

Notice No. 45-712

NOTICE AND REQUEST FOR COMMENT

**NOVA SCOTIA SECURITIES COMMISSION POLICY 45-601
COMMUNITY ECONOMIC DEVELOPMENT INVESTMENT FUNDS**

November 28, 2013

Introduction

The Nova Scotia Securities Commission (the "Commission") is proposing to adopt Nova Scotia Securities Commission Policy 45-601 Community Economic Development Investment Funds (the "Policy") and issue the corresponding Blanket Order No. 45-521 (the "Blanket Order") which is attached as Schedule A to the Policy.

The Policy is attached to this notice and is available on the Commission's website under Policies <http://nssc.gov.ns.ca/nssc-securities-law-policy/policies/>.

Background

Community Economic Development Investment Funds ("CEDIFs") sell shares to security holders and invest the proceeds. CEDIFs that do not seek to exercise control or actively manage the persons or companies (the "entities") they invest in, are classified as investment funds under the *Securities Act*, R.S.N.S. 1989, c. 418, as amended (the "Securities Act"). A number of existing CEDIFs are currently investment funds as defined in the Securities Act.

Under subsection 31(3) of the Securities Act, a person or company that directs the business, operations or affairs of an investment fund must be registered as an investment fund manager. The requirements in Nova Scotia securities laws relating to the registration of investment fund managers were implemented on September 28, 2009, subsequent to the creation of many existing CEDIFs.

Nova Scotia securities laws impose requirements on investment funds and investment fund managers designed to protect investors in such funds. These requirements include filing detailed disclosure and material change reports, appointment of a chief compliance officer that meets specified competency requirements, maintaining minimum capital amounts, and holding stipulated levels of insurance. CEDIFs that are investment funds may have difficulty meeting these requirements.

To facilitate the operation of the Province's CEDIF program while fulfilling the Commission's investor protection mandate, the Commission proposes to adopt the Policy and issue the Blanket Order.

Substance and Purpose

Investment funds are generally considered to be funds, similar to mutual funds, that pool assets from a number of investors and then passively invest those assets. An investment fund does not seek to exercise control or actively manage the persons or companies (the "entities") it invests in. A CEDIF that does not seek to exercise control or actively manage the entities it invests in is classified as an investment fund under the Securities Act.

The Policy sets out the three situations where a CEDIF that is an investment fund that does not comply with the investment fund requirements in Nova Scotia securities laws can be exempted from these requirements. To be exempt, the CEDIF must:

1. specify with particularity in its offering document the investments that the CEDIF will make or has made with the capital raised and obtain security holder approval for any subsequent changes to the investments;
2. limit the amount of capital raised by the CEDIF under each offering to not more than \$3,000,000.00 and the amount of capital raised by the CEDIF and any affiliated CEDIFs under all exemptions from the prospectus requirement to not more than \$6,000,000.00 in aggregate; or
3. if it is a CEDIF in existence on the effective date of the Policy (the "Effective Date") that is not in compliance with section 1 or 2 on the Effective Date, or it is a CEDIF that becomes non-compliant with section 2 after the closing of its first offering of securities, provide written notice (the "Notice") to its security holders describing with particularity the investments that the CEDIF has made with the capital raised and obtain security holder approval for any subsequent changes to the investments. The Notice is to be provided no later than the date the CEDIF is required to send out its materials for the next annual general meeting following the date that the CEDIF became non-compliant.

A CEDIF that chooses to rely on the exemptions described in the Policy must include a specific warning in its offering document or the Notice, as applicable, to advise investors that the CEDIF will not be required to comply with the requirements of an investment fund manager and therefore, when investors purchase or own shares in the CEDIF, they should be aware that they will not have the protections of the requirements and standards imposed on registered investment fund managers.

There is also a condition that the CEDIF and any other affiliated CEDIFs may raise no more than \$10,000 per beneficial investor per calendar year in aggregate, unless the investor is an accredited investor or an officer, director or promoter of the CEDIF.

Alternatives Considered

An alternative is to have CEDIFs comply with the investment fund requirements in Nova Scotia securities laws. This could be onerous for the CEDIFs and could detrimentally affect the Province's CEDIF program as some CEDIFs would likely not have the expertise or resources to comply with these requirements.

Anticipated Costs and Benefits

The Policy reflects the balancing of the interests of investor protection and fostering the process of capital formation. With the adoption of the Policy, Nova Scotia investors in CEDIFs that are investment funds exempt under the Policy will not have the protections of Nova Scotia securities laws for an offering of securities of an investment fund. However, the Policy is restricted to CEDIF investment funds that have disclosed the entities they propose to invest in or have invested in and therefore do not have the discretion to manage the investments or to CEDIF investment funds that have raised no more than \$6,000,000.00 using exemptions from the prospectus requirements.

Additionally, a non-accredited investor in CEDIFs that are investment funds exempt under the Policy can only invest up to \$10,000 per calendar year in aggregate, which limits the investor's potential loss. Accredited investors do not have a limit on the amount they can invest because they are better able to withstand loss than most investors. These limits may impact the amount of money that a CEDIF exempt under the Policy can raise.

Comments

We welcome your comments on the Policy. Please send your comments in writing by **Tuesday, December 31, 2013**, to:

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Nova Scotia Securities Commission Policy 45-601 Community Economic Development Investment Funds

1. Introduction

- 1.1. Community Economic Development Investment Funds (“CEDIFs”) sell shares to security holders and invest the proceeds. CEDIFs that do not seek to exercise control or actively manage the persons or companies (the “entities”) they invest in are classified as investment funds under the *Securities Act*, R.S.N.S. 1989, c. 418, as amended (the “Securities Act”). A number of existing CEDIFs are currently investment funds as defined in the Securities Act.
- 1.2. Under subsection 31(3) of the Securities Act, a person or company that directs the business, operations or affairs of an investment fund must be registered as an investment fund manager.
- 1.3. Nova Scotia securities laws impose requirements on investment funds and investment fund managers designed to protect investors in such funds. These requirements include filing detailed disclosure and material change reports, appointment of a chief compliance officer that meets specified competency requirements, maintaining minimum capital amounts, and holding stipulated levels of insurance.
- 1.4. The requirements in Nova Scotia securities laws relating to the registration of investment fund managers were implemented on September 28, 2009, subsequent to the creation of many existing CEDIFs.
- 1.5. To facilitate the operation of the Province’s CEDIF program while fulfilling the Commission’s investor protection mandate, the following conditions will apply to existing CEDIFs that are investment funds as defined in the Securities Act that are not in compliance with Nova Scotia securities laws for investment funds, and to all new offerings of securities by CEDIFs that are investment funds as defined in the Securities Act.

2. Definition of Investment Fund

- 2.1. CEDIFs that invest for the purpose of exercising or seeking to exercise control of the entities they invest in, or for the purpose of being actively involved in the management

of the entities they invest in, are not investment funds under the Securities Act and are not subject to this policy.

2.2. Whether a CEDIF is “exercising or seeking to exercise control of” or “actively involved in the management of” the entities it invests in is a question of fact that will depend on a number of factors including the ownership structure of the entity, the existence and content of shareholder or management agreements, the proportion of voting shares owned by the CEDIF and the proportion of voting shares owned by other block shareholders, among other indicia of control or management. For the purposes of this policy, examples of how a CEDIF may exercise or seek to exercise control of the entities that it invests in or may be actively involved in the management of the entities that it invests in include:

2.2.1. representation on the board of directors of the entities,

2.2.2. direct involvement in the appointment of managers of the entities,

2.2.3. the right to be consulted on material management decisions of the entities, or

2.2.4. the right to elect a board of directors and vote on corporate policy of the entities.

2.3. For the purposes of this policy, the mere fact of ownership of shares that represent less than a majority of the voting shares of an entity, in the absence of other indicia of control, is not sufficient to demonstrate that a CEDIF is exercising or seeking to exercise control of the entity or is actively involved in the management of the entity.

2.4. Whether a CEDIF controls, seeks to exercise control or actively manages the entities it invests in may change over time. It is the responsibility of the CEDIF to ensure that it is in compliance with Nova Scotia securities laws, including this policy, at all times.

3. Conditions for Exemption from Investment Fund Requirements

3.1. A CEDIF that does not invest for the purpose of exercising or seeking to exercise control of the entities it invests in and does not invest for the purpose of being actively involved in the management of the entities it invests in is an investment fund under the Securities Act and must comply with Nova Scotia securities laws relating specifically to investment funds unless one of the following conditions is met:

3.1.1. a) the offering document for the CEDIF specifies with particularity the investments that the CEDIF will make with the capital raised and any capital previously raised, including:

- i) the names of the entities invested in and to be invested in,
- ii) a description of the entities invested in and to be invested in, including information relating to the entities' activities, management and financial position,
- iii) the amount or percentage of the CEDIF's assets invested in and to be invested in each entity, and
- iv) a description of all potential material conflicts of interest for each officer, director, promoter or key person of the CEDIF with each entity invested in and to be invested in,

(collectively, the "Investee Information"),

b) prior to any change in these investments, the change must be approved by at least 50% plus 1 vote of the votes cast by security holders of the CEDIF who vote at a meeting of security holders called to consider the change, excluding the shares voted by officers, directors and promoters and parties related to the officers, directors and promoters, and

c) for the meeting referred to in paragraph b) above, if the CEDIF proposes to make new investments in entities, it has provided to its security holders, together with the materials for the meeting, the Investee Information relating to the entities that the CEDIF proposes to invest in,

3.1.2. the amount of capital raised by the CEDIF under each offering must not exceed \$3,000,000.00 and the amount of capital raised by the CEDIF and any affiliated CEDIFs, within the meaning in the *Equity Tax Credit Act* (Nova Scotia), under all exemptions from the prospectus requirement must not exceed \$6,000,000.00 in aggregate, or

3.1.3. a) for a CEDIF in existence on the effective date of this policy (the "Effective Date") that is not in compliance with section 3.1.1 or 3.1.2 on the Effective Date, or for a CEDIF that becomes non-compliant with section 3.1.2 after the closing of its first offering of securities (the date of non-compliance referred to hereafter as the "Date of Non-compliance"), the CEDIF provides a written notice (the "Notice")

containing the Investee Information for the entities it has invested in as of the Date of Non-compliance to all of its security holders no later than the date the CEDIF is required to send out its materials for the next annual general meeting following the Date of Non-compliance,

b) prior to any change in the investments as of the Date of Non-compliance, the change must be approved by at least 50% plus 1 vote of the votes cast by security holders of the CEDIF who vote at a meeting of security holders called to consider the change, excluding the shares voted by officers, directors and promoters and parties related to the officers, directors and promoters,

c) for the meeting referred to in paragraph b) above, if the CEDIF proposes to make new investments in entities, it has provided to its security holders, together with the materials for the meeting, the Investee Information relating to the entities that the CEDIF proposes to invest in, and

d) for any subsequent offering of securities by the CEDIF, the CEDIF satisfies the conditions in section 3.1.1.

3.2. A CEDIF that is an investment fund that satisfies one of the conditions in section 3.1 of this policy must include in its offering document or the Notice, as applicable, the following warning:

“WARNING: Unlike most investment funds, this fund will not be required to comply with the requirements of an investment fund manager provided the fund complies with Nova Scotia Securities Commission Policy 45-601 Community Economic Development Investment Funds. Other investment funds are required to have registered investment fund managers to afford investors a level of protection that is not present in this investment.

When investors purchase or own shares in this fund they should be aware that they will not have the protections of the requirements and standards imposed on registered investment fund managers under Nova Scotia securities laws which include:

- a) meeting experience and education requirements,
- b) complying with investment fund reporting requirements,
- c) employing a chief compliance officer,
- d) maintaining minimum levels of working capital,

- e) maintaining specified levels of insurance or bonding, and
- f) undergoing Commission compliance reviews.”

3.3. A CEDIF that is an investment fund that satisfies one of the conditions in section 3.1 of this policy, together with any other affiliated CEDIFs, may raise no more than \$10,000 per beneficial investor per calendar year in aggregate, unless the investor meets the definition of an accredited investor under National Instrument 45-106 *Prospectus and Registration Exemptions*, or is an officer, director or promoter of the CEDIF.

3.4. CEDIFs that are investment funds remain subject to all Nova Scotia securities laws otherwise applicable to CEDIFs.

3.5. A blanket order implementing this policy is attached as Schedule A.

4. Effective date

4.1. This policy is effective on _____, 2014.

Dated at Halifax, Nova Scotia, this ____ day of _____, 2014.

Nova Scotia Securities Commission

Sarah P. Bradley, Chair

Paul Radford, Q.C., Vice-chair

Schedule A

Blanket Order No. 45-521

In the Matter of the *Securities Act*, R.S.N.S. 1989,
Chapter 418, as amended

-and-

In the Matter of
Nova Scotia Securities Commission Policy 45-601
Community Economic Development Investment Funds

Order
(Section 151A)

Interpretation

1. Terms defined in the *Securities Act*, R.S.N.S. 1989, Chapter 418, as amended (the “Securities Act”) and National Instrument 14-101 *Definitions* have the same meaning in this order.

2. In this order:

“CEDIF” means a community economic development investment fund that makes or has made an offering of securities under the *Community Economic-Development Corporations Regulations*, N.S. Reg. 168/2011.

“entity” means a person or company that a CEDIF invests in.

“exempt CEDIF” means a CEDIF that does not invest for the purpose of exercising or seeking to exercise control of the entities it invests in and does not invest for the purpose of being actively involved in the management of the entities it invests in and is therefore an investment fund under the Securities Act that must comply with Nova Scotia securities laws relating specifically to investment funds unless one of the following conditions is met:

1. a) the offering document for the CEDIF specifies with particularity the investments that the CEDIF will make with the capital raised and any capital previously raised, including:
 - i) the names of the entities invested in and to be invested in,
 - ii) a description of the entities invested in and to be invested in, including information relating to the entities' activities, management and financial position,
 - iii) the amount or percentage of the CEDIF's assets invested in and to be invested in each entity, and
 - iv) a description of all potential material conflicts of interest for each officer, director, promoter or key person of the CEDIF with each entity invested in and to be invested in,(collectively, the "Investee Information"),
 - b) prior to any change in these investments, the change must be approved by at least 50% plus 1 vote of the votes cast by security holders of the CEDIF who vote at a meeting of security holders called to consider the change, excluding the shares voted by officers, directors and promoters and parties related to the officers, directors and promoters, and
 - c) for the meeting referred to in paragraph b) above, if the CEDIF proposes to make new investments in entities, it has provided to its security holders, together with the materials for the meeting, the Investee Information relating to the entities that the CEDIF proposes to invest in,
2. the amount of capital raised by the CEDIF under each offering must not exceed \$3,000,000.00 and the amount of capital raised by the CEDIF and any affiliated CEDIFs, within the meaning in the *Equity Tax Credit Act* (Nova Scotia), under all exemptions from the prospectus requirement must not exceed \$6,000,000.00 in aggregate, or
3. a) for a CEDIF in existence on the effective date of Nova Scotia Securities Commission Policy 45-601 Community Economic Development Investment Funds (the "Effective Date") that is not in compliance with section 1 or 2 of this definition on the Effective Date, or for a CEDIF that becomes non-compliant with section 2 of this definition after the closing of its first offering of securities (the date of non-compliance referred to hereafter as the "Date of Non-compliance"), the CEDIF provides a written notice (the "Notice") containing the Investee Information for the entities it has invested in as of the

Date of Non-compliance to all of its security holders no later than the date the CEDIF is required to send out its materials for the next annual general meeting following the Date of Non-compliance,

b) prior to any change in the investments as of the Date of Non-compliance, the change must be approved by at least 50% plus 1 vote of the votes cast by security holders of the CEDIF who vote at a meeting of security holders called to consider the change, excluding the shares voted by officers, directors and promoters and parties related to the officers, directors and promoters,

c) for the meeting referred to in paragraph b) above, if the CEDIF proposes to make new investments in entities, it has provided to its security holders, together with the materials for the meeting, the Investee Information relating to the entities that the CEDIF proposes to invest in, and

d) for any subsequent offering of securities by the CEDIF, the CEDIF satisfies the conditions in section 1 of this definition.

Background

1. CEDIFs sell shares to security holders and invest the proceeds. CEDIFs that do not seek to exercise control or actively manage the entities they invest in are classified as investment funds under the Securities Act.

2. Under subsection 31(3) of the Securities Act, a person or company that directs the business, operations or affairs of an investment fund must be registered as an investment fund manager.

3. Nova Scotia securities laws impose requirements on investment funds and investment fund managers designed to protect investors in such funds. These requirements include filing detailed disclosure and material change reports, appointment of a chief compliance officer that meets specified competency requirements, maintaining minimum capital amounts, and holding stipulated levels of insurance.

4. The requirements in Nova Scotia securities laws relating to the registration of investment fund managers were implemented on September 28, 2009, subsequent to the creation of many existing CEDIFs.

5. The issuance of this blanket order facilitates the operation of the Province's CEDIF program while fulfilling the Commission's investor protection mandate, for CEDIFs that are investment

funds as defined in the Securities Act that are not in compliance with Nova Scotia securities laws for investment funds, and to all new offerings of securities by CEDIFs that are investment funds as defined in the Securities Act.

6. The Commission is of the opinion that to do so is not prejudicial to the public interest.

Order

IT IS ORDERED pursuant to subsection 151A(1) of the Act that an exempt CEDIF is exempted from the requirements in Nova Scotia securities laws applicable to investment funds and investment fund managers provided that:

1. the exempt CEDIF includes in its offering document or the Notice, as applicable, the following warning:

"WARNING: Unlike most investment funds, this fund will not be required to comply with the requirements of an investment fund manager provided the fund complies with Nova Scotia Securities Commission Policy 45-601 Community Economic Development Investment Funds. **Other investment funds are required to have registered investment fund managers to afford investors a level of protection that is not present in this investment.**

When investors purchase or own shares in this fund they should be aware that they will not have the protections of the requirements and standards imposed on registered investment fund managers under Nova Scotia securities laws which include:

- a) meeting experience and education requirements,
- b) complying with investment fund reporting requirements,
- c) employing a chief compliance officer,
- d) maintaining minimum levels of working capital,
- e) maintaining specified levels of insurance or bonding, and
- f) undergoing Commission compliance reviews.”;

2. the exempt CEDIF, together with any other affiliated CEDIFs, may raise no more than \$10,000 per beneficial investor per calendar year in aggregate, unless the investor meets the definition of an accredited investor under National Instrument 45-106 *Prospectus and Registration Exemptions*, or is an officer, director or promoter of the CEDIF; and

3. the exempt CEDIF remains subject to all Nova Scotia securities laws otherwise applicable to CEDIFs.

Dated at Halifax, Nova Scotia, this day of , 2014.

Nova Scotia Securities Commission

Sarah P. Bradley, Chair

Paul Radford, Q.C., Vice-chair