Regulating Peer-to-Business Lending in Canada

by

Lucas Dorn

B.A. (Hons.), University of Toronto, 2008

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Approval

Name: Lucas Dorn
Degree: Master of Public Policy
Title: Regulating Peer-to-Business Lending in Canada
Examinining Committee: Chair: Doug McArthur
Professor

Dominique Gross
Senior Supervisor
Professor

Nancy Olewiler
Supervisor
Professor

Josh Gordon
Internal Examiner
Assistant Professor

Date Defended/Approved: April 9, 2019
Abstract

Peer-to-Business Lending (P2BL) is a sub-set of the Financial Technology (Fintech) sector that allows investors to lend money to businesses through online portals run by a third party. P2BL provides a potential alternative source of financing for Canadian small businesses that are underserved by traditional financial institutions. However, Canada’s adoption of P2BL, measured in values of loans issued, significantly lags many of its peers who have developed mature online lending industries. This study focuses on Canadian securities regulation applicable to P2BL to identify issues with the current regulatory regime. A case study methodology is used to examine the United Kingdom, Singapore, and Australia to identify potential policy options to implement in Canada. These policy options are analyzed to determine responsible ways encourage innovation and growth in the Canadian P2BL sector.

Keywords: Fintech; peer-to-business lending; regulation; Canada
To my mom. In life and now, your love and support is always the tailwind I need.
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<th>Acronym</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>AFS</td>
<td>Australian Financial Services</td>
</tr>
<tr>
<td>AMF</td>
<td>Autorité des Marchés Financiers</td>
</tr>
<tr>
<td>ASC</td>
<td>Alberta Securities Commission</td>
</tr>
<tr>
<td>ASIC</td>
<td>Australian Securities and Investments Commission</td>
</tr>
<tr>
<td>BCSC</td>
<td>British Columbia Securities Commission</td>
</tr>
<tr>
<td>CCMR</td>
<td>Cooperative Capital Markets Regulatory System</td>
</tr>
<tr>
<td>CSA</td>
<td>Canadian Securities Administration</td>
</tr>
<tr>
<td>DFAP</td>
<td>Digital Finance Advisory Panel</td>
</tr>
<tr>
<td>DRR</td>
<td>Digital Regulatory Reporting</td>
</tr>
<tr>
<td>FAA</td>
<td>Financial Advisers Act</td>
</tr>
<tr>
<td>FCA</td>
<td>Financial Conduct Authority</td>
</tr>
<tr>
<td>Fintech</td>
<td>Financial Technology</td>
</tr>
<tr>
<td>FTIG</td>
<td>Fintech and Innovation Group</td>
</tr>
<tr>
<td>GDP</td>
<td>Gross Domestic Product</td>
</tr>
<tr>
<td>IPRU(INV)</td>
<td>Interim Prudential Sourcebook for Investment Businesses</td>
</tr>
<tr>
<td>MAS</td>
<td>Monetary Authority of Singapore</td>
</tr>
<tr>
<td>MI</td>
<td>Multi-Lateral Instrument</td>
</tr>
<tr>
<td>MOU</td>
<td>Memorandum of Understanding</td>
</tr>
<tr>
<td>NI</td>
<td>National Instrument</td>
</tr>
<tr>
<td>OECD</td>
<td>Organization for Economic Cooperation and Development</td>
</tr>
<tr>
<td>OSC</td>
<td>Ontario Securities Commission</td>
</tr>
<tr>
<td>OSFI</td>
<td>Office of Superintendent of Financial Institutions</td>
</tr>
<tr>
<td>P2BL</td>
<td>Peer-to-Business Lending</td>
</tr>
<tr>
<td>P2PL</td>
<td>Peer-to-Peer Lending</td>
</tr>
<tr>
<td>PDN</td>
<td>Payment Dependent Notes</td>
</tr>
<tr>
<td>SCC</td>
<td>Supreme Court of Canada</td>
</tr>
<tr>
<td>SFA</td>
<td>Securities and Futures Act</td>
</tr>
<tr>
<td>SME</td>
<td>Small and Medium Enterprises</td>
</tr>
<tr>
<td>SYSC</td>
<td>Senior Management, Arrangements, Systems and Control</td>
</tr>
</tbody>
</table>
Executive Summary

This study analyzes the impediments to growth of the Canadian Peer-to-Business Lending (P2BL) sub-sector of Fintech. P2BL is a form of lending-based crowdfunding where an online funding portal acts as an intermediary by vetting borrowers and running an online portal that connects business borrowers and lenders to fund small business loans. P2BL is a potential alternative source of credit for small businesses who are underserved by traditional financial institutions that currently dominate the small business loan market. However, Canada significantly lags behind other developed countries in P2BL sector maturity partially due to its regulatory system.

I use a case study methodology to review three case study countries: The United Kingdom, Australia, and Singapore. All three are global leaders in terms of government action in response to Fintech. They have approached Fintech in similar ways by establishing specific Fintech regulatory bodies and regulatory sandboxes. Specific to P2BL there are key differences in their regulatory approaches. The UK created new P2BL specific rules that modify the existing regulatory framework governing P2BL operators’ actions and structure. Conversely, Singapore relies on existing exemptions from prospectus requirements that have been refined to accommodate P2BL. Australia does not make special accommodations for P2BL, which is generally subject to the same requirements as traditional financial firms.

Based on the case study analysis, I identify three potential policy options to implement in Canada. First, create a P2BL specific national regulation issued through the two national-level bodies, the Canadian Securities Administration (CSA) and Co-Operative Market Regulatory System (CCMR). Second, alter the functioning of the CSA’s regulatory sandbox by providing more dedicated staffing and resources. Third, institute a referral program to P2BL funding portals when a loan is rejected by a traditional financial institution. I evaluate the policy options along four criteria: effectiveness, cost, implementation complexity, and stakeholder support. The policy recommendation is to implement all three options in order to grow both supply and demand factors needed for P2BL industry growth.
Chapter 1.

Introduction

Fintech, the application of internet-based technology to deliver existing financial services, is a growing multi-billion dollar market globally, yet its adoption and prevalence in Canada lags behind other industrialized countries to a significant degree. Fintech’s potential as an economic driver lies in its ability to deliver traditional financial services more efficiently and conveniently. I study the Fintech sub-sector of lending, specifically peer-to-business lending (P2BL) for small businesses, to illustrate the complexity and difficulty of applying existing Canadian regulatory frameworks to new business models made possible by Fintech.

Chapters 2 to 5 delve further into Canadian Fintech with a focus on P2BL regulation and its related policy problem in Canada. Chapter 6 lays out the case study evaluative framework and criteria for the primary case study methodology. Chapter 7 analyzes the United Kingdom, Australia, and Singapore and reviews the secondary methodology findings. The use of a single regulatory body, issuance of standalone P2BL regulations, dedicated staffing to Fintech specific regulatory bodies and initiatives, and the degree of regulation prescriptiveness are key characteristics. Chapter 8 defines the four criteria of effectiveness, cost, implementation complexity, and stakeholder support through which policy options are evaluated. Chapter 9 analyzes the three identified policy options. First, create P2BL specific regulations that are proportional to potential risk. Second, the provision of dedicated resources to the Canadian Securities Administration’s existing Fintech initiatives. Third, to increase P2BL demand and awareness, institute a national level bank referral program where traditional institutions provide lists of alternative lenders to small businesses who have their loan applications rejected. I recommend implementation of all policy options to address supply and demand factors in the Canadian P2BL sector. Chapter 10 concludes with areas of future research as a result of the policy analysis.
Chapter 2.

Small Business Financing in Canada

Canadian small businesses, defined as private firms employing less than 100 paid employees, are an important contributor to Canada’s economy. They account for at least 30%\(^1\) of national GDP (BC Stats, 2017) and employ close to 8.2 million Canadians representing approximately 70% of the total private workforce (Innovation, Science, and Economic Development, 2016). A key driver of small businesses’ viability is their access to financing for business activities (Amarjit Gill & Nahum Biger, 2012).

Two recent surveys of small and medium enterprises (SMEs) show a relationship between the size of the SME, in terms of paid employees, and the approval rates for debt financing from traditional sources of lending (Innovation, Science, and Economic Development, 2016; Industry Canada, 2015). Table 1 shows that domestic banks are the largest source of SME financing, whose market share of the SME loan market increases along with SME employee count. The dominance of loan financing by domestic banks is unsurprising given that the major Canadian banks control an estimated 93% of the banking sub-sector\(^2\) (Department of Finance Canada, 2016). Bank concentration is not inherently undesirable for SME financing as long as the credit markets function efficiently and loan rejection rates remain small. However, companies with less than 100 employees are turned down for loans 15%-20% of the time compared to 4% for medium size enterprises, who have between 100-499 paid employees (Industry Canada, 2015). A smaller 2016 survey of 2,100 SMEs found similar rates of approval and rejection for debt financing applications by small businesses (Figure 1). There are prudent reasons for small businesses having their loan applications rejected. However, small businesses’ creditworthiness is difficult for lenders to ascertain given the lack of available public information (Liang Han, Stuart Fraser, & David J. Storey, 2009). The uncertainty created by this information asymmetry between small businesses and lenders is compounded by

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\(^1\) GDP contribution is based on BC Stats definition of small business as private businesses with less than 50 employees. Statistics Canada broadens their definition to include businesses with less 100 employees. Contributions to GDP may be underestimated due to firms considered for calculation.

\(^2\) The major Canadian banks considered are: Royal Bank of Canada, Scotiabank, Bank of Montreal, TD Canada Trust, CIBC.
the relatively small loan amounts being requested. The cost of processing and evaluating loans is completed manually and on a case-by-case basis by traditional financial institutions. The loan evaluation costs are similar for banks regardless of loan amount requested (Karen Gordon Mills & Brayden McCarthy, 2016; Competition Bureau Canada, 2017). The lack of information on the small business borrower and relatively high cost of the loan evaluation creates more barriers to financing for small businesses relative to larger firms. Another measure of small business barriers is the rate of discouraged borrowers, which are small businesses that require yet do not apply for credit. A recent Canadian credit condition survey found that the top reasons given by Canadian small businesses for not seeking financing, aside from financing not being needed, were the belief their request would be unsuccessful (4%) or that the application for credit is too difficult or time consuming (4%) (Innovation, Science, and Economic Development, 2017).

Table 1. Principal Source of Canadian Small Business Debt Financing by Firm Size

<table>
<thead>
<tr>
<th>Number of Employees</th>
<th>Domestic chartered bank</th>
<th>Credit union/caisses populaires</th>
<th>Government institution</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 to 4 employees</td>
<td>69.0</td>
<td>27.6</td>
<td>5.8</td>
</tr>
<tr>
<td>5 to 19 employees</td>
<td>70.1</td>
<td>24.7</td>
<td>7.2</td>
</tr>
<tr>
<td>20 to 99 employees</td>
<td>78.3</td>
<td>20.1</td>
<td>5.2</td>
</tr>
</tbody>
</table>

Source: Industry Canada (2015)
In summary, the financing rejection rate coupled with the dominance of Canadian banks implies there are few formal options for small businesses once they are turned down by traditional sources of financing (Competition Bureau Canada, 2017). Other credit indicators, such as interest rates and business risk premiums, point towards a stable credit environment for Canadian small businesses in recent years (OECD, 2018). However, relative to larger businesses, small businesses in Canada are underserved by the financing options available. Consequently, there is a market potential for alternative financing sources serving these small businesses.
Chapter 3.

Financial Technology and Peer-to-Peer Lending

The following chapter defines financial technology and what type of services it encompasses. Global adoption rates and investments are compared to Canada in order to demonstrate Canada’s slow pace of acceptance of Fintech. A sub-set of Fintech, peer-to-business lending, is described in more detail. The last section focuses on the benefits and potential importance of the P2BL model.

3.1. Financial Technology

Financial technology, or Fintech, is where new market entrants apply new technology to enhance and innovate the delivery of traditional financial services typically provided by incumbent firms, such as banks and credit unions. One of the main benefits of Fintech innovation is that it eliminates the need for a financial middleman in some way. By offering services direct to users, Fintech firms can save users the cost financial intermediary fees. This process is known as financial disintermediation. Financial intermediary fees are not trivial with one estimate pegging these costs at 2% of GDP for selected developed countries\(^3\) (Meyer Aaron, Francisco Rivadeneyra, & Samantha Sohal, 2017). Other benefits of Fintech include: creating a more competitive marketplace, greater price transparency, and allowing products to be built on non-proprietary IT systems that could increase accessibility and resiliency (Competition Bureau Canada, 2017).

Fintech firms attracted close to $58 billion in capital investment globally in the first six months of 2018 alone. (KPMG, 2018; KPMG, 2018a). These amounts contrast with Canadian specific Fintech investment that saw $1 billion dollars invested from 2010-2016 (Charlotte Watson & Alex LaPlante, 2018). Canada’s laggard status in Fintech is also evident in its user adoption rates. Despite adoption rates increasing globally, currently estimated at 33% global penetration, Canada lags behind with only 8.2% estimated adoptions rates (Ernst and Young, 2017). Reasons cited for Canada’s low

\(^3\) United States, France, Germany, United Kingdom
adoption of Fintech are that Canadian Fintech start-ups, relative to other countries, do not have the same access to technical and business talent, local venture capital funding, and/or clear regulatory requirements (Toronto Financial Services Alliance, 2017). On the demand side, Canadians are loyal to existing financial institutions due primarily to limited choices and banks having avoided the worst of the 2009 recession (Charlotte Watson & Alex LaPlante, 2018; Competition Bureau Canada, 2017).

Fintech is potentially a multi-billion dollar industry that Canada is well-positioned to benefit from due to the importance and strength of the existing Canadian financial sector. One of the ways Fintech can serve as a future economic driver is by augmenting the availability of credit for small businesses through the availability of alternative financing.

### 3.2. Crowdfunding: Peer-to-Business Lending

Crowdfunding is where funds are pledged online by users, acting as lenders or donors, to finance a higher value end goal. This end goal can be categorized into three main areas based on the intended use of offered capital: donation, rewards, and investment (Rainer Lenz, 2016). Figure 2 illustrates the different crowdfunding models with a focus on the investment sub-category of lending based activities. Most of these lending activities apply to both business and personal loans.

![Crowdfunding Breakdown by End Use of Raised Capital](image)

**Figure 2.** Crowdfunding Breakdown by End Use of Raised Capital

Source: Rainer Lenz (2016), Ziegler et al. (2018)
The scale of Fintech lending-related activities is increasing in Canada. From 2014-2017, loans issued increased from $85.1 million to $867.58 million (Tania Ziegler et al., 2018). However, Table 2 shows that the growth of the industry is clearly uneven across sub-categories indicating differing levels of market maturity. Specifically, Peer-to-Business Lending (P2BL) in Canada ranks near the bottom in originated loans within lending-based crowdfunding. Despite the low volume, I focus on the Canadian P2BL sub-sector of crowdfunding, highlighted in Figure 2 above, as the basis for my study for three primary reasons. First, P2BL is an additional source of potential financing for small businesses in Canada that are underserved by traditional financial institutions. Second, P2BL illustrates the difficulties that new financial technologies pose to existing regulatory frameworks. Third, the study requires a narrow focus because each sub-category of crowdfunding presents unique challenges.

Table 2. Lending Crowdfunding Volume in Canada by Sub-Category 2014-2017

<table>
<thead>
<tr>
<th>Rank Based on 2017 Volume</th>
<th>Type of Crowdfunding</th>
<th>Lenders</th>
<th>Borrowers</th>
<th>Canadian Market Volume (Millions $ CND)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>2017</td>
</tr>
<tr>
<td>1</td>
<td>Balance Sheet Business Lending</td>
<td>Platform</td>
<td>Business</td>
<td>$494.26</td>
</tr>
<tr>
<td>2</td>
<td>Balance Sheet Property Lending</td>
<td>Platform</td>
<td>Business and Consumer</td>
<td>$115.67</td>
</tr>
<tr>
<td>3</td>
<td>Marketplace/P2P Consumer Lending</td>
<td>Individuals and/or Institutions</td>
<td>Consumer</td>
<td>$94.12</td>
</tr>
<tr>
<td>4</td>
<td>Donation-based Crowdfunding</td>
<td>Individuals and/or Institutions</td>
<td>Business and Consumer</td>
<td>$88.59</td>
</tr>
<tr>
<td>5</td>
<td>Reward-based Crowdfunding</td>
<td>Individuals and/or Institutions</td>
<td>Business and Consumer</td>
<td>$22.94</td>
</tr>
<tr>
<td>6</td>
<td>Equity-based Crowdfunding</td>
<td>Individuals and/or Institutions</td>
<td>Business</td>
<td>$13.83</td>
</tr>
<tr>
<td>7</td>
<td>Balance Sheet Consumer Lending</td>
<td>Platform</td>
<td>Consumer</td>
<td>$11.57</td>
</tr>
<tr>
<td>8</td>
<td>Real Estate Crowdfunding</td>
<td>Individuals and/or Institutions</td>
<td>Business and Consumer</td>
<td>$11.50</td>
</tr>
<tr>
<td>Rank Based on 2017 Volume</td>
<td>Type of Crowdfunding</td>
<td>Lenders</td>
<td>Borrowers</td>
<td>Canadian Market Volume (Millions $ CND)</td>
</tr>
<tr>
<td>--------------------------</td>
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<td>-----------</td>
<td>-------------------------------------</td>
</tr>
<tr>
<td>10</td>
<td>Marketplace/P2P Property Lending</td>
<td>Individuals and/or Institutions</td>
<td>Business and Consumer</td>
<td>2017: $6.00, 2016: $5.00, 2015: $-, 2014: $-</td>
</tr>
</tbody>
</table>

Source: (Tania Ziegler et al., 2018)

P2BL is where business borrowers and lenders match using an online marketplace platform administered and operated by a third party known as a funding portal. Lenders are institutions, accredited investors, and/or retail investors. Funding portals, typically a technology start-up company, vet a business’ loan request based on internal risk management frameworks and ascribe a risk rating and corresponding interest rate for the loan. Once vetted and borrowers agree to the conditions, loans are posted to the online marketplace. Lenders are matched to loans by the platform or can chose specific loans to fund. Depending on the funding portal’s business model loans are fully funded by a handful of investors, typically large investors, or loans are funded in small increments by many lenders. Regardless of model, lenders receive a posted interest rate that is paid out, typically, at monthly intervals as the loan is repaid by the borrower (Rainer Lenz, 2016). Funding portals charge loan origination and servicing fees to lenders and borrowers. There are several business model variations on this core concept. Important variations to the P2BL business model are whether: retail investors are permitted to invest, the platform itself distributes loans and repayments, there is a limit on loan value, and lenders choose the loan they fund.

The promise of P2BL is that it provides another, potentially cheaper, avenue for Canadian small businesses to receive debt financing. P2BL takes shorter periods of time to raise the capital, the cost of the loan application process is low for borrowers, it is

---

4 Retail investors are everyday individuals who are not professional investors.
convenient for lenders and borrowers alike, and it provides investors a better rate of return than other fixed income options available (Rainer Lenz, 2016). In terms of risk for lenders, the effect of having many lenders reviewing borrowers’ loan requests appears to decrease the traditional information asymmetry between the lender and borrower\textsuperscript{5} (Kgoroeadira, Burke, & van Stel, 2019). Loans that funding portals rate as less risky, and give a lower interest rate, are more likely to be successful, which indicates less risk seeking behaviour on the part of lenders (Kgoroeadira, Burke, & van Stel, 2019; Emekter, Tu, Jirasakuldech, & Lu, 2015; Carlos Serrano-Cinca, Begoña Gutiérrez-Nieto, & Luz López-Palacios, 2015).

There are several risks associated with P2BL. First, high-risk borrowers could potentially be overrepresented leading to higher risk of default (Rainer Lenz, 2016). Second, investors may not have the ability or knowledge to adequately analyze financial statements and make a prudent financial decision on whether and how to lend money (Competition Bureau Canada, 2017). Third, P2BL funding portals are relatively new and have not been tested by a significant recession or market pull backs so it is unclear how funding portals, borrowers, and lenders would respond (Competition Bureau Canada, 2017). Lastly, concern regarding the potential for business fraud has gained more attention in recent years due, in part, to several high profile scandals. China in particular saw a wave of P2P lending platforms fail or engaging in fraudulent activity, such as Ponzi schemes. Importantly, the Chinese P2P lending industry developed largely without regulation or proper oversight (Wang, Shen, & Huang, 2016). Examples of fraud in other countries where regulations and oversight mechanisms are in place are more limited, but do exist. The use of data analytics (J. Xu, D. Chen, & M. Chau, 2016), lenders evaluation of funding portals’ characteristics, and minimum funding portal capital requirements are potential avenues to detect or prevent fraud in certain circumstances (Wang, Shen, & Huang, 2016). The importance of regulation and ensuring transparency in funding portals’ behaviour and risk management are essential to avoid these concerns in the Canadian context.

In summary, Fintech benefits consumers through more efficient and lower cost services made possible, primarily, by financial disintermediation. Crowdfunding is an example of this process where individuals and institutions can directly provide capital to

\textsuperscript{5} Based on US data.
businesses, causes, or individuals. A specific example is P2BL online marketplaces where small businesses can have loans financed directly by individuals or institutions. P2BL is a potential alternative source of funding for small businesses that have few other formal options for financing.
Chapter 4.

P2BL Regulation in Canada

Loan agreements stemming from P2BL models are known as ‘payment dependent notes’ (PDN), a debt-based financial security (Ontario Securities Commission, 2019). The PDN is distributed to lenders (investors) by the funding portal to require borrowers (businesses) to repay the lenders’ capital (Ontario Securities Commission, 2019). In essence, a PDN is a loan agreement between a business and investor which constitutes indebtedness of the former to the latter in provincial securities regulation (Ontario Securities Commission, 2009). Financial securities are regulated at the provincial level. Each province and territory enacts its own securities legislation that empowers a provincial regulatory body to supervise its capital markets. Consequently, any firm, including P2BL firms, seeking to operate nationally is subject to approval through each province’s securities regulator. Section 4.1 describes provincial efforts to coordinate financial securities regulation at the national level through the creation of voluntary coordinating bodies. Section 4.2 details how Canada is currently regulating P2BL industry.

4.1. Harmonized Securities Regulation in Canada

With provinces retaining authority over financial securities regulation, Canada is one of the only developed countries that does not have a national financial securities regulator (Naglie, 2017). Two Canadian regulatory bodies, Canadian Securities Administration (CSA) and the Cooperative Capital Markets Regulatory System (CCMR), are national level opt-in coordination bodies that provinces currently use to harmonize their provincial securities law.

CSA relies on cooperation between provinces to work towards harmonized regulations and creating a more efficient nationwide regulatory system securities. CSA issues regulations, referred to as a National Instrument (NI) or Multi-Lateral Instrument (MI), which provinces and territories can choose to adopt. MI 11-102 Passport System is a CSA initiative that creates a regulatory passport system where financial firms deal with only their principal regulator (Canadian Securities Administrators, 2009). The principal
The regulator is typically the province where the financial firm’s head office is based. The system relies on two methods of allowing access: mutual recognition and legal delegation. Under the former, any compliant market participant in one jurisdiction is recognized by all other member provinces in the same way in order to avoid that participant file relevant documents in all provinces (Provincial-Territorial Council of Ministers of Securities Regulation, 2004). Under legal delegation, participating provinces delegate their powers to one jurisdiction (Provincial-Territorial Council of Ministers of Securities Regulation, 2004). The main drawback of the CSA passport approach is that Ontario does not formally participate. Ontario is the largest Canadian securities regulator and capital market in the country that accounts for 50% of Canada’s market capitalization (Ontario Securities Commission, 2017). Instead, Ontario is the principal participating province in a separate national body, the CCMR.

Ontario, British Columbia, New Brunswick, Saskatchewan, and the Yukon established the CCMR in 2015 to act as a securities regulator for the participating provinces (Cooperative Capital Markets Regulatory System, 2016). The objectives of the CCRM are similar to the CSA as it seeks to provide uniform legislation, create a more globally competitive environment through better market integration, enhance oversight of systemic risk, and to gain more influence internationally through unification of domestic market regulations (Cooperative Capital Markets Regulatory System, 2016). Signatory provinces are expected to enact decisions made by the CCMR by amending their respective provincial legislation (Cooperative Capital Markets Regulatory System, 2018). The Supreme Court of Canada (SCC) ruled in November 2018 that the CCMR is constitutional after a challenge from Quebec. Importantly, the SCC emphasizes that provincial legislatures retain their supremacy in securities regulation (McMillan LLP, 2018). A draft of the Capital Markets Act, a set of laws applicable to all participating CCMR governments, is currently being revised after a comment period that ended in August 2018 (Cooperative Capital Markets Regulatory System, 2018). Table 3 summarizes each province’s membership in one or both of these national bodies along with their share of Canadian market capitalization they regulate.
Recent studies point towards some sort of consolidated approach to securities regulation as desirable (Competition Bureau Canada, 2017; Charlotte Watson & Alex LaPlante, 2018; Competition Bureau Canada, 2017a; Toronto Financial Services Alliance, 2017). The underlying sentiment is that a consistent national framework creates certainty and predictability for Canadian P2BL investors, regulators, and firms alike. Nagile (2018) argues that, through the CSA passport system, securities regulations are already largely harmonized. However, P2BL demonstrates that new business models that do not fit neatly into pre-existing regulatory frameworks make harmonization across provinces difficult.

4.2. Certainty and Clarity: Knowing What Rules to Follow

Stocks, investment funds, and similar financial securities available to the public are required by law to issue a prospectus. A prospectus is a detailed investment document that provides investors with pertinent information regarding the issuer, the securities issued, and the risks of investing in the securities (Ontario Securities Commission, 2018). Issuers and market dealers, entities that distribute securities, can apply to provincial regulators to be exempt from issuing a prospectus for a financial...
security based on specific criteria. Entities that receive these exemptions operate in what is known as the exempt market. NI 45-106 Prospectus Exemptions, issued through the CSA, is the principal means for securities dealers to be exempt. It is recognized in every province and territory, including Ontario (Canadian Securities Administrators, 2011). Through NI 45-106 financial firms apply to their principal regulator to be exempt from prospectus requirements related to certain activities including capital raising (Canadian Securities Administrators, 2011). Provincial regulators classify P2BL as issuing debt-based securities so P2BL funding portals are considered market dealers by law (Ontario Securities Commission, 2019). Issuing a prospectus for each loan originated is a costly and burdensome requirement for a P2BL funding portal that looks to originate dozens or hundreds of loans annually. To avoid this requirement, P2BL firms presently rely on prospectus exemptions in the existing securities framework to operate nationally. The main capital raising prospectus exemptions relevant to P2BL firms are related to investor wealth and experience (accredited investor exemption) and document requirements (offering memorandum exemption) (Canadian Securities Administrators, 2011).

Provinces attempted to address the unique structure of crowdfunding through several crowdfunding related regulations, which are listed in Table 4. MI 45-108 Crowdfunding, issued through the CSA in 2016, provides prospectus exemptions for crowdfunding activities generally (Canadian Securities Administrators, 2016). However, it does not differentiate between equity and lending based crowdfunding, which carry different risks for investors and require different investor sophistication. More importantly, not all provinces and territories have adopted MI 45-108 making national operation difficult for a P2BL firm that relies on the exemption. Overall, the adoption rate of MI-45-108 is extremely low due to advertising restrictions (BCSC, 2018; Ontario Securities Commission, 2018). No P2BL firms currently rely on 45-108 Crowdfunding exemption. Instead, the only two operating Canadian P2BL marketplace firms rely on traditional prospectus exemptions (Ontario Securities Commission, 2019; Ontario Securities Commission, 2019a). Despite the existing coordination between provincial regulators, these exemptions require each individual province to approve, which limits efficiency and certainty in the process (Competition Bureau Canada, 2017).
### Table 4. Regulatory Instruments Potentially Applicable to P2BL - by Province

<table>
<thead>
<tr>
<th>Regulation</th>
<th>Effective Year</th>
<th>Participating Province(s)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Multilateral CSA 45-316 Start-up Crowdfunding Registration and Prospectus Exemptions</td>
<td>2015</td>
<td>British Columbia, Saskatchewan, Manitoba, Quebec, New Brunswick, Nova Scotia</td>
</tr>
<tr>
<td>Alberta Securities Commission Rule 45-517 Prospectus Exemption for Start-up Businesses</td>
<td>2016</td>
<td>Alberta</td>
</tr>
<tr>
<td>National Instrument 45-106 Prospectus Exemptions</td>
<td>2016</td>
<td>All Provinces</td>
</tr>
<tr>
<td>Multi-lateral Instrument Crowdfunding 45-108</td>
<td>2016</td>
<td>Alberta, Saskatchewan, Manitoba, Ontario, Quebec, New Brunswick, Nova Scotia</td>
</tr>
<tr>
<td>BCI 72-505 Distributions outside Province using Crowdfunding</td>
<td>2016</td>
<td>British Columbia</td>
</tr>
<tr>
<td>BC Instrument 45-535 Start-up Crowdfunding Registration and Prospectus Exemptions</td>
<td>2017</td>
<td>British Columbia, Saskatchewan, Alberta</td>
</tr>
</tbody>
</table>

**Sources:** Canadian Securities Administrators, 2019; Kitay, 2016

King (2016) notes that Canadian Fintech firms suffer from a lack of clarity in knowing what regulations are applicable to their business models. With no national regulator there are few avenues new Fintech firms can turn to for clarity on compliance (Competition Bureau Canada, 2017; Michael King, 2016; Toronto Financial Services Alliance, 2017). The consequences of uncertainty affect the business prospects of P2BL operators in Canada. P2BL operators are technology start-ups that rely on formal and informal sources of start-up capital that concentrates on creating the underlying tech (Competition Bureau Canada, 2017a). The cost of compliance is an additional cost to these start-ups that is exacerbated by the uncertainty concerning what regulations to follow and understanding how their businesses are governed through the existing framework (Toronto Financial Services Alliance, 2017). Uncertainty begets risk for investors. If an investor cannot adequately asses the risk and chances of success there is little incentive for investment without clarity (Competition Bureau Canada, 2017; Toronto Financial Services Alliance, 2017).

In addition to securities regulation, P2BL firms must also adhere to rules regarding anti-money laundering, terrorist financing, consumer protection, privacy, and data security among others (Charlotte Watson & Alex LaPlante, 2018). With the exception of the federal anti-money laundering legislation, data security, privacy and
consumer protection have both federal and provincial variations (Charlotte Watson & Alex LaPlante, 2018).

In summary, Canada’s regulatory system relies on provincial coordination through the CSA and CCMR, both opt-in umbrella groups. Neither of these national-level securities regulatory bodies have the participation of all provinces. Due to lack of uniformity there are inconsistencies in regulation. Consequently, new market entrants using new technology and business models are unclear how their firms are treated under the current regulatory regime.
Chapter 5.

Policy Problem and Stakeholders

The policy problem is regulatory barriers that P2BL funding portals face affect the potential size of the Canadian P2BL market and alternative financing available for small businesses in Canada.

Although there are several important determinants of Fintech growth, government regulation is the focus of my study due to its direct impact on private investment and its use as a policy lever by governments. Regulation is even more salient for the P2BL sector because the resultant debt obligations are considered financial securities in Canada, which imposes further layers of provincial regulation on their issuance and use. Technology start-ups trying to establish new P2BL businesses in Canada navigate overlap in regulatory mandates between governments and the identification and determination of applicability of regulations to their business models. P2BL is the focus of my study because it is at the cross-section of potential and existing economic levers for Canada, Fintech and small businesses. P2BL represents the complexity and challenges governments face in regulating new Fintech industries, regardless of sub-sector focus, because the underlying technology entails little marginal cost to scale to a national level yet the regulatory burden of doing so is considerable.

There are several key stakeholders involved in this issue. New entrants to the P2BL sector that operate the funding portals, which are typically technology start-up firms only recently established. Canadian small businesses with less than 100 employees who are the borrowers in the P2BL model. Lenders, who could be retail investors or accredited investors or institutions, who finance the business loans in a P2BL marketplace. Canadian federal government is responsible for regulating federal financial institutions through anti-laundering money acts and the Bank Act. Canadian provincial governments are responsible for financial securities regulation and enforcement.
Chapter 6.

Case Study Methodology

My study uses international case study analysis as the primary methodology to identify potential policy options that are applicable to Canada. A secondary methodology is used to validate the case study findings. A secondary methodology uses academic studies and government reports to validate case study analysis. Policy options are provided and analyzed based on these results.

The research objective is to identify the practices that effectively respond to new business models and technologies without undermining investor protections. Qualitative information is sourced from government documents and academic literature. Industry research is used to highlight key characteristics of P2BL, such as user adoption and popularity relative to other Fintech sub-sectors, in selected countries. This on-going survey research is publicly available\(^6\) and conducted quarterly or annually by consulting firms.

6.1. Case Study Selection

The case studies selected are the United Kingdom, Australia, and Singapore. The criteria for case study selection are summarized in Table 5. The focus is on each country’s current regulatory regime and responses to Fintech generally and P2BL specifically.

\(^6\) Market research firms do offer premium paid services that provide more detailed analysis. This study uses only information that is publicly available.
### Table 5. Case Study Criteria

<table>
<thead>
<tr>
<th>Criteria</th>
<th>United Kingdom</th>
<th>Australia</th>
<th>Singapore</th>
</tr>
</thead>
<tbody>
<tr>
<td>Level of Government Responsible for Securities Regulation</td>
<td>Financial Conduct Authority (FCA); Federal Level</td>
<td>Australian Securities and Investments Commission (ASIC); Federal Level</td>
<td>Monetary Authority of Singapore (MAS); Federal level</td>
</tr>
<tr>
<td>Formal Fintech Regulatory Program</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Guidance Issued on P2BL</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Fintech Use by User Activity</td>
<td>2015: 14.3% 2017: 42%</td>
<td>2015: 13.0% 2017: 37%</td>
<td>2015: 14.7% 2017: 23%</td>
</tr>
</tbody>
</table>

Source: Ernst and Young, 2017

### 6.2. Limitations of Case Studies

The selected countries have a top-down financial authority that is able to apply any change in regulation to essentially all financial institutions in the country. Canada’s federated system of powers makes direct implementation of policy options selected from abroad more difficult because all individual provinces are responsible for their own securities legislation.

P2BL is a fairly young industry where even the most mature international markets have only been in operation for just over a decade. The study of the effects of government policy and regulation of the P2BL industry is even shorter. Consequently, P2BL case study analysis limits definitive conclusions and analysis on policy reforms over the long-term.

### 6.3. Evaluation Framework

The evaluation framework is an analytical tool to outline important features of the regulatory bodies’ efforts to adapt to Fintech. The characteristics are based on the summary of various consultant and government reports. These reports focus on the categories and characteristics in Table 6 to evaluate countries’ responses to Fintech regulation.
### Table 6. Case Study Evaluation Framework

<table>
<thead>
<tr>
<th>Category</th>
<th>Characteristic</th>
<th>Measure</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regulatory Body Structure</td>
<td>Authority</td>
<td>Is regulatory authority shared with any other body?</td>
</tr>
<tr>
<td></td>
<td>Responsibility for Fintech Regulation</td>
<td>Is there a dedicated authority or group responsible for regulating Fintech firms?</td>
</tr>
<tr>
<td></td>
<td>Scope</td>
<td>What is the value of the P2BL industry?</td>
</tr>
<tr>
<td>Relationship Building</td>
<td>International Cooperation</td>
<td>Is the regulatory body party to international cooperation agreements with other regulators?</td>
</tr>
<tr>
<td></td>
<td>Dedicated Fintech Resources</td>
<td>Does the regulatory body have dedicated staff or similar resources for Fintech initiatives?</td>
</tr>
<tr>
<td>Knowledge Building</td>
<td>Sandbox</td>
<td>Is there a regulatory sandbox with strong participation?</td>
</tr>
<tr>
<td>P2BL Regulation Issued</td>
<td>Guidance</td>
<td>What direction has the regulatory given to market participants on P2BL?</td>
</tr>
<tr>
<td></td>
<td>Principle Based Regulation</td>
<td>Are regulations focused on outcomes?</td>
</tr>
<tr>
<td></td>
<td>Scaled Regulation</td>
<td>Do regulations account for differences in market participants?</td>
</tr>
</tbody>
</table>

Cases are evaluated along four categories: regulatory body structure; relationship building; knowledge building; and P2BL regulations. Each of these four categories are briefly reviewed below.

Regulatory body structure is explained by defining: the regulator’s authority, the regulatory body responsible for Fintech development, and the scope of the P2BL industry. These characteristics provide an understanding of the powers of the regulator and the extent of their control over Fintech developments. Understanding the scope of the market activity in each case study helps to contextualize the P2BL regulatory efforts mentioned later.

Relationship building is where regulators maintain contact with market participants and other regulatory bodies. International cooperation with other regulatory bodies is another way to keep abreast of market developments. Cultivating these relationships is aided by regulators having dedicated Fintech resources, such as staff and/or budgets, available for use.

Knowledge building takes several forms with regards to Fintech. The most common example is regulatory sandboxes. Regulatory sandboxes are programs run by the relevant authority that new Fintech market entrants can apply to in order to test out their idea or business model in constrained and limited real-world conditions. The firm’s activities are usually provided a temporary and time-limited exemption by the regulatory
body from the full gambit of potential applicable rules so that the regulator and firm can assess impact to the consumers and potential risks a new business model introduces to the financial system (Charlotte Watson & Alex LaPlante, 2018). The sandbox acts as a knowledge building exercise for regulators and a way for firms to build a minimum viable product without shouldering the full burden of compliance (Digital Finance Institute 2016; McCarthy Teterault LLP, 2016). Upon completion of the sandbox, firms are expected to comply with all identified regulations or receive an explicit regulatory exemption from specified rules.

P2BL regulation issued by case study countries indicates how P2BL is being treated by the regulatory bodies. In particular, whether specific P2BL guidance, in the form of regulations or policy briefs, has been issued. If so, further analysis is done to determine whether this guidance is focused on outcomes and if guidance is scalable. These two characteristics indicate how regulatory guidance is likely to affect market participants of varying sizes.

Overall, the goal of the analysis is to identify common regulatory characteristics across the case studies using the evaluative framework.
Chapter 7.

Case Study Analysis

This chapter reviews each case study along the four categories of regulatory body structure, relationship building, knowledge building, and P2BL regulation issued. I identify the strengths and weakness of each case study to determine potentially useful characteristics to incorporate into the Canadian context. Table 8, given at the end of sub-section 7.4, summarizes the key findings of my analysis.

7.1. Regulatory Body Structure

Understanding a regulator’s power and authority provides a way to evaluate the degree to which the regulator is constrained. Correspondingly, understanding the mechanisms in place to respond to Fintech development and the scope of the country’s P2BL industry contextualize each country’s regulatory response.

7.1.1. Authority

The Financial Conduct Authority (FCA) is an independent government body that reports to the UK’s Treasury department. It is funded by collecting fees charged to firms they regulate. The FCA is responsible for overseeing industries such as retail lending, retail investment, insurance, and pensions, among others (Financial Conduct Authority, 2018). FCA shares regulatory oversight with the UK’s Prudential Regulatory Authority, who is responsible primarily for systemic risk identification and monitoring.

The Australian Securities and Investment Commission (ASIC) is a self-funded independent government body that is part of Australia’s Treasury department. ASIC regulates a broad range of activities including consumer credit, financial services, and financial markets (Australian Securities and Investments Commission, 2018). The Australian Prudential Regulator Authority (APRA) is another main regulator, but it focuses on the overall functioning of the market. Its main purpose is to monitor and identify the financial system for systemic risk.
The Monetary Authority of Singapore (MAS) is both the securities regulator and the central bank for Singapore. Internally, the MAS is structured into several groups that are responsible for specific financial oversight. For example, the Prudential Policy and Macro-Prudential Surveillance Departments housed within MAS focus on identifying and monitoring systemic risk. The Capital Markets group oversees capital market and securities supervision through four functionally separate departments.

The common feature of the FCA, ASIC, and MAS, with respect to securities regulation, is that they all govern in a top-down manner from the national level. Regulations and policy guidance are created at the national level and administered by subsidiary departments or regional groups within the regulatory body. Financial regulations and directives require little to no coordination with other government bodies. Unlike the case study countries, Canada has no top-down securities regulator. Each province is responsible for supervising its own markets. National supervision relies on the CSA and, in the future, CCMR, which are opt-in umbrella groups.

7.1.2. Responsibility for Fintech Regulation

The UK introduced Project Innovate in October 2014. The goal is to provide dedicated staff to work with Fintech firms to encourage innovation that protects consumers and promotes competition through innovation. Project Innovate is the first point of contact for Fintech firms and is responsible for any Fintech initiatives. In carrying out this activity, it also acts as an informal communication between regulator and market participants.

Australia established the Innovation Hub in 2015. The goal of the Innovation Hub is to provide resources to help efficiently issue appropriate market licenses (Australian Securities and Investments Commission, 2017). ASIC’s Innovation Hub is the primary point of regulatory contact for Fintech firms. It provides an opportunity to communicate informally with new market entrants who have questions regulatory compliance questions and issues (Australian Securities and Investments Commission, 2017). From 2015-2018, the Innovation Hub worked with 353 Fintech firms, 41 of whom were focused on marketplace lending, and provided informal guidance to 313 additional firms (Australian Securities and Investments Commission, 2018).
Singapore created the Fintech and Innovation Group (FTIG) in 2015 to focus on risk management, developing regulatory policies and guidance for new technology, and ensuring fair competition in Fintech. FTIG is made up of three divisions that each focus on a specific area of Fintech: payments, technology infrastructure, and technology innovation lab. Each of FTIG’s three sub-groups are the main points of contact for firms in those Fintech areas.

All three case studies have set up a body to directly address Fintech issues and opportunities at around the same time. The FCA and ASIC bodies are very similar in structure and role. MAS’s FTIG is similar in function to the efforts of the FCA and ASIC, but differs in structure. FTIG is further broken down by specific Fintech applications. In Canada, the responsible groups for Fintech regulation vary from province to province based on the priorities of the regulators. Ontario, Quebec, and BC have organizations within their securities regulator that have similar functions to the UK and Australia groups. There is no comparable body at the Canadian national level that is dedicated in a manner resembling the case studies.

7.1.3. P2BL Scope

The P2BL sub-sector of UK’s P2BL sector increased significantly from 2011 to 2016, in terms of value of total loans issued. It increased from $35.55 million in 2011 to $3.452 billion\(^7\) in 2017 (Bryan Zhang et al., 2018). The growth in total value mirrors the growing awareness of surveyed small businesses to alternative forms of financing, which increased from 25% in 2012 to 47% in 2017 (British Business Bank, 2018).

Australian alternative business financing increased from $13.08 million in 2013 to $468.07 million in 2016 (Kieran Garvey et al., 2017). However, P2BL loan values totaled only $9.16 million in 2016. Balance sheet business lending and invoice trading are the drivers of the Fintech business lending. They accounted for $287.34 million and $171.68 million respectively in 2016 (Kieran Garvey et al., 2017).

Singapore’s P2BL sub-sector grew from $0.661 million in 2013 to $152 million in 2016\(^8\) in total value of business loans issued (Kieran Garvey et al., 2017). P2BL

\(^7\) Converted from pound sterling at an exchange rate of 1.69.

\(^8\) Converted from US dollars at an exchange rate of 1.32.
represents the largest alternative finance sub-sector, by market value, accounting for 54% of the alternative finance market in Singapore (Kieran Garvey et al., 2017).

The UK is the most developed with this maturity reflected in the value of loans issued. Singapore’s P2BL is also increasing, but on a substantially smaller scale than the UK. Australian lending through Fintech firms while growing, is increasing in a more varied way than in the UK and Singapore. Australia’s P2BL sector growth is on a similar trajectory to Canada where balance sheet lending is dominant and P2BL constitutes a considerably smaller market share of loan-based crowdfunding.

7.2. Relationship Building

Building relationships with industry participants is a way for regulators to better understand the existing pain points in the system and potentially identify future issues. All regulators have formal cooperation agreements with other national regulators. At home, regulators’ efforts in relationship building activities with market participants are, in some cases, facilitated by dedicated staff or other resources.

7.2.1. International Cooperation

The Memorandum of Understanding (MOU) creates a formal relationship between two signatory countries. A MOU typically focuses on information sharing and acting as a referral mechanism for Fintech firms between the signatory countries’ regulators. MOUs between regulators creates an international network that leverages the experiences of other regulators.

The UK is signed onto seven MOUs, Australia has signed onto five MOUs, and Singapore leads all case studies having signed eight. Ontario is following suit by signing four international cooperation agreements. Two of these agreements were signed with case study countries, UK and Australia (Ontario Securities Commission, 2018). Abu Dhabi and France signed a cooperation agreement that included the OSC and the majority of other provincial regulators (Ontario Securities Commission, 2017; 2017a). OSC also recently signed onto to participate in the Global Finance Innovation Network (GFIN) as another means to communicate with international regulators. The goal is information sharing between the current 11 members and future signatory bodies.
(Ontario Securities Commission, 2018a). The lack of coordination among provinces is clear through the imbalance in signed agreements participation in the GFIN, which is shown in Appendix A.

### 7.2.2. Dedicated Fintech Resources

The FCA does not freely release financial information concerning Project Innovate. However, a 2016 freedom of information request concerning the cost of Project Innovate provided some insight into the costs at the time. As of November 2016, roughly two years since its creation, Project Innovate spent £1,853,840.21 (Financial Conduct Authority, November 2, 2016a). The total cost is broken down in Table 7. It shows that £1,669,400.76, or 90%, of total costs are staff related. Of those staff costs, £90,183.94 are directed solely to the regulatory sandbox initiative (Financial Conduct Authority, November 2, 2016).

**Table 7. Breakdown of FCA Project Innovate’s Cost in 2016**

<table>
<thead>
<tr>
<th>Cost</th>
<th>Project Innovate</th>
<th>Regulatory Sandbox</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Staff</strong></td>
<td>£1,669,400.76</td>
<td>£90,183.94</td>
</tr>
<tr>
<td><strong>Operational-Travel</strong></td>
<td>£21,585.24</td>
<td></td>
</tr>
<tr>
<td><strong>Operational-Events and Staff Training</strong></td>
<td>£31,794.84</td>
<td></td>
</tr>
<tr>
<td><strong>Operational-Consultants</strong></td>
<td>£119,660.30</td>
<td></td>
</tr>
<tr>
<td><strong>Operational-Catering, Printing, and Miscellaneous</strong></td>
<td>£11,399.07</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>£1,853,840.21</td>
<td>£90,183.94</td>
</tr>
</tbody>
</table>

Source: Financial Conduct Authority (November 2, 2016)

Costs associated with ASIC’s Innovation Hub could not be found. Staff is required to vet regulatory sandbox applications, conduct outreach events, and provide support to Fintech firms. It is unclear whether these are dedicated staff within ASIC or if they have other responsibilities.

In the same year of the establishment of FTIG, MAS allocated $219 million for Fintech sector development (Kieran Garvey et al., 2017). It is unclear the breakdown of these costs as they relate to their various initiatives and outreach events. MAS’s regulatory sandbox requires dedicated regulatory staff to work with firms on a case-by-case basis so there are some resources that are clearly committed.
Costs are somewhat unknown for all three case studies. However, the UK and Singapore do provide dedicated staffing for regulatory sandbox initiatives. The FCA in particular spends a considerable known amount on staffing. Dedicated staff allows the FCA to run several groups within Project Innovate, such as the Advice Unit or the direct support group that both engage directly with Fintech firms. These dedicated resources are the first step in building relationships with Fintech firms. In Canada, Ontario and BC both have dedicated staff that focus solely on Fintech issues. Quebec convenes a working group that accomplishes the same goals, but the staff is not dedicated.

## 7.3. Knowledge Building

Regulators are attempting to keep up with the pace of technological change in the financial industry through knowledge building activities. Section 7.3.1 reviews the new initiative known as the regulatory sandbox.

### 7.3.1. Regulatory Sandbox

UK’s Project Innovate created the first regulatory sandbox for Fintech in 2016. The goals of the sandbox are to: reduce the time to market for new products, provide better access to financing by providing some regulatory certainty, increase the number of products tested, and allow the FCA to work directly with innovative firms to provide more tailored made regulations (Financial Conduct Authority, 2015). As of 2018, the UK sandbox is in its fourth phase of receiving applicants. The rate of firms successfully applying and working with the FCA to test their products is increasing with each year (Financial Conduct Authority, 2018). The tools of UK’s sandbox used during the testing phase include: exemptions or rule modifications, guidance to firms on applicable regulations, restricted authorization for Fintech firm to only test ideas as outlined in their sandbox application and agreed upon by the FCA, informal guidance, and, where exemptions or rule modifications are not suitable, FCA may issue a No Enforcement Letter that, within limits, no disciplinary action is taken against the firm while testing (Financial Conduct Authority, 2017c).

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*Appendix B provides a more detailed breakdown.*
ASIC introduced its sandbox framework in December 2016 that provides regulatory guidance on testing Fintech products or services. The framework is based on three main pillars. First, it highlights existing exemptions available to firms under ASIC’s authority or current law. These exemptions are applicable to only certain types of businesses. Second, firms can apply for licensing exemptions specific to an individual firm and its proposed product. Lastly, it provides procedures for a Fintech licensing exemption where a firm does not need to be licensed as a registered financial or credit service provider in order to operate. This exemption is restricted in the length to a maximum of twelve months and is subject to a number of conditions (Australian Securities and Investments Commission, 2017). These conditions focus on limiting the scope of the product or service by limiting its allowable customer base to 100 retail investors who are exposed to less than $5 million worth of financial risk (Australian Securities and Investments Commission, 2017). The Fintech exemption requires the firm to have adequate dispute resolution mechanisms, insurance provisions, and meet certain disclosure requirements (Australian Securities and Investments Commission, 2017). The exemption is also limited to the type of business. Only Fintech firms dealing or distributing financial products or providing advice are eligible (Australian Securities and Investments Commission, 2017). As of October 2018 only six participants have made use of the Fintech exemption through the ASIC sandbox initiative in its sandbox initiative (Australian Securities and Investments Commission, 2018).

MAS established its regulatory sandbox guidelines in November 2016 with the goal of encouraging Fintech firms to experiment within a time-bound and defined control environment (Monetary Authority of Singapore, 2016). The MAS sandbox is similar in structure to UK’s Project Innovate as it has a formal application and review process where, upon acceptance, the regulators work closely with firms. MAS requires applicants to demonstrate that their technology meets the following criteria: its technology is truly innovative, the product or service benefits consumers, the firm intends to operate in Singapore, limits on testing and expected outcomes are clearly defined, an appropriate risk management framework is in place, and firms have a plan for exiting the sandbox into the marketplace (Monetary Authority of Singapore, 2016). During the evaluation phase, MAS reviews exemptions or regulations that may require relaxation based on the firms proposed technology although there are certain regulations such as money laundering rules, that are ‘to be maintained’ (Monetary Authority of Singapore, 2016).
Singapore’s sandbox receives applications and accepts firms into the program on a rolling basis. It reviews each application on a risk-based approach and determines the appropriate regulatory exemptions, if any, on a case-by-case basis (Monetary Authority of Singapore, November 2016a). More recently, MAS proposed to create pre-defined sandboxes called Sandbox Express for certain markets where risks are fairly low and well-known. (Monetary Authority of Singapore, 2018).

The sandbox acts as a knowledge building exercise for regulators and a way for firms to build a minimum viable product without shouldering the full burden of compliance (Digital Finance Institute 2016; McCarthy Teterault LLP, 2016). In Canada, the OSC established an Ontario regulatory sandbox in 2016. More recently, the CSA established a national level sandbox in 2017. However, the bulk of the vetting process is completed by the regulators of the applicant’s home province. Canadian sandboxes rely primarily on granting existing exemptions from regulations on a case-by-case basis (Competition Bureau Canada, 2017).

7.4. **P2BL Regulation**

Regulators have responded to P2BL in two main ways. First, regulatory bodies use existing regulatory exemptions for market participants and apply these tools to P2BL operators and business models. The other way is to rewrite regulations and explicitly define P2BL operators and their various activities. Section 7.4.1 reviews both approaches, which have been used in the case studies. Section 7.4.2 and 7.4.3 reviews how regulations themselves are written.

7.4.1. **P2BL Guidance and Regulation**

The FCA amended its Handbook, a compilation of rules FCA regulated firms must follow, in several sections to include reference to P2P activities and arrangements. The amendments introduce formal definitions for P2P loans (designated investment), P2P operators (operator of an electronic system in relation to lending), and how the lender and borrower relationship is formed (Financial Conduct Authority, 2014). The regulations, specifically Section 4.1.8A, give the P2P operator control over how their risk management framework is designed based on the nature of its business (Financial
Conduct Authority, 2014). Several major sub-sections of the FCA Handbook are also amended. Specific amendments are discussed in section 7.4.2 and 7.4.3.

ASIC does not alter its existing regulatory framework to accommodate P2BL. Rather it directs firms to the appropriate existing rules whose applicability depends on the specific nature of the P2BL operator. For example, P2BL platforms that focus on small-business loans are subject to the requirements of the Australian Financial Services (AFS) license (Australian Securities and Investments Commission, December 2017a). This license, in turn, requires firms have several safe guards in place such as an appropriate risk management framework, adequate resources, and basic financial requirements. These requirements apply equally to P2BL as they do to traditional financial firms.

MAS regulates P2BL within its existing framework for marketplace lenders. The two main acts that govern these securities and, consequently P2BL, in Singapore are the Securities and Futures Act (SFA) and the Financial Advisers Act (FAA). Through the SFA and FAA, debt based securities require a prospectus issued unless the offering meets the criteria for certain exemptions. The other characteristic of MAS P2BL regulation is it requires operators be licensed under the SFA, which requires a $100,000 security deposit (Monetary Authority of Singapore, 2016a). A 2016 consultation paper on P2BL regulations suggest that the MAS approach is unlikely to significantly change in structure. MAS stated that it believes the existing exemptions protect investors while working well for P2BL if a few adjustments to the requirements are made (Monetary Authority of Singapore, 2016).

The FCA approached P2BL by changing its legislation to formally incorporate P2BL into their financial framework. MAS and ASIC did not significantly alter their existing regulations to accommodate P2BL businesses. Instead, each regulator provided publicly available guidance documents to clarify what existing exemptions and licenses the regulator are allowed or required. Canada’s system resembles Australia and Singapore because of reliance on exemptions from existing financial regulations. New national instruments have been created through the CSA, in particular 45-108 Crowdfunding. However, this guidance does not differentiate between P2BL and equity based crowdfunding. Also, in practice, P2BL firms rely on existing prospectus exemptions available through MI 45-106 Prospectus Exemptions.
7.4.2. Principle Based Regulations

As discussed in section 7.4.1, amendments to FCA regulations were made in 2014 to insert language that broadly defines various aspects of crowdfunding lending. The definitions are written broadly to include many different types of lending. The amendment generally focus on requirements for P2BL funding portals to provide lenders with the appropriate information to determine the amount of risk they are taken on. More specifically, Section 4.1.8A allows firms to determine what steps are ‘reasonable’ for them to take in order to ensure that loan agreements are maintained in the event that the P2BL funding portal ceases activity (Financial Conduct Authority, 2014). The regulations give the P2P operator control over how their risk management framework is designed based on the nature of its business. The desired outcome being that investors and borrowers are protected in the event that the P2P operator ceases operations.

Australian guidance does not contain any new regulations for P2BL, but clarifies how P2BL fits into the existing regulatory system. ASIC is focused on consumer protection outcomes of regulation as evidenced by the registration requirement with ASIC for P2BL operators involving retail investors. Otherwise, it relies on rules that are equally applicable to traditional lenders and market investment firms.

MAS’s regulations do not meaningfully depart from the regulations already in place prior to the emergence of P2BL. MAS is primarily concerned with limiting the use of P2BL by retail investors who do not have the knowledge and financial competency of accredited and institutional investor to understand the risks of P2BL (Monetary Authority of Singapore, 2016). The desired outcome of P2BL regulation for MAS is to limit potential harm to retail investors. MAS believes the current regulatory framework, specifically the Small Offer prospectus exemption, is sufficient to accomplish this goal.

The UK’s specific regulations have examples of principle based regulations that focus on regulatory outcomes as opposed to the means. Australia and Singapore rely on more prescriptive rules that largely existed prior to P2BL industry growth. Canada is similar to Australia and Singapore in relying on exemptions from existing rules that are typically prescriptive.
7.4.3. Scaled Regulation

Scaled regulation refers to regulation that is proportionate to the nature, complexity, and scope of the regulated entity. Instead of a one-size-fits-all approach regulation aims to account for differences in firm resources and ability to meet regulatory requirements.

In the UK, amendments to the FCA’s Interim Prudential sourcebook for Investment Businesses (IPRU (INV)) and Senior Management, Arrangements, Systems and Control (SYSC) section of the FCA Handbook are relevant examples of attempts at scalable regulation. The IPRU (INV) section of the FCA Handbook focuses on establishing ‘reasonable’ threshold limits for financial solvency limits\(^\text{10}\) P2BL operators must maintain (Financial Conduct Authority, 2014). Section 12.2.4 of the IPRU (INV) scales the financial solvency requirement based on the value of outstanding loans a P2P operator holds (Financial Conduct Authority, 2014).

MAS and ASIC do not have standalone P2BL regulatory regimes and, instead, provide clarification on how existing legislation is applicable to P2BL. The main regulations rely on exemptions from issuing prospectuses (Singapore) and requiring a license from the relevant regulator based on specific P2BL activities. These modifications to existing regulations do not represent scaled regulation.

\(^{10}\) Appendix C provides more details on the UK’s proposed solvency requirements.
### Table 8. Summary of Case Study Findings

<table>
<thead>
<tr>
<th>Category</th>
<th>Characteristic</th>
<th>Australia</th>
<th>Singapore</th>
<th>UK</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Fintech Specific Regulator</td>
<td>Yes; Innovation Hub</td>
<td>Yes; FTIG</td>
<td>Yes; Project Innovate</td>
</tr>
<tr>
<td>Relationship Building</td>
<td>International Cooperation</td>
<td>5 agreements in place. Includes referral and knowledge sharing mechanism.</td>
<td>8 agreements in place. Includes referral and knowledge sharing mechanism.</td>
<td>7 agreements in place. Includes referral and knowledge sharing mechanism.</td>
</tr>
<tr>
<td></td>
<td>Dedicated Resources</td>
<td>Potentially</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Knowledge Building</td>
<td>Sandbox</td>
<td>Yes; Few Participants</td>
<td>Yes; Few Participants</td>
<td>Yes; Robust participation</td>
</tr>
<tr>
<td>P2BL Regulation</td>
<td>Guidance and Regulation</td>
<td>Issued guidance. No tailored P2BL rules. Issued guidance on P2BL firms fit within existing regulations.</td>
<td>Issued guidance. Some modifications to existing exemptions to accommodate P2BL firms.</td>
<td>Formed new regulations specific to P2BL. Issued guidance on how new regulations fit within existing framework.</td>
</tr>
<tr>
<td></td>
<td>Outcome Based</td>
<td>Focus on consumer protection</td>
<td>Focus on consumer protection</td>
<td>Focus on consumer protection. P2BL regulations allow firm to decide appropriate risk management framework.</td>
</tr>
<tr>
<td></td>
<td>Scaled P2PL Regulation</td>
<td>No</td>
<td>No</td>
<td>Some examples</td>
</tr>
</tbody>
</table>

### 7.5. Summary of Findings

Australia, Singapore, and the UK are global leaders in terms of government action in response to Fintech. They have approached Fintech in similar ways by establishing specific Fintech regulatory bodies and regulatory sandboxes. All case studies focus on industry and international engagement through regularly scheduled events and participating in MOUs with other regulatory bodies. Through these examples the case studies continue to engage with and build their understanding of the Fintech industry.
Specific to P2BL there are key differences in how the case study countries have approached regulation. Australia and Singapore clarified how P2BL fits within their financial licensing and registration frameworks. ASIC and MAS regulate P2BL as a form of securities trade and fit P2BL within their existing securities framework. The FCA created new P2BL specific rules that modify the existing regulatory framework governing P2BL operators’ actions and structure. Conversely, Singapore relies on existing exemptions from prospectus requirements that have been refined to accommodate P2BL. Australia does not make special accommodations for P2BL, which is generally subject to the same requirements as traditional financial firms. All three case studies do focus on consumer protection with Australia and Singapore favoring policies that limit the exposure of retail investors/individual consumers to P2BL. The scope of the P2BL industry also varies with the UK industry growing to over 3 billion while Singapore lags considerably with P2BL loan values of $152 million and $9 million, respectively.

Through my analysis I identify two common and important characteristics present in all three countries. First, all countries run a form of a regulatory sandbox, largely based on the UK’s example. These sandboxes are one of the novel ways that regulators are responding to similarly novel Fintech developments. Second, some form of regulatory guidance specific to P2BL is common across case study countries. This finding indicates that clear rules or at least an understanding of how regulators view P2BL business models is an important characteristic. The importance and quality of these results is confirmed through a secondary methodology in sub-section 7.6.

7.6. Secondary Methodology

The case study findings in section 7.5 are now evaluated using a secondary methodology. The evaluation is based on program performance, where data exists, and academic articles that examine the effective characteristics identified through the case study analysis. The characteristics chosen for further study are regulatory sandboxes and regulatory guidance.

7.6.1. Regulatory Sandboxes

As mentioned earlier, the UK sandbox initiative is one of the first and most successful sandbox initiatives. In 2017, the FCA reported on the lessons learned through
the sandbox’s one year of operation. It reported that the sandbox: reduced time to market for firms, facilitated access to investor capital, reduced data sharing issues, enhance consumer protections, and allowed market testing product viability (Financial Conduct Authority, 2017a). Didenko (2018) outlines characteristics of successful sandbox programs. These characteristics involve creating clear and objective criteria for selection into the program, report on the outcomes of participants, and reduce preferential treatment ideally through law (Didenko, 2018).

CSA launched its own regulatory sandbox in late 2017 with the objective of delivering the same type of outcomes as the FCA. The structure differs from other case studies due to the provincial regulators being the relevant authorities. Fintech firms applying to the sandbox must do so through the provincial regulator where they wish to operate. Even though the CSA, a national body, runs the sandbox, the provincial regulators are the authorities that supervise the implementation of the program. The other practical consequence is that Fintech firms are restricted to operating in that province during the testing period unless they apply to multiple provinces. The CSA does post all decisions on its website and outlines the process in fairly clear detail.

7.6.2. Regulatory Guidance for P2BL

The common feature of the case studies is that official guidance documents were produced to inform P2BL firms. Didenko (2018) argues that providing this type of guidance is important. He found that successful Fintech regulatory regimes require regulators to provide written guidance in clear and easy-to-understand language. Clarity and certainty of applicable rules is a key concern to Fintech market participants who responded to Competition Bureau Canada’s (2017a) market study. Ferrarini (2017) found that regulatory regimes for loan-based crowdfunding fall into certain categories of existing financial regulation rather than creating new regulations.

Regulation and access to securities exemptions are uneven across Canada due to the provincial authority to regulate. Provincial securities regulators try to harmonize their rules through the CSA, which issues guidance documents. Canada’s system most closely resembles Australia’s and Singapore’s approaches that funnel P2BL funding portals through existing market exemptions. The CSA issued Multilateral Instrument 45-108 Crowdfunding in November 2015 to provide guidance to firms setting up crowd
funding portals (Canadian Securities Administrators, 2016). These guidelines do not necessarily apply to all P2B lending platforms as it depends on their business model (those that are considered investment funds are excluded) (Canadian Securities Administrators, 2016).
Chapter 8.

Policy Options and Criteria

The focus of this chapter is to identify policy options that increase the supply of available SME financing through P2BL platforms operating Canada wide. There are three policy objectives of investor protections, encouraging innovation in P2BL firms, and providing regulatory guidance. I evaluate the policies based full implementation in year one of the short-term, which is defined as 1-4 years.

8.1. Evaluation Criteria

The criteria are standards used to evaluate potential policy options to determine the appropriate short-term regulatory changes governing the P2BL industry. The criteria used for evaluation are: effectiveness, cost, integration complexity, and stakeholder acceptance. Each criterion has one or several measurements. Each measurement is scored with 1 for low, 2 for medium, and 3 high to gauge the quality of implementation. Where there is more than one measure for a criterion the average score is taken to weight all criteria equally. Table 9 summarizes characteristics of the criteria.
<table>
<thead>
<tr>
<th>Criterion</th>
<th>Definition</th>
<th>Measure</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Effectiveness</td>
<td>Investor Protection High - Retail investors annual investments capped at an absolute dollar value. Explicit requirements for firm disclosures and risk management systems Medium - Retail investors annual investments capped on percentage of their net worth. Requirements for firm disclosures and risk management systems are subjective Low - No restriction on retail investor limits. Minimal firm disclosure requirements. Risk management framework not vetted by regulators</td>
<td>High - 20% or more increase to value of P2BL loans originated Medium – 10% to 19.9% increase to value of P2BL loans originated Low – Less than 10% increase to value of P2BL loans originated</td>
<td>High = 3 Medium = 2 Low = 1</td>
</tr>
<tr>
<td></td>
<td>Scale of Canadian P2BL Industry High - 0%-5% increase in provincial regulators’ expenses Medium - 5.1%-10% increase in provincial regulators’ expenses Low - Higher than 10% increase in provincial regulators’ expenses</td>
<td></td>
<td>High = 3 Medium = 2 Low = 1</td>
</tr>
<tr>
<td>Cost</td>
<td>Annualized Implementation Cost for Provincial Governments High – Legislative Amendments Medium - Legislative Amendments and Administrative Changes Low - Restructured</td>
<td></td>
<td>High = 3 Medium = 2 Low = 1</td>
</tr>
<tr>
<td>Implementation Complexity</td>
<td>Changes to Existing Legislation High - Provinces and Territories Coordinate Through Both CSA and CCMR Medium - All Provinces and Territories Coordinate Either Through CSA or CCMR Low - Provinces Implement Independently with No National Coordination</td>
<td></td>
<td>High = 3 Medium = 2 Low = 1</td>
</tr>
</tbody>
</table>
### Stakeholder support

<table>
<thead>
<tr>
<th>Criterion</th>
<th>Definition</th>
<th>Measure</th>
<th>Value</th>
</tr>
</thead>
</table>
| Provincial Securities Regulators | **High** - Likely to Support  
Medium - Neutral  
Low - Unlikely to Support | **High** = 3  
Medium = 2  
Low = 1 |           |
| P2BL Firms | **High** - Likely to Support  
Medium - Neutral  
Low - Unlikely to Support | **High** = 3  
Medium = 2  
Low = 1 |           |
| Investors  | **High** - Likely to Support  
Medium - Neutral  
Low - Unlikely to Support | **High** = 3  
Medium = 2  
Low = 1 |           |
| Borrowers  | **High** - Likely to Support  
Medium - Neutral  
Low - Unlikely to Support | **High** = 3  
Medium = 2  
Low = 1 |           |

### 8.1.1. Effectiveness

The first definition of effectiveness, *Investor Protection*, is how well investors are protected by the proposed policy option. Investors are protected through two avenues. First, P2BL firms provide safeguards in the forms of investment disclosure documents to investors, internal risk management frameworks, and other internal system controls. Second, investors are protected by limiting their financial exposure to P2B loans through regulatory caps on annual investments. Investor protection is an important criterion because policies that promote P2BL without sufficient investor protection can introduce more risk and potential harm. A policy option that explicitly prescribes P2BL internal controls and limits retail investor’s annual financial exposure to an absolute dollar value is ranked as high. More subjective internal control requirements and a retail investor investment limit as a percentage of their net worth per year is ranked as high is medium. Few or no specified internal controls and no annual limit on retail investors is ranked as low.

The second definition of effectiveness, *Scale of Canadian P2BL Industry*, is the expected likelihood that policy options can stimulate growth of the Canadian P2BL industry. Gauging the expected impact on Canadian P2BL is a proxy measure of the additional financing potentially available to small businesses. The definition is measured by the expected impact to the loan origination values of the Canadian P2BL industry,
currently estimated at $9.1 million (Tania Ziegler et al., 2018). A 20% increase or higher ranks as high, 10% to 19.9% ranks medium, and less than 10% ranks low.

8.1.2. Cost

The definition of cost is the *Annualized Implementation Cost for Provincial Governments*. The criterion is measured by each policy option’s impact to provincial securities regulators’ annual expenses. Evaluating these estimated costs provides a way to analyze the on-going cost implications of policy implementation. Estimates are generated from case study research. High is defined as 0-5% increase, medium is 5.1%-10% increase, and low is 10.1% increase or more. Table 10 shows the operating expenses of provincial securities regulators and the magnitude of a 5% and 10% increase in expenses.

### Table 10. Budget of Largest Provincial Securities Regulators 2017/2018 (Millions)

<table>
<thead>
<tr>
<th>Province</th>
<th>Annual Securities Regulation Expense</th>
<th>Increase in Securities Regulation Expense</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>5%</td>
</tr>
<tr>
<td>Ontario</td>
<td>$117.1</td>
<td>$5.9</td>
</tr>
<tr>
<td>Alberta</td>
<td>$38.4</td>
<td>$1.9</td>
</tr>
<tr>
<td>Quebec</td>
<td>$122.3</td>
<td>$6.1</td>
</tr>
<tr>
<td>British Columbia</td>
<td>$50.0</td>
<td>$2.5</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$327.8</strong></td>
<td><strong>$16.4</strong></td>
</tr>
</tbody>
</table>


8.1.3. Implementation Complexity

The first definition of implementation complexity is *Changes to Existing Legislation* required to implement the policy option. Any change to provincial securities law requires each individual province to amend their respective legislation. The degree of change, if any, to existing provincial securities legislation subsequently affects the degree of complexity for policy implementation. Changes to legislation that require only amendments to existing legislation rank High, amendments and administrative changes rank Medium, and legislative restructuring ranks Low.
The second definition on implementation complexity is the amount of Collaboration Between Provinces. This dimension captures how much, or little, the policy option makes use of the existing inter-provincial securities coordination bodies, which are the CSA and CCMR. The more these bodies are capable of implementing a policy option the less coordination is needed between individual provinces. The higher degree of coordination required between provinces without the aid of established coordinating bodies the more complex the option becomes to implement. Implementation through both the CSA and CCMR is given a value of High, through either the CSA or CCMR receives a value of Medium, and requiring provinces to implement independently ranks Low.

8.1.4. Stakeholder Support

Provincial Securities Regulators, P2BL Firms, Investors, and Borrowers are identified as the key stakeholders impacted by changes to the P2BL industry. The importance of stakeholder support is that it is affects the likelihood of growing the P2BL industry in several ways. First, Provincial Securities Regulators have the constitutional power to regulate securities. Any effort to operate at a national level invariably requires the buy-in of the provincial governments and their regulators to create an effective and efficient regulatory framework. Second, P2BL Firms may be discouraged from operating in Canada if regulation is seen as too restrictive or complicated. Conversely, if there is uncertainty around how their operations are regulated, unknown compliance costs similarly discourage P2BL operations investment. Lastly, Investors and Borrowers that supply and receive credit, respectively, in P2BL markets are needed to ensure there is a functioning market for P2BL industry. Each stakeholder’s support is measured as likely to support, neutral, and unlikely to support.

8.2. Policy Options

There are three policy options chosen for further review. First, the creation of a regulation specific to lending based crowdfunding. Second, providing dedicated resources to CSA that allow the participant oversight process to be controlled in a top-down manner. Third, the creation of a loan referral requirement to alternative credit providers upon loan rejection by traditional financial institutions.
8.2.1. National Instrument on P2BL Adopted by CSA and CCMR

The first policy option is for the CSA and CCMR issue P2BL specific guidance that clearly separates requirements for loan-based and investment-based crowdfunding. The current guidance from CSA, and likely to be adopted by the CCMR, is provided under CSA Multilateral Instrument 45-108 *Crowdfunding*. Under MI 45-108, debt and equity based crowdfunding are both defined as a ‘securities based model’ of crowdfunding (Canadian Securities Administrators, 2016a). A one-size fits all approach to crowdfunding regulation makes creating regulations proportionate to the risk more difficult. I propose that the CSA and CCMR create a new stand-alone national instrument that applies only to loan-based crowdfunding. Doing so recognizes that there are different risk profiles between loan and equity based crowdfunding.

Issuing a new national instrument also provides an opportunity to review whether the prescriptive protections and funding portal limitations contained in MI 45-108 are suitable. As discussed in Section 7.4, the UK utilizes more principle based and scaled regulation that puts the onus on the funding portal operator to construct ‘reasonable’ risk management and compliance systems. In a post-implementation review of these 2016 regulations, the FCA recommends understanding lending business models in greater detail (Financial Conduct Authority, 2018). Separating investment (or equity) based crowdfunding regulations from loan-based crowdfunding is a step that would help Canadian regulators understand the risks posed by each type of crowdfunding model.

The newly created national instrument would keep the current investor investing limits in place until the risk of borrowers defaulting on loans can be adequately assessed by regulators. The main test being the rate of default of P2BL borrowers during a prolonged economic downturn. Limitations on P2BL operators and their business operations need to be reviewed proportionate to the risk of the business model, as determined by regulators during the application stage.

8.2.2. Top-Down Regulatory Sandbox Program

The second option is to provide the CSA with dedicated resources and staffing for operating the existing national regulatory sandbox. Provincial regulators are responsible for vetting applicants to the CSA regulatory sandbox in their jurisdiction.
Only after the provincial review is complete is an application referred to the CSA for review. Provincial regulators know their rules and markets the best so they can provide the best guidance for applicants. However, this arrangement provides the provinces, and especially the largest four (Ontario, Alberta, Quebec, and BC), with power to reject applications without requiring consideration for how applicants might operate in other jurisdictions or nationally. It is also unclear what avenues for information sharing exist between provincial regulators to communicate new developments specific to applicants who were denied referral to the CSA sandbox program. The policy option proposes to move away from this bottom-up referral program to a top-down approach. Applicants to the sandbox apply directly to the CSA to enter into the sandbox programs. Dedicated staff from the CSA review the applications and work directly with applicants to better understand their business model. The composition of the CSA regulatory sandbox staff is such that all provinces are represented by staff that provincial regulators nominate to represent them. The CSA sandbox staff liaise with the provincial regulators of the applicant’s home jurisdiction to jointly review applications. The provincial regulators where applicants propose to operate would have to agree with the CSA’s approval of an applicant into the sandbox program. The CSA sandbox prepares reports on all applicants, both successful and unsuccessful, that details reasons for acceptance or rejection. These reports are issued to all member provinces’ regulators on a quarterly basis to keep abreast of developments and capture lessons learned from unsuccessful applicants.

8.2.3. Mandatory Bank Referral to Alternative Credit Provided Upon Loan Rejection

The third policy option is to mandate federal financial institutions (FFI) to refer SMEs to alternative credit providers, including P2BL, upon rejection of applicant’s loan. The goal of the policy is to create market awareness and drive demand for P2BL while serving SME financing requirements. The FCA initiated a similar program in 2016 that is administered by the British Business Bank and overseen by the FCA (Financial Conduct Authority, 2018). In Canada, regulation is enacted under the federal Bank Act. This policy option requires all FFI to refer unsuccessful business loan applicants to a government-approved alternative finance provider, including P2BL firms. The Office of the Superintendent of Financial Institutions (OSFI) is responsible for FFI regulatory compliance. The OSFI is similarly responsible for enforcing FFI compliance with the
proposed alternative financing program. P2BL platforms who wish to participate in the referral program apply and are vetted through the CSA to ensure that platforms are well-run and able to provide the necessary funding to SMEs. Through this process the CSA maintains a short-list of qualified platform operators where the FFI can refer unsuccessful clients’ information. Consent from loan applicants is required during the original loan application with the FFI to distribute their information to the CSA short-listed platforms. Once received the P2BL can provide the loan applicant with terms for loan funding through the P2BL platform. The loan applicant is under no obligation to accept any financing from the short-listed platforms.
Chapter 9.

Policy Option Evaluation

This section evaluates the proposed policy options with the chosen criteria. Table 12 provides a summary of the policy option analysis at the end of evaluations. Section 9.4 summarizes the policy recommendations.

9.1. National Instrument Specific to P2BL Adopted by CSA and CCMR

Effectiveness. Degree of Investor Protection could be less relative to the current regulations. The current prescriptive regulations certainly protect both accredited and non-accredited investors from substantial monetary losses. These losses are capped at $50,000 and $10,000, respectively, per year for the majority of the provinces. It is unclear whether these amounts are proportionate to the risk inherent in funding P2B loans. The main reason is that the resiliency of P2BL has not been tested by a significant economic downturn. Without knowing the true risk of borrowers defaulting on loans during a prolonged economic downturn it is prudent to keep current investor funding limits in place until more information is known. However, the P2BL-specific regulation would limit investor annual investments to 10% of their self-reported net worth rather than an absolute dollar value. Doing so ensures the risk of investment loss is proportionally between investors while allowing more capital to be invested. The second goal of the policy option is to reduce restrictions on P2BL operators. It is conceivable that putting the onus on operators to put in place their own compliance and risk management systems could lead to poor business practices. Potential risks to investors in doing so could be deceptive marketing tactics, poor record keeping, and/or lack of sufficient arrangements to close out operations if the business fails (Financial Conduct Authority, 2018). While investor protections are still maintained in investing limits there is a chance for potential harm. The option is given a rank of MEDIUM (2). Scale of Canadian P2BL Industry is positively affected by stand-alone regulations that are created and adopted by both the CSA and CCMR. An easier pathway to national operation can reasonably expect to reduce barriers to entry for new P2BL funding portals (Competition Bureau Canada, 2017). Based on statistics from Canada’s few
nationwide P2B lenders, loan originations in the first two years are expected to be approximately $1 million (Lending Loop, 2019). Easier national operation can induce new market entrants to begin operations or encourage existing firms to scale up to operate nationally. In allowing an easier pathway to operating nationally, this option is given a rank of HIGH (3).

Cost. The Annualized Implementation Cost for Provincial Governments is expected to be minimal if the P2BL regulations largely resemble the current MI 45-108 that is relied upon for crowdfunding regulation. Changes require collaboration among regulators so there would be administrative costs incurred. However, relative to the budget of the provincial securities regulators, it is expected to be within the threshold of 0%-5% cost increase. The option ranks as HIGH (3).

Implementation Complexity. Changes to Existing Legislation are required through the new national instrument. By basing the new instrument on the current 45-108 Crowdfunding and 45-106 Prospectus Exemptions guidance, time to draft the new regulation could be significantly reduced. However, the new instrument requires passage by both the CCMR and CSA in identical form to be useful as a national regulation. Doing so requires amendments to provincial regulation that recognizes the new proposed regulation. Additionally, administrative changes are needed to account for the changes to the annual capital limits for investors. Due to the legislative amendments and administrative changes required, this option is given a rank of MEDIUM (2).

Collaboration Between Provinces requires both the CSA and the CCMR to issue the same regulation so that rules are applied uniformly across Canada. Coordinating between these two institutions is hampered in two ways. First, the CCMR is still in its implementation stage with bills needing to be passed at the federal and provincial levels. Second, once created, it is unclear how the CCMR intends to interact with non-signatory provinces such as Alberta and Quebec (McMillan LLP, 2018). The current drafts of the federal and provincial CCMR bills do not address this issue. If the CCMR does not participate in issuing the regulations, it is feasible for the CSA to issue updated guidance on its own. This new instrument could be recognized under CSA’s existing passport regime. However, doing so could exclude Ontario’s participation. With uncertainties regarding implementation and coordination between the provinces, this option is given a rank of MEDIUM (2).
Stakeholder Support. For Provincial Securities Regulators there remains provincial disagreements over specific investor protection limits and regulatory exemptions that apply to crowdfunding generally (Kitay, 2016). These disagreements would likely carry over into a similar regime for P2BL. However, the CCMR is set up differently than the CSA. CSA is an umbrella group that serves to facilitate dialogue and coordination amongst the provinces. All national instruments may be adopted by provinces, but cannot be mandatory. More conformity to CCMR regulations is expected due to its existence being based in enabling provincial and federal legislation, although signatory provinces do retain legislative authority. With the uncertainty of national-level regulators this option is given a rank of MEDIUM (2). P2BL Firms are likely to support specific guidelines issued by the two main national level securities regulatory bodies. It would provide P2BL operators with clarity on how their businesses would be treated by regulators. Support from P2BL firms for regulatory certainty this option is given a rank of HIGH (3). Investors are provided with fewer restrictions relative to an absolute dollar so are likely to support the measure. This option is given a rank of HIGH (3). Borrowers are likely to support the policy option because it can potentially provide additional sources of loan financing so this option is given a rank of HIGH (3).

9.2. Top-Down Regulatory Sandbox Program

Effectiveness. Ensuring Investor Protection is one of the principal utilities of regulatory sandboxes. The purpose of regulatory sandboxes are to test new and innovative business models in a time-limited and controlled way. The policy option reorganizes the first point of contact to be the CSA rather than the home provincial regulatory of the applicant. There are still reviews conducted by provincial regulators. However, with the CSA being involved in all applications, both unsuccessful and successful, institutional knowledge is gained that can be used in reviewing subsequent applications. Incorporating lessons learned from previous reviews and having a dedicated staff at the national level retains and likely increases the regulatory sandbox’s effectiveness. This option is given a rank of HIGH (3). Scale of Canadian P2BL Industry is addressed indirectly. A top-down regulatory sandbox is not specific to P2BL firms. Any type of Fintech firm could apply to this sandbox. The policy option addresses P2BL specific issues because P2BL firms currently rely on regulatory exemptions from provincial regulators to operate. Relying on exemptions creates uncertainty for the P2BL
so there must be close contact with provincial regulators. A desired by-product of augmenting the capability and information sharing of the CSA national regulatory sandbox is that P2BL firms receive more timely and constructive feedback from provincial regulators. Furthermore, a national regulatory sandbox with a top-down structure and dedicated resources helps coordination between provinces. Doing so eliminates the applicant going to each province to work out solutions individually. The option’s impact on the scale of the P2BL industry is indirect and uncertain so this option is given a rank of LOW (1).

Cost. The *Annualized Implementation Cost for Provincial Governments* is calculated based on the FCA cost of establishing Project Innovate and running its regulatory sandbox. Discussed in Section 7.2.3 the cost of Project Innovate, including its regulatory sandbox, is approximately £1,943,000 or $3,341,000\(^\text{11}\) over a 25 month period. The total estimated monthly cost is $133,000. The resultant estimated annual cost is $1,600,000 or approximately $1,658,000 after accounting for inflation.\(^\text{12}\) The four largest regulators sharing cost equally\(^\text{13}\) and operating out of a centralized office would see an annual increase of $415,000 to their annual operating cost. This accounts for less than 1% of 2017/2018 expenses. Table 11 shows the detailed breakdown. The increase in operating cost is likely to be partially off-set by provincial regulators saving resources by transferring responsibilities to the new CSA staff. BC, Ontario, and Quebec all have dedicated FinTech teams that currently handle these requests. The $1.6 million overall annual cost associated with the regulatory sandbox appears high relative to the overall size of the Canadian P2BL industry, which is $9.16 million. However, this sandbox is not exclusively for the benefit of P2BL firms. Any FinTech firm can benefit from the sandbox program. A more comparative metric is the scale of the Canadian FinTech industry, where the first half of 2018 saw $263 million invested in FinTech (KPMG, 2018). Due to the relative low impact to current budgets this option is given a rank of HIGH (3).

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\(^\text{11}\) Based on an exchange rate of 1.72 from pound sterling to Canadian dollar.

\(^\text{12}\) Calculated based on Bank of Canada data [https://www.bankofcanada.ca/rates/related/inflation-calculator/](https://www.bankofcanada.ca/rates/related/inflation-calculator/).

\(^\text{13}\) Ontario, Alberta, Quebec, and BC currently share the costs equally for various CSA electronic filing systems. BC’s higher relative cost is justified by the vibrant Vancouver tech community who can reasonably be assumed to make more use of the CSA regulatory sandbox relative to other provinces.
Table 11. Budget Impact of Top-Down CSA Regulatory Sandbox ($ Millions)

<table>
<thead>
<tr>
<th></th>
<th>Ontario</th>
<th>Alberta</th>
<th>Quebec</th>
<th>BC</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenue</td>
<td>$115.8</td>
<td>$50.9</td>
<td>$161.5</td>
<td>$46.7</td>
<td>$374.9</td>
</tr>
<tr>
<td>Expenses</td>
<td>$117.1</td>
<td>$38.4</td>
<td>$122.3</td>
<td>$50.0</td>
<td>$327.8</td>
</tr>
<tr>
<td>$415,000 annual cost as percentage of current expenses</td>
<td>0.4%</td>
<td>0.1%</td>
<td>0.3%</td>
<td>0.8%</td>
<td>0.13%</td>
</tr>
</tbody>
</table>


Implementation Complexity. No Changes to Existing Legislation are required. Each participating regulator requires alterations to current budgets that must be approved by their respective provincial governments. Due to the low impact on budgets it is not expected to be difficult to do so. There are substantial administrative changes required in order to implement the new regulatory sandbox process. There are also new staff to be hired and offices required to be setup. This option is given a rank of MEDIUM (2). Significant Collaboration Between Provinces is required to implement the policy option. The proposed CSA body requires the provinces to relinquish some control over the regulatory sandbox process. Provincial coordination required to set up the CSA body is needed because all provinces need to agree on the mechanisms and functioning of the referral process. Once established the coordination of the program is facilitated by the CSA. However, information sharing and cooperation among provinces are crucial for the ongoing effective operation of a top-down CSA regulatory sandbox. All provinces retain their legislative powers in matters of securities regulation. Consequently, provincial approval is ultimately required for any sandbox participant to begin operations. This option is given a rank of LOW (1).

Stakeholder Support. Provincial Securities Regulators support for CSA sandbox depends largely on the composition. To ensure appropriate provincial representation, each province is given the right to appoint their own representative to the CSA sandbox. Provinces are still closely involved in the application vetting process. They also retain their right to decide whether a firm is approved to operate in their jurisdiction under the negotiated regulatory exemptions. Ontario may resist these changes because it currently has a dedicated Fintech team, previously established a provincial sandbox, and is taking steps to represent itself internationally. A national body could be seen as a way to dilute Ontario’s competitive advantage, who is trying to establish itself as a Fintech friendly jurisdiction. With some uncertainty around how Ontario would react to the proposed changes, this option is given a rank of MEDIUM (2). P2BL Firms can apply to participate
in the regulatory sandbox through a national level body. The sandbox participant is still required to work with each provincial regulator however. By reducing the administrative complexity of the sandbox program for participants this option is given a rank of HIGH (3). The option does not directly affect either Investors or Borrowers. Given the neutral support this option is given a rank of MEDIUM (2) for both stakeholders.

9.3. Mandatory Bank Referral to Alternative Credit Provided Upon Loan Rejection

Effectiveness. Investor Protection is undertaken by the CSA review of the short-listed P2BL platforms and the additional oversight of the OSFI. The CSA is responsible for vetting the platforms because they have the ability to work with the provinces to determine regulatory exemptions. The platforms applying to the referral program must already be operating in Canada. To do so, P2BL operators are required to have already consulted with and have their required regulatory exemptions approved by the CSA and/or the applicable provincial regulator(s). With the requirement to be operating as P2B lender prior to applying for the referral program there are several times that the business model of the P2BL is vetted. First when it receives approval for the CSA and province(s) to operate. Second, when it enters the referral program the P2BL firm is reviewed again. The double review process ensures that P2BL platforms are of sufficient quality before they are given the chance to expand. This option is given a rank of HIGH (3). The policy option directly impacts the Scale of Canadian P2BL Industry. Regulatory reform is needed first to allow a sufficient number of platforms to be approved to operate at the national level. Data from a similar program in the UK shows that between 2016 and 2018 a bank referral program originated £15,590,925 in loans (HM Treasury, 2018). A similar number is not likely in Canada given the more mature UK industry and investor awareness of P2BL generally. However, the loan program is likely to exceed 20% of the current P2BL industry scope given that they are operating funding portals that would be able to take on additional loans. This option is given a rank of HIGH (3).

Cost. The expected Annualized Implementation Cost for Provincial Governments is minimal due to the design of the program. The referral mechanism assumes that eligible P2BL are already approved for operation. The additional costs are minor compliance costs for existing FFI and issuing notices of rejected loans to P2BL firms. The CSA cost of vetting applicants is likely the most substantial cost although it is
expected that most of the work is already accomplished through the original approval process to operate in the first place. This option is given a rank of HIGH (3).

*Implementation Complexity.* Changes to Existing Legislation are required at the federal and provincial levels. The Canadian Bank Act requires amendments to include the provision for the implementation and oversight of the program. The CSA, working with the provinces, also require enabling regulations to be issued and adopted by all provinces. Administrative changes are required at the OSFI and CSA to handle their respective duties under the act. In doing so, all legislative changes must comply with the federal Professional Information Protection and Electronic Documents Act (PIPEDA) to ensure the sensitive information provided by the loan applicant is adequately safeguarded. This option is given a rank of LOW (1). A high degree of Collaboration Between Provinces is required to make the referral program effective. Even before agreeing to participate in the program, provinces require significant cooperation for allowing a P2BL to operate nationally in the first place. A referral program is an evolution of policy that focuses on P2BL firms operating nationally. This option is given a rank of LOW (1).

*Stakeholder Support:* The support of the Provincial Securities Regulators is required. The pre-condition of the referral program is that the P2BL funding portal is already approved by the CSA and relevant provinces. With the provinces already having vetted P2BL funding portals through the CSA, this option is given a rank of HIGH (3). Similarly, P2BL Firms support is likely for this option because it provides an avenue to increase awareness of their product among their targeted customer base. This option is given a rank of HIGH (3). Investors may indirectly benefit from a potential increase in the size of the P2BL industry by this option increasing potential demand. However, this is not certain because businesses are not required to make use of the alternative lenders. Given the uncertain and indirect nature of the benefits, the option is given a rank of MEDIUM (2). Borrowers are likely to support the option because it increases their access to optional financing sources. This option is given a rank of HIGH (3).
### Table 12. Summary of Policy Analysis

<table>
<thead>
<tr>
<th>Criteria</th>
<th>Definition</th>
<th>National Instrument Specific to P2BL Adopted by CSA and CCMR</th>
<th>Top-Down Regulatory Sandbox Program</th>
<th>Mandatory Bank Referral to Alternative Credit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Effectiveness</td>
<td>Investor Protection</td>
<td>Medium (2)</td>
<td>High (3)</td>
<td>High (3)</td>
</tr>
<tr>
<td></td>
<td>Scale of Canadian P2BL Industry</td>
<td>High (3)</td>
<td>Low (1)</td>
<td>High (3)</td>
</tr>
<tr>
<td>Effectiveness Total</td>
<td></td>
<td>2.5</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>cost</td>
<td>Annualized Implementation Cost for Provincial Governments</td>
<td>High (3)</td>
<td>High (3)</td>
<td>High (3)</td>
</tr>
<tr>
<td>Cost Total</td>
<td></td>
<td>3</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>Implementation Complexity</td>
<td>Changes to Existing Legislation</td>
<td>Medium (2)</td>
<td>Medium (2)</td>
<td>Low (1)</td>
</tr>
<tr>
<td></td>
<td>Collaboration Between Provinces</td>
<td>Medium (2)</td>
<td>Low (1)</td>
<td>Low (1)</td>
</tr>
<tr>
<td>Implementation Complexity Total</td>
<td></td>
<td>2</td>
<td>1.5</td>
<td>1</td>
</tr>
<tr>
<td>Stakeholder Support</td>
<td>Provincial Securities Regulators</td>
<td>Medium (2)</td>
<td>Medium (2)</td>
<td>High (3)</td>
</tr>
<tr>
<td></td>
<td>P2BL Firms</td>
<td>High (3)</td>
<td>High (3)</td>
<td>High (3)</td>
</tr>
<tr>
<td></td>
<td>Investors</td>
<td>High (3)</td>
<td>Medium (2)</td>
<td>Medium (2)</td>
</tr>
<tr>
<td></td>
<td>Borrowers</td>
<td>High (3)</td>
<td>Medium (2)</td>
<td>High (3)</td>
</tr>
<tr>
<td>Stakeholder Support Total</td>
<td></td>
<td>2.75</td>
<td>2.25</td>
<td>2.75</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>9.75</td>
<td>9.3</td>
<td>9.75</td>
</tr>
</tbody>
</table>

### 9.4. Policy Recommendations

Two policy options, *National Instrument Specific to P2BL Adopted by CSA and CCMR* and *Mandatory Bank Referral to Alternative Credit*, have equal total estimated values from factors. I recommend prioritizing a national regulation over instituting a bank referral program because the former is expected to encourage new P2BL market entrants. A bank referral program, without enough P2BL operators, risks being ineffective if existing suppliers cannot meet demand created by the option. Conversely, if
the existing P2BL funding portals can meet the demand created by the program, the policy would essentially pick winners by favouring P2BL firms already in operation. The option is ranked equally effective as the mandatory bank referral to alternative credit and more effective than a top-down regulatory sandbox. It receives a lower ranking for *Investor Protection* because the regulation provides more discretion to P2BL firms and a cap on investors that is not an absolute dollar value. Both of these features can pose more risk to investors relative to current rules. The proposed national regulation requires on-going monitoring by CSA and CCMR to mitigate potential abuses or misuses. The FCA reviewed its peer-to-peer lending rules in 2018 that subsequently lead to tighter controls for P2BL firms and investors. A similar strategy is recommended in Canada. CSA and CCMR should commit to conduct a post-implementation review of P2BL national regulation every five years to gauge the utility of the regulation and changes to the P2BL market. In terms of *Scale of Canadian P2BL Industry*, the national regulation scored equally as the mandatory bank referral program. A national regulation gives more certainty to P2BL firms and potential investors because they know the rules apply equally in all provinces. The bank referral program directly affects the potential size of the P2BL industry by stimulating demand. A top-down regulatory sandbox is potentially only indirectly beneficial to growing the P2BL industry. All options receive the highest rank for *Annualized Implementation Cost for Provincial Governments* so there is no substantial difference between options on this criterion. A national regulation specific to P2BL is recommended due its high ranking on *Implementation Complexity* relative to the other options. The CSA and CCMR jointly creating a national regulation helps coordinate the provinces and unify the administration of the regulation. The inter-provincial coordination and legislative changes required make the other options more difficult to implement relative to the recommended option. Expected *Stakeholder Support* varies across the options with the recommended option ranking in the middle. Expected support among *Provincial Regulators* does not rank high because there is some uncertainty on how the CCMR and CSA bodies are going to work together. However, the adoption of MI 45-108 *Crowdfunding* by the majority of provinces, CSA, and, tentatively, the CCMR demonstrates that widespread use is possible for a similar regulation specific to P2BL.

I further recommend the implementation of the top-down regulatory sandbox program and mandatory bank referral to alternative credit within 3-4 years after the
national regulation specific to P2BL is implemented. As evident by the low uptake of MI 45-108 *Crowdfunding*, simply creating a regulation does not guarantee utilization. A national regulation helps to clarify the rules specific to P2BL, however committing more resources to a top-down regulatory sandbox programs helps address any inefficiencies or items missed in the national regulation. Knowledge gained through the sandbox efforts can be used to refine the national regulation on an on-going basis. The feedback loop between the two options, if information is collected and disseminated appropriately, can reinforce the effectiveness of the national regulation. It can also help grow the supply side of the P2BL industry by encouraging more firms to enter the market. On the demand side, the bank referral program can help grow the customer the base of P2BL firms and awareness of the P2BL market for small businesses. The potential risk with the proposed implementation plan is that each option, to some degree, builds upon the others. If policy implementation does not go as planned for one option it may affect the viability of the others. For example, if the national regulator for P2BL and/or the regulatory sandbox options do not have the intended effect of encouraging more firms to enter the P2BL market then the bank referral program suffers from lack of firms to offer financing. However, the phased implementation allows policymakers a chance to assess the effectiveness of the national instrument specific to P2BL prior to implementing the other two options.
Chapter 10.

Conclusion

In this study, I presented ways that Canada could approach growth in its P2BL sector by examining how the UK, Australia, and Singapore, have responded to P2BL. Through the case study analysis, there were some key similarities. The three countries created groups within its securities regulatory body that focused on studying and serving the Fintech area. All three case studies also have a national regulatory body that can coordinate a national response to these new developments. There were two key approaches to regulating P2BL. Case study countries either try to fit P2BL into existing regulations through the use of exemptions or create new regulations specific to P2BL.

Three policy options resulted from my case study analysis: a national regulation specific to P2BL; dedicated funding to a national regulatory sandbox; and bank referrals to P2BL platforms. These options are evaluated along four criteria in order to determine which options are suitable for implementation in Canada. Through this evaluative framework I found that all options should be implemented at varying times. The priority is to implement a national regulation specific to P2BL through the CSA and CCMR bodies.

My study focused on the regulatory framework required to encourage the P2BL industry. A workable regulatory regime is useless if there is not the talent or funding to make use of it. The development of the appropriate technical talent and attracting venture capital to fund P2BL platforms are critical pieces that require further research. In addition, the demand side of the market needs to be developed to encourage borrowers and lenders to use the service. A potential area of study is how tax incentives could be used to grow the demand side of the P2BL market. A potential example is allowing investors to hold P2B loan notes in Tax Free Savings Account (TFSA) to encourage adoption among investors. Interest payments received on loans to SMEs, currently taxed, would be sheltered.
References


Ernst and Young. (2017). *EY Fintech Adoption Index 2017* (p. 44) [Annual]. Ernst and Young.


Appendix A.

Summary of International Regulatory Cooperation Agreements by Case Study Country and Province

Table A.1. International Cooperation Agreements by Case Study Country

<table>
<thead>
<tr>
<th>Signatory Countries</th>
<th>Australia</th>
<th>United Kingdom</th>
<th>Singapore</th>
</tr>
</thead>
<tbody>
<tr>
<td>Signatory Countries</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Canada (Ontario)</td>
<td>Australia</td>
<td>Abu Dhabi</td>
</tr>
<tr>
<td></td>
<td>Kenya</td>
<td>Canada (Ontario)</td>
<td>Australia</td>
</tr>
<tr>
<td></td>
<td>United Kingdom</td>
<td>China</td>
<td>France</td>
</tr>
<tr>
<td></td>
<td>Singapore</td>
<td>Hong Kong</td>
<td>India</td>
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<td></td>
<td>Indonesia</td>
<td>Japan</td>
<td>Japan</td>
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<tr>
<td></td>
<td></td>
<td>Korea</td>
<td>Korea</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Singapore</td>
<td>Switzerland</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>United Kingdom</td>
</tr>
<tr>
<td>Total Signed</td>
<td>5</td>
<td>7</td>
<td>8</td>
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<tr>
<td>Agreements</td>
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<td></td>
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</tr>
</tbody>
</table>

Source: Deloitte LLP (2017); Australian Securities and Investments Commission (2017)

Table A.2. Signed International Cooperation Agreements by Province

<table>
<thead>
<tr>
<th>Province</th>
<th>Abu Dhabi</th>
<th>Australia</th>
<th>France</th>
<th>UK</th>
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</thead>
<tbody>
<tr>
<td>Ontario</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Quebec</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>Alberta</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>BC</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>Manitoba</td>
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<td>No</td>
<td>Yes</td>
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<td>Saskatchewan</td>
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<td>Yes</td>
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<td>Nova Scotia</td>
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<td>PEI</td>
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<td>No</td>
<td>No</td>
</tr>
<tr>
<td>Newfoundland</td>
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</table>

Source: Ontario Securities Commission (2017); (2017a); (2018)
Appendix B.

UK Participation in Sandbox Program

Table B.1. UK Regulatory Sandbox Participation Rate

<table>
<thead>
<tr>
<th>Cohort</th>
<th>Applicants</th>
<th>Successful</th>
<th>Percentage of Applicants Entering Product Testing</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 – 2016</td>
<td>69</td>
<td>24 Accepted; 18 Firms Tested</td>
<td>26%</td>
</tr>
<tr>
<td>2- 2017</td>
<td>77</td>
<td>31 Accepted; 24 Tested</td>
<td>31%</td>
</tr>
<tr>
<td>3- 2018</td>
<td>61</td>
<td>18 Accepted; 15 Tested</td>
<td>34%</td>
</tr>
<tr>
<td>4- 2018</td>
<td>69</td>
<td>29 Accepted; Unknown amount of firms Tested</td>
<td>Unknown</td>
</tr>
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</table>

Source: Financial Conduct Authority, (2018e)
Appendix C.

UK P2PL Solvency Requirements

Table C.1. Financial Solvency Requirements for P2PL Section 12.2.4 of the IPRU (INV)

<table>
<thead>
<tr>
<th>Tier</th>
<th>Percentage Required</th>
<th>Tiers Based on Loans Outstanding</th>
<th>Solvency Requirement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tier 1</td>
<td>0.2%</td>
<td>First £50,000,000 of firm’s total value of loans outstanding</td>
<td>0.2 x £50,000,000</td>
</tr>
<tr>
<td>Tier 2</td>
<td>0.15%</td>
<td>Next 200,000,000 of firm’s total value of loans outstanding</td>
<td>0.15 x £200,000,000</td>
</tr>
<tr>
<td>Tier 3</td>
<td>0.1%</td>
<td>Next £250,000,000 of firm’s total value of loans outstanding</td>
<td>0.1 x £250,000,000</td>
</tr>
<tr>
<td>Tier 4</td>
<td>.05%</td>
<td>Any remaining amount</td>
<td>0.05 x Remaining Amount</td>
</tr>
</tbody>
</table>

Source: Financial Conduct Authority (2014)