

# Staying Onside the Regulation D Bad Boy Disqualifications

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Most non-underwritten private placements of securities by Canadian companies to U.S. investors are made in reliance upon Rule 506 of Regulation D. Since September 2013, this exemption has been subject to “bad boy disqualifications.” Generally speaking, a company is prohibited from relying on Rule 506 if the company, any of its predecessors, any of its affiliated issuers, or any of its directors, officers, general partners, managing members or promoters has been subject to certain convictions, orders, judgments, decrees in the United States or suspension or expulsion of membership from certain organizations in the United States. In addition, if any person has been or will be paid (directly or indirectly) remuneration for solicitation of purchasers in the Rule 506 offering, then the offering will generally not qualify for Rule 506 if the person being paid, any general partner or managing member of such person or any director or officer of any of the foregoing has been subject to any such disqualifying events. A limited exception exists if the event occurred prior to September 2013 and is appropriately disclosed to prospective purchasers prior to the sale.

Canadian companies that want to ensure the availability of Rule 506 should ask their directors, officers, 20% beneficial shareholders, general partners, managing members and promoters to periodically complete an appropriate Rule 506 bad boy questionnaire. We recommend that companies obtain a completed questionnaire from such persons at least annually, and that a questionnaire be completed by any person who newly becomes subject to the requirements (e.g., a newly appointed officer or a shareholder who first becomes a 20% beneficial shareholder). An appropriate form of questionnaire is available to clients upon request.

In addition, Canadian companies should not agree to pay any person any remuneration or commission (directly or indirectly) for soliciting purchasers in a Rule 506 offering (e.g., an underwriter, agent or “finder”), unless it is first confirmed that the person is a U.S. registered broker-dealer that is legally permitted to receive such a commission and the parties enter into an appropriate contract in which the person confirms that no bad boy disqualifications are applicable. Companies should seek U.S. counsel’s advice on the

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appropriate language.