



STAFF NOTICE 45-704

REVIEW OF OFFERING MEMORANDA UNDER MI 45-103 *CAPITAL RAISING EXEMPTIONS*

Background

Multilateral Instrument 45-103 *Capital Raising Exemptions* (“MI 45-103”) came into force on June 16, 2003. It contains four new exemptions from the prospectus and registration requirements that issuers can use to raise capital. One of the exemptions, the “Offering Memorandum Exemption” permits issuers to sell its own securities to investors in Saskatchewan using an offering memorandum. Each investor must receive a copy of an offering memorandum (“OM”) prepared in accordance with MI 45-103. Issuers are not required to have Commission staff review the OM before they use it.

In Staff Notice 45-703 we set out how we will monitor the use of exemptions under MI 45-103. We stated that we will review offering memoranda filed by issuers who have their head office in Saskatchewan to confirm that they contain the disclosure required in the offering memorandum form.

In the past 18 months we have selected a sample of OMs filed under MI 45-103, and have reviewed them. All of the OM’s reviewed were filed by non-qualifying issuers under MI 45-103. Non-qualifying issuers are issuers that are not reporting issuers. For all issuers, this was their first offering of securities.

This Staff Notice sets out the results of our review of the OMs filed by these non-qualifying issuers.

General Comments

Staff identified material disclosure deficiencies in all of the OMs reviewed. In general, the OMs were poorly prepared and did not provide the disclosure required.

If issuers trade securities under an OM that does not comply with MI 45-103, they have not met the requirements of the OM Exemption, and the trade will be illegal.

Individuals preparing an OM under MI 45-103 should read the relevant sections of the MI, Companion Policy 45-103CP, Form 45-103F1, and the Instructions for Completing Form 45-103F1 before they attempt to prepare an OM.

Form 45-103F1 provides an Item-by-Item guide about what information to provide in the offering memorandum, with the form providing instruction within each Item. Accompanying the Form are Instructions for Completing Form 45-103F1. These Instructions provide additional

guidance in completing the Form, as well as substantial guidance on financial statement disclosure requirements for the OM. The Companion Policy 45-103CP provides further detailed guidance for issuers preparing an OM.

If issuers or issuers' professional advisers have questions on the disclosure requirements for these OMs, we encourage them to contact the staff in the Corporation Finance Branch of the Commission's Securities Division to discuss their questions before they prepare or use the OM to sell securities.

Consequences to Issuers of failing to comply with the OM disclosure requirements

The following are the main consequences for issuers who fail to comply with the OM disclosure requirements:

1. *Offering suspended.* Staff may request that the offering be suspended until investors are provided with proper disclosure.
2. *Remedial information provided.* Staff may request that an issuer provide remedial information to investors.
3. *OM amended and redelivered.* Staff may request that the OM and related documents be amended and delivered to investors.
4. *Money refunded.* Staff may request that the issuer refund investors' money to them.
5. *Cease trade order.* The Director may issue an order that the issuer cease trading in securities.
6. *Enforcement hearing before the Commission.* Staff may take the parties signing a certificate in an OM to a hearing before the Commission. The Commission has the ability to levy sanctions against these parties, including removing their right to use exemptions, and imposing an administrative penalty of up to \$100,000.00
7. *Civil action.* If an OM contains a misrepresentation, investors have a right of action against everyone who signed the certificate in an OM. Also, if an offering of securities is made in contravention of the Act, investors have a right of action pursuant to section 141.

Summary of Disclosure Deficiencies

The following are our observations based upon a review of a sample selection of offering memorandums filed under MI 45-103:

General Disclosure Problems

1. Failure to follow the form Items. (Refer to Form 45-103F1).

2. Failure to follow the order of the Form Items. (Refer to A.2 of the Instructions for Completing Form 45-103F1).
3. Failure to follow the Instructions for Completing Form 45-103F1, which is attached to Form 45-103F1.
4. Failure to follow the guidance outlined in Companion Policy 45-103CP.
5. General lack of attention to detail, poorly prepared, disorganized. (Refer to the General Instructions of Instructions for Completing Form 45-103F1).
6. *Attachments.* The majority of OM's had many attachments and appendices (eg: projections, financial statements, and summaries of other pertinent information to the investment being offered). In many cases, Form 45-103F1 disclosure was partially provided in the body of the OM, and the balance was provided in an attachment. In most cases, this information should have been provided in the body of the OM, as required by Form 45-103F1, and the Instructions for Completing Form 45-103F1. Providing the required information in one location substantially improves the readability of the OM. Where attachments are necessary (eg: providing a fully copy of the limited partnership agreement) the attachments must be incorporated by reference into the OM.

Material Agreements

7. Failure to properly summarize key terms of material agreements in the OMs in a manner that will fully inform investors. (Refer to Item 2.7 of Form 45-103F1).
8. Failure to properly identify material agreements as material agreements, and provide the details in the OM to properly inform investors. (Refer to Item 2.7 of Form 45-103F1).

Projections

9. Failure to provide an audit report on projections included in the OM. (Refer to B.12 of Instructions for Completing Form 45-103F1).
10. Audit reports on projections included in an OM referred to an incorrect number of years. (Refer to AuG-6 Examination of a financial forecast or projection included in a prospectus or other offering document, CICA Handbook).
11. Audit reports on projections were not clearly identified as audit reports. (Refer to AuG-6 Examination of a financial forecast or projection included in a prospectus or other offering document, CICA Handbook).
12. Audit reports referred to the hypotheses and assumptions accompanying the projections when there are no hypotheses provided. (Refer to AuG-6 and Section 4250 – Future Oriented Financial Information in the CICA Handbook).
13. Audit Report did not cover all of the various projected statements/schedules provided in the OM. Eg. Schedules projecting tax benefits.

14. Figures provided in projections were not arithmetically correct in relation to the supporting assumptions on calculation methodology.
15. Narrative body of the offering memorandum indicated that projections were not audited, when in fact they were audited.
16. Narrative provided in the body of the offering memorandum contradicted details provided in the projections.
17. Projections included in the OM were not accompanied by the supporting hypothesis and assumptions, making them of little use to investors. (Refer to National Policy 48 – Future Oriented Financial Information, and Section 4250 – Future Oriented Financial Information CICA Handbook).
18. Projections included in the OM were based upon an offering size that differs from that contemplated by the narrative of the OM.
19. It was not clearly distinguished whether projected cash distributions to investors were a return of original capital invested, or based upon operating earnings.
20. Projections covered an unreasonably lengthy period of time. (Refer to Section 4250 – Future Oriented Financial Information in the CICA Handbook).

Financial Statements

21. No financial statements of the issuer were included in the OM. (Refer to B. Financial Statements – General, of the Instructions for Completing Form 45-103F1).
22. No financial statements of companies to be acquired were included in the OM. (Refer to C. Financial Statements – Business Acquisitions of Instructions for Completing Form 45-103F1).
23. No financial statements of the general partner were included in the offering memorandum. (Refer to Clause 13 of B. Financial Statements – General, of the Instructions for Completing Form 45-103F1).

Investors Rights / Certificates

24. Failure to properly document investors' rights in the OM, in terms of the parties that may be sued if there is a misrepresentation. (Refer to MI45-103, Part 4 Offering Memorandum Exemption, and Item 11 of Form 45-103F1).
25. In the case of offerings by limited partnerships, there was failure to provide required certificates of the issuer, general partner, and promoters. (Refer to Item 13 of Form 45-103F1, General Instruction A.6 of Instructions for Completing Form 45-103F1, and 4.4 of Companion Policy 45-103CP).

26. Audit reports on projections and financial statements were dated by the auditor on a more current date than that provided on the certificate of the issuer, raising questions on the validity of the certificate provided.

Other

27. Structuring the offering as an indirect offering, with little detail in the OM on the actual operating company/providing financial statements for the actual operating company, or the investment details in the operating company. (Refer to 1.8 of Companion Policy 45-103).
28. Complete failure to properly describe the indirect investment and how returns will be calculated on that investment.
29. Describing securities as redeemable without providing details on how the redemption will be funded and possible effects on the overall investments of the issuer.
30. Using the 45-103 OM for a continuous offering, without updating the OM for material changes, effectively resulting in the marketing of securities with a stale dated OM. (Refer to 4.4 Of Companion Policy 45-103CP).

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Contact:

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