portfolio of securities. This definition would include issuers that hold portfolios of mortgages, other loans, or receivables. To the extent they are permitted to use the OM Exemption, the definition would also include investment funds.

Issuers that are collective investment vehicles would be required to complete new Schedule 2 *Additional Disclosure Requirements for an Issuer That is a Collective Investment Vehicle* to Form 45-106F2, which includes:

- A description of the issuer's investment objectives.
- Disclosure of penalties, sanctions, bankruptcy, insolvency and criminal or quasi-criminal convictions for persons involved in the selection and management of the investments.
- Disclosure of information regarding the portfolio.
- Disclosure regarding the performance of the portfolio.

We think the Draft Amendments as they relate to issuers that are collective investment vehicles are necessary because as noted, research indicates that a large proportion of issuers utilizing the OM Exemption could under the Draft Amendments be collective investment vehicles. We think investors need more information, including about the party making the investment decisions,

how the investments are chosen and the composition and performance of the portfolio. As with issuers engaged in real estate activities, we think issuers that would be collective investment vehicles will also benefit from the greater certainty provided by a disclosure framework tailored for them.

General Amendments

The General Amendments include:

- Making the provisions in the OM Exemption that deal with the standard of disclosure for an offering memorandum and amending an offering memorandum clearer and more user-friendly for issuers and investors.
- Requiring that the filed copy of an offering memorandum allow for the searching of words electronically. This change is intended to make reading and reviewing offering memorandums more efficient for all recipients.
- With respect to Form 45-106F2:
 - The addition of several more disclosure items to the cover page to highlight those matters for investors.
 - Enhanced disclosure where a material amount of the proceeds of the offering will be transferred to another issuer that is not the issuer's subsidiary, or a material amount of the issuer's business is carried out by another issuer that is not the issuer's subsidiary. This is intended to give investors better disclosure as to arrangements of this nature and the ultimate use of the offering proceeds.
 - Disclosure of any purchase or sale history of any business or asset of the issuer's (excluding real property) with a Related Party, so investors can better evaluate transactions involving Related Parties.
 - The addition of Related Parties that receive compensation to the compensation disclosure and securities ownership table.
 - For item 3.3, adding disclosure of criminal or quasi-criminal convictions. This is consistent with disclosure requirements for more recently developed prospectus exemptions.
 - The addition of disclosure regarding fees or limitations with respect to redemption or retraction rights.
 - Further disclosure regarding redemption or retraction, including requests made to the issuer, requests fulfilled by the issuer including the price paid and the source of the funds, and outstanding requests.
 - A new requirement to disclose the source of funds for dividends or distributions paid that exceeded cash flow from operations.
 - Reference to the requirements of *Regulation 33-105 respecting Underwriting Conflicts*.
 - New cautionary disclosure for instances where expert reports, statements or opinions are included in an offering memorandum and there is no statutory liability against the expert.
 - A new requirement to amend an offering memorandum to include an interim financial report for the most recently completed 6 month interim period when a distribution of securities under an offering memorandum is ongoing.

- Other amendments intended to clarify or streamline existing provisions or provide improved disclosure.

The General Amendments are closely related to issues that we have seen in our ongoing review and compliance work regarding offering memorandums.

Other matters included in or related to the Draft Amendments

In addition, the Draft Amendments also include changes to Form 45-106F4 *Risk Acknowledgement*, which is the required form of risk acknowledgement for investors purchasing a security under the OM Exemption. These changes are to make the form more understandable and useful to investors, and are consistent with recent amendments to risk acknowledgement forms required in connection with other prospectus exemptions.

We note that if the Draft Amendments are enacted in the future, some of the guidance in Multilateral CSA Staff Notice 45-309 *Guidance for Preparing and Filing an Offering Memorandum under Regulation 45-106 respecting Prospectus and Registration Exemptions (SN 45-309)* may no longer apply or may need to be revised. Consequently, we expect that if in the future the Draft Amendments or some version of them is enacted, we would publish a revised SN 45-309 in conjunction with the effective date of those amendments.

Impact on Investors

The Draft Amendments would give investors enhanced disclosure, and where the issuer is engaged in real estate activities, or is a collective investment vehicle, the investor would receive disclosure that is more tailored to that kind of issuer. We anticipate that this enhanced and tailored disclosure would provide investors with better information, enabling them to make more informed investment decisions.

Local Matters

An annex is being published in any local jurisdiction that is proposing related changes to local securities laws, including local notices or other policy instruments in that jurisdictions. It may also include additional information that is relevant to that jurisdiction only.

Request for Comments

We welcome your comments on the Draft Amendments.

Please submit your comments in writing on or before December 16, 2020. If you are not sending your comments by email, please send a CD containing the submissions (in Microsoft Word format).

Address your submission to all of the CSA as follows:

British Columbia Securities Commission
Alberta Securities Commission
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
Office of the Superintendent of Securities, Service NL
Financial and Consumer Services Commission, New Brunswick
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island
Nova Scotia Securities Commission
Office of the Yukon Superintendent of Securities
Northwest Territories Office of the Superintendent of Securities
Nunavut Securities Office

Deliver your comments only to the addresses below. Your comments will be distributed to the other CSA jurisdictions.

M^e Philippe Lebel
Corporate Secretary and Executive Director, Legal Affairs
Autorité des marchés financiers
Place de la Cité, tour Cominar
2640, boulevard Laurier, bureau 400
Québec (Québec) G1V 5C1
Fax : 514 864-8381
consultation-en-cours@lautorite.qc.ca

Gordon Smith
Associate Manager, Legal Services, Corporate Finance
British Columbia Securities Commission
1200 - 701 West Georgia Street
P.O. Box 10142, Pacific Centre
Vancouver, British Columbia V7Y 1L2
604 899-6656
gsmith@bcsc.bc.ca

Steven Weimer
Manager, Compliance, Data & Risk
Corporate Finance – Compliance, Data & Risk
Alberta Securities Commission
Suite 600, 250 – 5th Street SW
Calgary, Alberta T2P 0R4
403 355-9035
steven.weimer@asc.ca

The Secretary
Ontario Securities Commission
20 Queen Street West
22nd Floor
Toronto, Ontario M5H 3S8
Fax: 416-593-2318
comments@osc.gov.on.ca

We cannot keep submissions confidential because securities legislation in certain provinces requires publication of the written comments received during the comment period. All comments received will be posted on the websites of each of the Alberta Securities Commission at www.albertasecurities.com, the Autorité des marchés financiers at www.lautorite.qc.ca and the Ontario Securities Commission at www.osc.gov.on.ca. Therefore, you should not include personal information directly in comments to be published. It is important that you state on whose behalf you are making the submission.

Questions

Please refer your questions to any of the following:

Autorité des marchés financiers
Alexandra Lee
Senior Policy Adviser
Corporate Finance
514 395-0337, ext. 4465
alexandra.lee@lautorite.qc.ca

Najla Sebaai
Senior Policy Adviser
Corporate Finance
514 395-0337, ext. 4398
najla.sebaai@lautorite.qc.ca

British Columbia Securities Commission
Gordon Smith
Associate Manager, Legal Services, Corporate Finance
604 899-6656
gsmith@bcsc.bc.ca

Eric Pau
Senior Legal Counsel, Legal Services, Corporate Finance
604 899-6764
epau@bcsc.bc.ca

Alberta Securities Commission

Lanion Beck
Senior Legal Counsel
Corporate Finance
403 355-3884
lanion.beck@asc.ca

Alaina Booth
Senior Capital Markets Analyst
Corporate Finance – Compliance, Data & Risk
403 355-6293
alaina.booth@asc.ca

Steven Weimer
Manager, Compliance, Data & Risk
Corporate Finance – Compliance, Data & Risk
403 355-9035
steven.weimer@asc.ca

Financial and Consumer Affairs Authority of Saskatchewan

Heather Kuchuran
Director, Corporate Finance
306 787-1009
heather.kuchuran@gov.sk.ca

Manitoba Securities Commission

Wayne Bridgeman
Deputy Director, Corporate Finance
204 945-4905
wayne.bridgeman@gov.mb.ca

Financial and Consumer Services Commission, New Brunswick

Jason Alcorn
Senior Legal Counsel
506 643-7857
jason.alcorn@nbsc-cvmnb.ca

Nova Scotia Securities Commission

Peter Lamey
Legal Analyst
Corporate Finance
902 424-7630
peter.lamey@novascotia.ca

Abel Lazarus
Director, Corporate Finance
902 424-6859
abel.lazarus@novascotia.ca