

Notice No. 45-714

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

January 17, 2014

Introduction

On January 17, 2014, following a public consultation process, the Nova Scotia Securities Commission (the "Commission") adopted Nova Scotia Securities Commission Policy 45-601 Community Economic Development Investment Funds (the "Policy") and issued the corresponding Blanket Order No. 45-521 (the "Blanket Order"), a copy of which is attached as Schedule A to the Policy.

The Policy is attached to this notice as Annex A 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.

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

The Province's CEDIF program is intended to encourage capital raising by small, community based issuers run by non-professional managers. To facilitate the operation of the CEDIF program while fulfilling the Commission's investor protection mandate, the Commission has adopted the Policy and issued 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 can be exempted from the investment fund requirements in Nova Scotia securities laws . To be exempted, the CEDIF must satisfy the requirements of one of the following:

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 (a “Specified CEDIF”).
2. Limit the amount of capital raised by the CEDIF under each offering to not more than \$3,000,000 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 in aggregate.
3. If it is a CEDIF in existence on the effective date of the Policy (the “Effective Date”) that has not satisfied one of the requirements set out above on the Effective Date, or it is a CEDIF that is not a Specified CEDIF and exceeds the capital raising limits set out above 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 the materials for its 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 \$15,000 per beneficial investor per calendar year in aggregate or \$30,000 per beneficial investor per calendar year in aggregate if the investor receives advice from a registered investment dealer or exempt market dealer. These investment limits do not apply to an investor that is an accredited investor or an officer, director or promoter of the CEDIF.

Summary of Comments and Responses

The proposed Policy was published for comment on November 28, 2013, in Notice No. 45-712. We received submissions from 13 commenters. Copies of the comment letters can be found on the Commission's website.

We have considered the comments received and thank all of the commenters for their input. A list of the commenters together with a summary of the comments and our responses is attached as Annex B to this notice.

Summary of Changes to the Policy

After considering the comments, we made the following key changes in the Policy:

1. In section 2.2, we provided examples of exercising or seeking to exercise control where the entity that a CEDIF invests in is a limited partnership; and
2. In section 3.3, the limit for investment by an unaccredited investor has been raised to \$15,000 per beneficial investor and the limit for investment by an unaccredited investor purchasing through a registered investment dealer or exempt market dealer has been raised to \$30,000 per beneficial investor. These investment limits do not apply to an officer, director or promoter of the CEDIF.

Questions

If you have any questions regarding the Policy, please contact:

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Annex A

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. The Province’s CEDIF program is intended to encourage capital raising by small, community based issuers run by non-professional managers. To facilitate the operation of the 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 be exercising or seeking 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, or where an entity is a limited partnership, representation on the board of directors of the general partner of the limited partnership;

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 or where an entity is a limited partnership, the right to elect a board of directors and vote on corporate policy of the general partner of the limited partnership.

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 is exercising or seeking to exercise control of or actively involved in the management of 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 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 in aggregate.
- 3.1.3. 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 is not in compliance with section 3.1.1 and 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:

- a) 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 under the *Community Economic-Development Corporations Regulations*, N.S. Reg. 168/2011, 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:

- a) \$15,000 per beneficial investor per calendar year in aggregate, or
- b) \$30,000 per beneficial investor per calendar year in aggregate if the investor has obtained advice regarding the suitability of the investment from a person or company registered as an investment dealer or exempt market dealer authorized to sell securities of the CEDIF.

These investment limits do not apply to an investor that 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.

4. Implementation

4.1 A copy of the blanket order implementing this policy is attached as Schedule A.

5. Effective date

5.1. This policy is effective on January 17, 2014.

Dated at Halifax, Nova Scotia, this 17th day of January, 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 CEDIF Regulations.

“CEDIF Regulations” means 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 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 in aggregate.
 3. 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 is not in compliance with section 1 of this definition and 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:

- a) 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 under the CEDIF Regulations, 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 Province's CEDIF program is intended to encourage capital raising by small, community based issuers run by non-professional managers. The issuance of this blanket order facilitates the operation of the CEDIF program while fulfilling the Commission's investor protection mandate and applies to 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:
 - a) \$15,000 per beneficial investor per calendar year in aggregate, or
 - b) \$30,000 per beneficial investor per calendar year in aggregate if the investor has obtained advice regarding the suitability of the investment from a person or company registered as an investment dealer or exempt market dealer authorized to sell securities of the CEDIF,except that these investment limits do not apply to an investor that 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 17th day of January, 2014.

Nova Scotia Securities Commission

Sarah P. Bradley, Chair

Paul Radford, Q.C., Vice-chair

Annex B

Summary of Comments and Responses **Policy 45-601 Community Economic Development Investment Funds**

List of Commenters

The Northumberland Wind Field Inc.

The Chebucto Wind Field Inc.

Peter Hickleton

The Canadian Advocacy Council for Canadian CFA Institute Societies

Farmworks Investment Co-operative Limited

Wayne Stobo

CEDIF Management Ltd.

Wind4All

McInnes Cooper

Assante Capital Management Ltd.

Dept of Energy

Terry Norman

Sarah Greenwood

We thank all commenters for their comments.

In this summary of comments and responses, we categorized similar comments we received on our proposed policy into broad themes and described these themes in the headings to the comments. Following our discussion of these themes and the comments, we set out the Nova Scotia Securities Commission (“NSSC”) responses.

Where appropriate, suggestions relating to non-substantive drafting changes have been made. Some commenters also took this opportunity to comment on issues outside of this policy, and we have responded separately to these commenters.

Application of control test to limited partnerships

Some commenters expressed concern that the limited partnership model used by many wind fields excludes the Community Economic Development Investment Funds (“CEDIFs”) from control and recommended an addition to 2.2.1 allowing the CEDIF to demonstrate “control” through representation on the board of directors of a limited partnership’s general partner.

Response

The policy has been amended in section 2.2. In order to demonstrate control, the CEDIF must have either (or both):

- a contractual right to representation on the board of the general partner and exercise that right; or
- the right to vote by 50%+1 to change the general partner.

We note that there is a possibility that exercising this control could have implications for the liability of the limited partners, and CEDIFs should consult legal counsel on this matter.

Additional regulatory burden on CEDIFs

One commenter expressed concern that the description of the information required by section 3.1 of the proposed policy and the retroactive requirement for the information presents an unmanageable burden for CEDIFs.

Response

Although the CEDIF program is intended to encourage capital raising by small, community based entities run by non-professional managers, providing investors with sufficient information to allow them to make informed investment choices is an essential component of investor protection. It is our view that if a CEDIF is engaged in managing an investment fund larger than \$6 million, investors should be provided with the information required by section 3.1.1 in order to enable them to properly evaluate their investment performance.

CEDIFs which have raised less than \$6 million, including capital raised by affiliated CEDIFs, and meet the conditions of section 3.1.2 are not required to make any additional disclosures.

The \$10,000 per-investor limit on investment

Numerous commenters expressed the opinion that the \$10,000 limit would reduce the amount of capital that can be raised by CEDIFs. One commenter commented that there was an inconsistency between the \$10,000 limit per investor in section 3.3, the minimum number of investors for additional offerings of 3, and the requirement to raise \$50,000. Another commenter noted that \$10,000 could be a low fraction of the investor's wealth and that a \$6 million fund would require 600 investors. Another noted that the risks to investors is mitigated by the tax credits associated with CEDIF investment, so that after the tax credits are taken into account, the net capital at risk for each investor is in fact less than the whole amount invested. One commenter cited the Savoy Report's recommendation of increasing the limit for Equity Tax Credit ("ETC") to \$250,000.

Response

The policy has been amended. The limit for investment by an unaccredited investor who is not a director or officer or promoter of the CEDIF has been raised to \$15,000 per beneficial investor and the limit on sales to unaccredited investors purchasing through a registered investment dealer or registered exempt market dealer has been raised to \$30,000 per beneficial investor.

There is no per-investor limit for CEDIFs that are not investment funds and there is no per-investor limit for accredited investors or individuals who are directors or officers or promoters of the CEDIF.

Limits on investment are a simple and commonly-used tool for investor protection because they greatly reduce the risk of catastrophic loss for investors. In this case, we consider it an appropriate mechanism for protecting investors in CEDIF investment funds who do not have large investment portfolios or very high income levels, and are not actively involved in the management of the CEDIF. We observe that the tax credit reduces the potential net economic loss but does not eliminate the possibility of a total loss of the remaining investment which can still be meaningful to investors.

In our opinion, the “know your client”, “know your product” and suitability requirements that registrants are required to comply with increase investor protection and justify a higher per-investor limit for investments sold through a registered investment dealer or exempt market dealer.

With regard to concerns relating to inconsistency, we note that there is no requirement that any CEDIF raise a minimum of \$50,000. The amount raised by a CEDIF is determined by the capital required to complete the CEDIF’s proposed project, the economies involved in raising that capital, and a strategic determination relating to which other exemptions may be more efficient for raising the capital. The requirement for 3 investors is due to the alignment with the ETC Act and is not investor protection related.

The number of investors in any CEDIF can vary significantly based on a number of factors unrelated to per-investor maximum investments. Many CEDIFs have numerous small investors, and a small number of very significant investors. In our view, this investment pattern is unlikely to be disrupted by the policy. Additionally, individual investors may invest over multiple years.

The Savoy Report recommendation related to direct investment in active businesses, and not in discretionary investment funds. There are no investment limits on CEDIFs which are not investment funds.

Investment limits may not be complied with

One commenter expressed the view that the investment limits should require investors to sign statements that they have not exceeded those limits.

Response

Responsibility for ensuring compliance with the policy rests with the CEDIFs. Staff will engage in period reviews as part of the regular compliance procedure review.

The per-offering limits on capital raising under the exemption are too low

Several commenters noted that the \$3 and \$6 million limits should be removed as they will impede and reduce citizen investment in Nova Scotia CEDIFs.

Response

We note that the CEDIF program is intended to encourage capital raising by small, community based entities run by non-professional managers. The \$3 million limit is not a change in policy, but has always been in the regulations. In the past, only 1 CEDIF has raised more than \$3 million in a single offering and most have raised significantly less.

The limit of \$6 million in total size for CEDIFs that are discretionary investment funds provides investor protection by limiting unqualified investment fund management. Persons managing investment fund portfolios larger than \$6 million are in the investment fund management business and should be registered to do so. If a fund wishes to continue to grow beyond the \$6 million limit, it can do so provided it hires a registered investment fund manager or becomes a specified investment fund by declaring its investments to its investors and seeking their approval in accordance with the requirements of the policy.

Investor protection would be better served through increased oversight and monitoring of the quality of CEDIF management

Some commenters noted that increased regulatory oversight of CEDIF management would be preferable to the investor protection measures in the policy. Some commenters appeared to be of the view that such oversight of management is currently taking place.

Response

NSSC staff do not evaluate whether a fund is being operated to their satisfaction or in a prudent manner. This responsibility rests with the CEDIF and its management who are solely responsible for their offerings and disclosure. NSSC staff review the offering document and non-objection to CEDIF offerings ensures only that the required disclosures have been made, and does not express or imply that the offering is of any particular quality or is a prudent investment or is suitable for any investor. Further, NSSC staff are not in a position to ensure appropriate governance structures are in place or to monitor CEDIF governance on a continuous basis. The principal means by which the NSSC promotes the protection of CEDIF investors are by enforcing compliance with the regulatory requirements relating to the offering document contents, reports of trade, continuous disclosure and investment limits.

Without a requirement for investment fund manager registration there are not enough additional protections for investors

One commenter was concerned that the level of protection for unsophisticated investors with limited investing experience investing into an investment fund which does not have a registered investment fund manager was too low and that greater investor protection measures should be implemented.

Response

We believe that the requirements of the policy provide reasonable protections to unsophisticated investors by providing them with offering document warnings concerning the risks of investing without a registered investment fund manager, enhanced investment disclosures, and enhanced investment decision making rights; as well as limiting investment amounts and therefore potential losses.

Investor approval of investment changes should be higher than a simple majority

One commenter expressed the view that the vote on any investment changes should be a two-thirds (2/3) majority vote not a simple 50% +1.

Response

The majority of votes required by the policy excludes votes cast by officers, directors and promoters, and we are of the view that a simple majority vote of 50% +1 is a suitable threshold.

The accredited investor test is not suitable

Several commenters raised issues with the imposition of an accredited investor test, expressing the view that it does not ensure investor sophistication. Some commenters noted that self - declaration of accredited investor status is inadequate, and some noted that an investor test that limits investment to no more than 10% of assets would be more appropriate. One commenter expressed concern that accredited investors would be reluctant to self-identify.

Response

Although the accredited investor test may in some cases be a reasonable indication of investor sophistication, we agree that this is not always the case. We note that accredited investor status is commonly used as a threshold for exemption from various securities regulations because it also demonstrates a capacity to withstand investment loss and the ownership of financial resources to obtain expert advice.

The obligation and usefulness of accredited investor self-declaration is currently being examined by the Canadian Securities Administrators and amendments to the accredited investor prospectus exemption in National Instrument 45-106 are expected in early 2014. CEDIFs offering securities to accredited investors will be required to comply with this exemption.

A percentage of investable assets test is a theoretically useful means for limiting the potential for catastrophic loss, but in our view, such a test would impose an undue administrative burden on CEDIFs.

Reluctance on the part of investors to disclose their accredited investor status to the selling agents is not a situation unique to the CEDIF context. All investors wishing to purchase securities on the basis of accredited investor status will be required to self-identify in accordance with National Instrument 45-106.

Mixed opinions on the use of registrants to sell CEDIFs

One commenter strongly objected to the idea of involving mutual fund or stock brokers and brokerages selling CEDIF shares. Another commenter voiced a contrary opinion, and was of the view that an offering sold through a registrant offers an additional level of protection to investors.

Response

The CEDIF programme has always allowed registrants (other than mutual funddealers) to sell CEDIF investments provided they had the required proficiencies. In our opinion, the “know your client”, “know your product” and suitability requirements that registrants are required to comply with increase investor protection and justify an increased limit on sales to unaccredited investors purchasing through a registrant. As noted above, this limit has been raised to \$30,000 per beneficial investor where the CEDIF sells shares through a registered investment dealer or registered exempt market dealer.

CEDIFs are unlike traditional investment funds in many ways and should not be required to comply with this policy.

Commenters argued that because of the differences between CEDIFs and traditional investment funds, CEDIFs should not be subject to any securities regulations relating to investment funds. The specific differences that were raised are enumerated below.

- 1) The primary purpose of an issuing CEDIF is to carry out its approved community economic development plan in a local community. Investing the money of its shareholders is incidental to this primary purpose.
- 2) The process of non-objection by the NSSC further enhances their appropriateness for investment.
- 3) The intention of National Instrument 31-103 is to ensure professional investment management for the public. CEDIFs do not undertake the same activities as these public registrants.
- 4) Traditional investment funds require professional management due to the complexity of the capital markets. CEDIFs are not complex and make long term investments in privately held companies.
- 5) Unlike traditional investment funds, CEDIFs do not receive fees or commissions for their management activities.

Responses

- 1) The definition of community in the ETC Regulations has been broadly interpreted and includes “common economic interest”. Therefore, CEDIFs are not always limited to a local geographic community as may have been intended by the legislation. However, we agree that this community development purpose is a fundamental distinction between CEDIF investment funds

and other investment funds. This is the principal rationale for the policy, which exempts CEDIFs from the investment fund requirements while imposing alternative investor protection measures.

- 2) The CEDIF and its officers, directors and promoters are responsible for the CEDIF and the disclosure in the offering document. NSSC staff's non-objection process ensures compliance with the regulations and does not evaluate nor purport to evaluate the quality of the offering, management, officers, directors and key persons or its suitability for investment.
- 3) In our view, if a CEDIF sells shares to the public, pools these investments, and passively invests these funds or exercises discretionary power over the ultimate investment choices made, then its activities *vis a vis* its investors are the same in all essential respects as those of any other public investment fund and regulatory investor protection measures are justified.
- 4) We agree that this relative lack of complexity is an important distinction between CEDIF investment funds and other investment funds. CEDIF investors should be able to understand and evaluate the investments that are typically made by CEDIFs if they are provided with adequate information. This is the rationale for the policy, which exempts CEDIFs from the investment fund requirements while imposing alternative investor protection measures, including in the case of a specified CEDIF, providing investors with the basic information they need to approve or not approve of the CEDIF's investment choices.
- 5) The investment fund requirements of Canadian securities law are based on an acknowledgement of the increased risk investors face when investing in pooled, passive investment funds managed by a another person or entity. Whether and how investment fund managers receive compensation for their activities does not alter this investor risk.

The treatment of OM offerings and CEDIFs is inconsistent

One commenter expressed the view the limitations of this policy on CEDIFs are inconsistent with the approach under Nova Scotia securities laws for exempt offerings to the public under a prescribed offering memorandum pursuant to subsection 2.9(1) of National Instrument 45-106 (the "OM Exemption").

The commenter said that the disclosure required in an offering document under the CEDIF Regulations is substantially similar to that required by Form 45-106F2, Offering Memorandum for Non-Qualifying Issuers ("OM Form"), other than financial statement requirements. In addition, the commenter noted that unlike the OM Form, each offering document of a CEDIF is required to be filed with, and is subject to the review and non-objection by, the NSSC.

Response

If an investment fund wishes to raise capital using the OM exemption, it must comply with the investment fund requirements of securities law by having, *inter alia*, a registered investment fund manager and audited financial statements

OM offerings pursuant to Blanket Order 45-519, which are similar to CEDIFs in that they do not require audited financial statements, limit the issuer to raising \$500,000 in total with a maximum investment of \$2,000 per investor.

Enhanced disclosure should be required from CEDIF investment funds without a registered investment fund manager

One commenter expressed concern relating to the perceived inadequacy of the disclosure required of CEDIF investment funds and observed that the policy should include enhanced disclosures to ensure adequate investor protection in the absence of an investment fund manager.

The commenter suggested that such enhanced disclosure should include background information on officers and directors and more information on the CEDIF track record and the track record of the CEDIF's past performance as a group. The commenter observed that this track record takes on more importance because the CEDIF managers are not required to meet registration standards.

Response

Officers and directors are required to disclose their CEDIF involvement in the offering document; potential investors can research other CEDIFs as required. In our view, requiring disclosure of all past CEDIF information would in most cases unnecessarily lengthen the offering document without additional benefit to investors.

We agree that if a reliable organization could provide past performance information for CEDIFs as a group it may be useful to investors. However, we note that the CEDIF program is intended to encourage capital raising by small, community based entities run by non-professional managers, and in our view appropriately valuing and quantifying historical performance is not feasible for this market segment.

Increased regulatory compliance monitoring should be implemented for CEDIF investment funds & those who sell them

One commenter observed that given the increased risk to investors posed by allowing investment funds to operate without an investment fund manager, enhanced continuing regulatory compliance monitoring should be put in place given the nature of the funds.

This commenter also noted that regulators should review the sales proficiency requirements of dealers permitted to sell CEDIFs and monitor closely unlicensed sellers and the suitability of their sales.

Response

NSSC staff monitor compliance of on-going disclosure and enforce securities law where breaches have been detected. With limited resources, the NSSC endeavours to provide appropriate investor protection as warranted.

With regard to increased monitoring of those selling CEDIF investments, we note that the CEDIF program is intended to encourage capital raising by small, community based entities run by non-professional managers. Offering documents, on-going disclosure, and investment limits for non-accredited investors are the primary investor protections imposed by the NSSC pursuant to CEDIF Regulations and the policy. Pursuant to the CEDIF Regulations, unregistered sellers can only sell two offerings at one time and can only supply information that is in the offering document. Registered sellers must obtain their firm's approval to sell the CEDIF shares and must meet regulatory proficiency standards.