

September 30, 2011

## Who is an Accredited Investor? What the Corporation should know.

*By: David J. Lowdon*

The Ontario Securities Commission (the “OSC”) recently published Staff Notice 33-735 “Sale of Exempt Securities to Non-Accredited Investors” (the “Staff Notice”). The Staff Notice outlines the OSC’s concern that dealers and corporations may be solely relying on an investor’s assurance that the investor is an accredited investor when selling securities under the accredited investor exemption.

The accredited investor exemption allows corporations to issue securities from treasury in return for cash without the costly requirement to provide the investor with a prospectus or an offering memorandum. Issuing shares under the accredited investor exemption provides the financial underpinning for many small public and private corporations. To fall within this exemption, investors must fit into one of the narrowly defined categories of an accredited investor. One of the most often used accredited investor definitions is: “an individual who, either alone or with a spouse, beneficially owns, directly or indirectly, **financial assets** having an aggregate realizable value that before taxes, but **net of any related liabilities** exceeds \$1,000,000.”

The Staff Notice emphasizes the difference between the phrase “financial assets” and the phrase “net assets”, which is used in certain other accredited investor definitions – stressing that the value of an investor’s personal residence or other real estate must not be included in the calculation of financial assets when calculating whether an individual beneficially owns financial assets having an aggregate value before taxes but net of any related liabilities that exceeds \$1,000,000. The Staff Notice suggests, probably correctly, that many people checking off the afore-mentioned “millionaire” definition in the accredited investor certificate they are completing do not understand this distinction.

The Staff Notice states it is not sufficient for dealers or corporations to rely solely on the investor’s initials or other indication in the appropriate box of an accredited investor certificate to determine whether or not the investor does in fact meet the definition of an accredited investor. Dealers and corporations must ensure the investor understands the distinction between “financial assets” and “net assets” and dealers and corporations should make clear to investors that the value of their personal residence or other real estate can not be included when calculating their financial assets to see if they meet the definition.

A dealer or corporation must take reasonable steps beyond simply obtaining a completed accredited investor certificate to ensure that an investor is indeed an accredited investor. For dealers, this usually takes the form of completing a know your client (“**KYC**”) form. Corporations issuing securities in a private placement on a non-brokered basis without the services of a dealer should also consider developing and using a KYC form, in addition to obtaining an accredited investor certificate, to ensure



PERLEY-ROBERTSON,  
HILL & MCDUGALL LLP/s.r.l.

the corporation has proof of a due diligence inquiry into an investor's assertion that he or she is an accredited investor.

OSC Staff Notices are generally a forewarning that the OSC is going to take a renewed and more searching interest in a particular subject. Corporations should be aware that, in future, the OSC is likely to ask how they have satisfied themselves that investors alleging to be accredited investors are in fact accredited investors. Your lawyer can help you with that.

*David is a lawyer in our Corporate Law Group and can be reached at [dlowdon@perlaw.ca](mailto:dlowdon@perlaw.ca) or 613.566.2809.*