

# Allen & Allen Update on Securities Law

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## Enacted:

### **New rules for exempt distributions in Ontario**

Ontario has replaced the former private company, private issuer, \$150,000, seed capital and government incentive security exemptions with new exemptions, including:

The "Closely-Held Issuer Exemption" permits issuers to raise a total of \$3 million, through any number of financings, from up to 35 investors without concern for the investor's "qualifications" or "sophistication". Excluded from the 35 investors maximum are "accredited investors", and current or former directors, officers, employees or consultants who acquire securities as compensation by or under an incentive plan. The exemption does not apply to public issuers, because the securities of a "closely-held" issuer must have transfer restrictions. No advertisements can be made, and no selling or promotional expenses can be incurred, other than the professional services of a registered dealer. If there are more than five shareholders after the trade, a generic information statement must be delivered to the investor(s) at least four days prior to the trade. No promoter can act as the promoter of any other issue of securities under this exemption within the preceding twelve months, and issuers in a "common enterprise" will be treated as one issuer for the purpose of the exemption.

The "Accredited Investor Exemption" permits issuers to raise any amount at any time from any person or company that meets certain qualifications, including: (1) various institutional investors; (2) companies, partnerships or trusts with net assets of at least \$5 million; (3) officers, directors and promoters of the issuer and certain family members; and (4) individuals who, either alone or jointly with a spouse, beneficially own financial assets having an aggregate realizable value that, before taxes but net of any related liabilities, exceeds \$1 million; or whose net income before taxes exceeded \$200,000 in each of the two most recent years; or whose net income before taxes combined with that of a spouse exceeded \$300,000 in each of those years and who, in either case, has a reasonable expectation of exceeding the same net income level in the current year.

The "Government Incentive Security Exemption" is for a security, or an interest in a partnership or joint venture, in which the issuer has agreed to renounce in favour of the holder, Canadian exploration or development expenses, or Canadian oil and gas property expenses, as defined by the Income Tax Act. The current exemption would largely be preserved, which limits solicitations in all jurisdictions to 75 persons and sales to 50, provided, before entering into an agreement, investors are given an offering memorandum with certain standard information about the directors, officers and promoter, together with a "contractual right of action". The prospective purchaser must have access to substantially the same information that a prospectus would provide, and each investor must be able to evaluate the investment because of net worth, investment experience or advice from an independent consultant (unless the investor is a senior officer or director or certain family members). No advertisements can be made, and no selling or promotional expenses can be incurred, other than the professional services of a registered dealer. No promoter can act as the promoter of any other issue of securities under this exemption within the calendar year.

The "Private Pooled Fund Exemption" is for a security in a private mutual fund or non-redeemable investment fund. The exemption would apply if: (a) the purchaser purchases as principal; (b) either (i) the security has an aggregate acquisition cost to the purchaser of not less than \$150,000; or (ii) the purchaser then owns securities having either an aggregate acquisition cost or an aggregate net asset value of not less than \$150,000 (a "top up"); and (c) the mutual fund or non-redeemable investment fund is managed by a portfolio adviser or a trust corporation registered under the Loan and Trust Corporations Act. (The exemption is slightly different for foreign managed funds.)

Ontario Rule 45-501 – Enacted November 30, 2001

### **Four month holds extended nationally – Enacted**

Four month holds on resales of certain exempt distributions by a "qualifying issuer", is now a national rule, except for Quebec. A "qualifying issuer" is a reporting issuer (or equivalent), who is an electronic filer under SEDAR, who has filed a current Annual Information Form ("AIF"), and either has a class of equity securities listed or quoted on certain specified exchanges or markets, or outstanding securities that have received an approved rating. Securities of a "non-qualifying" issuer must be held for 12 months from the later of the date of the distribution and the date the issuer becomes a "reporting issuer". Securities of issuers that are not "reporting issuers" can never be resold, absent a further exemption.

National Rule 45-102 Enacted November 30, 2001

## **Alberta joins BC with short form prospectus rule for CDNX issuers.**

Alberta will join BC, and permit CDNX issuers to distribute up to \$2 million of its listed securities per year, with a “short form [CDNX] prospectus”. The short form prospectus incorporates by reference (a) the current Annual Information Form (“AIF”), (b) the most recent audited annual financial statements, (c) all unaudited quarterly financial statements, quarterly reports and material change reports filed since the date of the current AIF, and (d) all technical reports and consents required under NI 43-101 (re mineral projects).

Alberta and BC Local Rule 45-509

## **CDNX temporarily relaxes private placement and CPC restrictions**

Until December 31, 2002, CDNX issuers can complete a one-time private placement offering at 5 cents per share up to a maximum of \$100,000 with various conditions, provided the issuer is inactive or is suffering financial hardship. Under the old rules, the minimum was 10 cents per share for a private placement, with no more than a 25 per cent discount to market.

Also on an interim basis, Capital Pool Companies (“CPCs”) listed on the CDNX have new options for completing their “Qualifying Transaction”. Subject to prior approval, (1) CPCs can combine with other CPCs to complete a Qualifying Transaction, or (2) CPCs can invest in and combine with an existing public company.

These change are in response to a “slumping” junior market.

## Proposed:

### **Exempt distributions in Alberta and BC - expanded and harmonized exemptions - Proposed**

Alberta and BC propose to expand and harmonize distribution exemptions. The new rules respond to industry comments that the cost of raising money is too high, especially for small and medium-sized businesses. The proposed exemptions are:

(1) Private Issuer Exemption – increased ability of private companies (i.e. those with restrictions on transfer and not more than fifty shareholders, excluding employees) to raise money while remaining private, without a disclosure document. The new exemption would allow a private issuer to raise capital from: (a) persons specifically listed in the exemption, (b) other persons who are not "the public", and (c) accredited investors.

(2) Family, Friends and Business Associates Exemption – would allow issuers to raise any amount of money from family members, close friends and close business associates without a disclosure document.

(3) Accredited Investor Exemption – would allow issuers to raise any amount of money from various financial institutions, pensions, investment dealers, established companies and wealthy individuals without a disclosure document. (As in the new Ontario Rule, an individual would be an accredited if he or she and spouse: (a) have financial assets exceeding \$1 million, or (b) have net income exceeding \$300,000 - \$200,000 without a spouse - in each of the last two years, and a reasonable expectation of exceeding that amount in the current year)

(4) Offering Memorandum Exemption – would allow issuers to raise any amount of money from anyone provided that the investor acknowledges the risks of investing and receives an offering memorandum - a short, simple disclosure document, in prescribed form. Investor protection provisions would also be added giving purchasers almost identical rights to those under a prospectus. The rights include a two-day right to cancel the purchase and broader rights to cancel or sue for damages if there is a misrepresentation in the offering memorandum. The prescribed form would be short and incorporate by reference an Annual Information Form for qualifying issuers, and longer in other cases.

Alberta and BC are also proposing that the shares for debt exemption and the bonus or finder's fee exemptions be available to all reporting issuers. Public comments will be considered until November 30, 2001.

Proposed Multilateral Instrument 45-103

**Please call if you have any questions - 416-865-0303**

## Allen and Allen

**WILLIAM ALLEN:** A graduate of the University of Toronto, Bill was called to the Bar in 1954. He later obtained a Masters of Law (LL.M.) from Osgoode Hall. He has lectured for the Canadian Bar Association and the Law Society of Upper Canada. He is the author of the Estate Planning Handbook (with three editions, published in 1985, 1991 and 1999) and has worked in the area of securities law since the early 1960s.

**JOHN ALLEN:** A graduate of law from Queen's University, John was called to the Bar in 1991, clerked with the Ontario Superior Court, and has a Masters of Law in securities law from Osgoode Hall. He is a graduate of the "Canadian Securities Course", "Financial Planning Course", and has all academic requirements for the designation of Certified Financial Planner (CFP). He is also the author of a monthly securities "Netletter" available only on Quicklaw ([www.quicklaw.com](http://www.quicklaw.com)), a fee-based legal database service.