

45-502CP (BC) Cooperative Associations [Proposed CP - Lapsed]

COMPANION POLICY 45-502CP (BC) COOPERATIVE ASSOCIATIONS

PART 1 BACKGROUND

1.1 Background

Legislation introducing the *Cooperative Association Act*, S.B.C. 1999, c.28, as amended, consequentially amended section 46(h) of the *Securities Act* by requiring that certain conditions must be met in order for an association to which the *Cooperative Association Act* applies (a "cooperative association"), to issue securities under the exemption from the registration requirements. Section 75(a) of the *Securities Act* provides a corresponding prospectus exemption.

1.2 Purpose

The purpose of Commission Rule 45-502 (BC) is to prescribe the conditions under which exemption from the registration and prospectus requirements of the *Securities Act* will be available to securities that cooperative associations issue under sections 46(h) and 75(a).

1.3 Application

The Commission Rule applies only to associations to which the *Cooperative Association Act* applies, including extraprovincial corporations that are registered under the *Cooperative Association Act*.

PART 2 STATUTORY EXEMPTIONS

2.1 General - The Commission Rule is not intended to restrict cooperative associations from using other exemptions that are available to issuers in general. These exemptions are described briefly below and are described in greater detail in Local Policy Statement 3-24 *Statutory and Discretionary Exemptions*. Where an offering memorandum is required for the use of an exemption, Form 43, which is attached for convenience only as Appendix "A", is the required form of offering memorandum. Cooperative associations and their members are advised to consult with their legal counsel in relation to the interpretation or applicability of the Commission Rule or the statutory exemptions.

2.2 Private issuer exemption - Sections 46(j) and 74(1)(a) of the *Securities Act* provide registration and prospectus exemptions where the trade is in securities of a private issuer and the securities are not offered for sale to the public. A private issuer must meet the definition of private issuer in section 1(1) of the *Act*, including having restrictions on transfer of its designated securities and being beneficially owned by not more than 50 persons, excluding employees, and the issuer not having distributed any of its designated securities to the public. The courts have suggested

two tests for determining who the "public" is. The first test enquires into the sophistication of the prospective purchaser to ascertain whether investor protection is necessary. The second test determines whether the relationship between the issuer and the prospective purchaser is close enough to assume that the information contained in a prospectus is not necessary.

If available, the private issuer exemption may be used by both the issuer and holders of its securities.

2.3 \$97,000 exemption - Sections 45(2)(5) and 74(2)(4) of the *Securities Act*, together with sections 90 and 129 of the *Securities Rules*, provide registration and prospectus exemptions where the purchaser purchases as principal and the trade is in a security that has an aggregate acquisition cost of not less than \$97,000. The exemption is therefore not available if, for example, the purchaser gathers 10 individuals who each put up \$9,700. In that case, the purchaser would not be purchasing as principal.

As long as the issuer does not advertise to find investors, the issuer does not have to provide purchasers with a prescribed form of disclosure under the *Securities Act*. Section 134 of the *Securities Rules* sets out what types of communication issuers can make to certain prospective purchasers without an offering memorandum being required. If the issuer does advertise, it must deliver an offering memorandum to the purchasers before an agreement of purchase and sale is entered into. The offering memorandum must be in the required form (generally Form 43) and must provide contractual rights of action to the purchaser if there is a misrepresentation.

If the issuer relies on this exemption, it must obtain an acknowledgement from each individual purchaser of their limited rights (Form 20A) and must file a report of the distribution with the Commission (Form 20) and the offering memorandum (if any) within ten days of the distribution.

If available, this exemption may be used by both the issuer and holders of its securities.

2.4 50 Purchaser Exemption - Sections 89(a) and 128(a) of the *Securities Rules* provide registration and prospectus exemptions for an issuer to sell securities to no more than 49 purchasers in any 12-month period. Each purchaser must be a spouse, parent, brother, sister or child of a director or senior officer of the issuer or a sophisticated purchaser (described below) and must purchase as principal. The issuer must not advertise and must not pay any selling or promotional expenses, other than for fees for professional services or services performed by a registered dealer. The issuer must also deliver an offering memorandum in the required form to each purchaser.

Each purchaser must sign a Form 20A acknowledging their limited rights and also certifying that the purchaser is a spouse, parent, brother, sister or child of a director or senior officer of the issuer or is a sophisticated purchaser. The issuer must retain those forms for six years and make them available to the Commission upon request. The issuer must also file a Form 20 and the offering memorandum with the Commission within ten days of the distribution.

2.5 \$25,000 Exemption for Sales to Sophisticated Purchasers - Sections 89(b) and 128(b) of the *Securities Rules* provide registration and prospectus exemptions for an issuer who sells securities to sophisticated purchasers in minimum amounts of at least \$25,000.

The term sophisticated purchaser is defined in section 1(1) of the *Securities Rules* and means a purchaser that gives an acknowledgement to the issuer (Form 20A) that the purchaser has a net worth of at least \$400,000 or an annual net income for each of the previous two years of at least \$75,000 (or \$125,000 if including annual net income of one's spouse) and reasonably expects that level of income in the current year. In addition, the purchaser must be able to evaluate the risks and merits of the investment on the basis of financial, business or investment experience or on the basis of advice from someone registered under the *Securities Act*, or exempted from the requirement to be registered, to provide advice.

Again, the issuer must deliver an offering memorandum to the purchaser, must file the offering memorandum and a Form 20 with the Commission within ten days of the distribution and must obtain an acknowledgement in Form 20A from each purchaser.

2.6 \$25,000 Exemption Where Sales Through a Registrant - Section 128(c) of the *Securities Rules* provides a prospectus exemption for an issuer that uses a person registered under the *Securities Act* to sell securities in amounts of at least \$25,000. The registrant must be qualified to sell the securities that are being offered. Unlike the other exemptions discussed, a corresponding registration exemption is not provided.

Once again, the issuer must deliver an offering memorandum to the purchaser, must file the offering memorandum and a Form 20 with the Commission within ten days of the distribution and must obtain a Form 20A from each purchaser. In the Form 20A, the purchaser must identify the registrant who acted for him or her in the purchase of the securities.

2.7 Employee exemption - Sections 45(2)(10) and 74(2)(9) of the *Securities Act* provide registration and prospectus exemptions where the trade is by an issuer in a security of its own issue with an employee, senior officer or director of the issuer so long as the person is not induced to purchase by expectation of employment or continued employment.

The employee exemption is available to an issuer for a trade to a *bona fide* employee. The following persons would be considered *bona fide* employees:

(a) an individual who is considered an employee under the *Income Tax Act* and for whom income tax is deducted at source;

(b) an individual who is a full-time or part-time dependent contractor (who provides services normally provided by an employee and who works under the same control and direction as an employee of the issuer but for whom income tax is not deducted at source).

2.8 Rights offering exemption - Sections 45(2)(8) and 74(2)(7) of the *Securities Act* provide registration and prospectus exemptions where the trade is by an issuer

in a right granted by the issuer to holders of its securities to purchase additional securities of its own issue, if the issuer gives written notice to the Executive Director stating the details of the proposed trade.

Further details of the rights offering exemption, including the required form of disclosure to security holders, is set out in proposed National Instrument 45-101 *Rights Offerings*, which was published for comment on November 21, 1997, or any successor instrument.

2.9 Redemption by the issuer - Sections 45(2)(29) and 74(2)(27) of the *Securities Act* provide registration and prospectus exemptions where the trade is in a security to the issuer of the security pursuant to the purchase, redemption or acquisition of the security by the issuer.