



**Finance and
Municipal Affairs**

Community Economic Development Business Program

A Guide to Starting a CEDB

November 2011

Overview

The Community Economic-Development Business (CEDB) program provides a method for Islanders to invest in economic development within their community. Through the program, an eligible business approved and registered as a CEDB may obtain equity financing in the Province through a specified issue of shares. The Province of Prince Edward Island provides an income tax credit to eligible investors who purchase shares of the CEDB.

This guide describes the CEDB program. It is intended to assist members of communities interested in developing a CEDB. For more information on the CEDB program, please contact the CEDB Coordinator:

CEDB Coordinator
Economics, Statistics and Federal Fiscal Relations Division
Department of Finance and Municipal Affairs
PO Box 2000
Charlottetown, PE C1A 7N8

Tel: 902.368.4030
Fax: 902.368.4034
Email: CEDB@gov.pe.ca
URL: www.gov.pe.ca/CEDB

Eligible Investors

A tax credit is available to residents of Prince Edward Island who are at least 19 years of age. It should be noted that any approval of an issue of shares under the program does not constitute an endorsement by government of the business issuing the shares. The province does not guarantee any investment. The investor bears the risk of the investment.

Tax Credit

Beginning with the 2011 taxation year, the tax credit is calculated at 35% of the investment made by the individual to a maximum annual investment of \$20,000 (maximum annual credit \$7,000).

The investment may be made within the calendar year or within 60 days of the end of the taxation year.

The credit is not refundable but may be carried forward for seven years or carried back three years, however the credit cannot be carried back beyond the 2011 taxation year.

The maximum credit which can be claimed in a single taxation year (including current year and carry forward or back amounts) cannot exceed \$7,000. Tax credit receipts will be issued by the Department of Finance and Municipal Affairs and must be submitted with the individuals T1 Income Tax return.

Investors are required to hold the investment for at least five years. If an investment is disposed of, within this five year period, the individual shall be required to repay a prorated amount of the tax credits.

Note: Under provincial legislation, an individual can own up to 20% of an investment and be eligible for the provincial tax credit. Beginning in 2011, the federal government will levy a special tax on investments held in an RRSP or RRIF, when ownership is greater than 10%. Similar rules previously existed for investments held in a TFSA. Individuals can own more than 10% of an investment but will have to hold the investment outside of and RRSP, RRIF, TSFA to avoid the new federal tax.

Eligible Businesses

Businesses that are eligible for registration as CEDBs include companies and co-operative associations formed under the laws of Prince Edward Island. To be eligible for registration, the company or association must

1. have authorized capital consisting of at least one class of voting equity shares
2. have assets or revenues of less than \$3 million;
3. have at least 75% of its salaries and wages paid in Prince Edward Island;
4. carry on active business, or have a constitution that restricts it to making specified investments in local businesses; and
5. have at least six directors who are residents of a defined community in which the eligible business carries on business.

The CEDB raises capital by issuing shares to individuals through a formal offering process in accordance with Prince Edward Island securities law. It is also to be noted that the shares cannot be distributed in any other jurisdiction.

The shares cannot be eligible for any other tax credit or deduction allowed under the Income Tax Act (Canada), except as a deduction for RRSP purposes.

An initial offering of shares of a CEDB must have at least 25 purchasers.

In the case of a company, the issued shares must be newly issued voting common shares of the company that are non-redeemable, nonconvertible, and that are not restricted in profit sharing or participation upon dissolution.

In the case of an association, the issued shares must be one or more fully paid membership shares such that, if they were the only shares issued to the investor, they would allow the investor to vote and participate in the affairs of the co-operative.

CEDB Application and Securities Review Process

An eligible business must make application to the Minister of Finance and Municipal Affairs to obtain a certificate of registration as a CEDB. Application forms may be obtained from the CEDB Coordinator. Electronic copies are also available at: www.gov.pe.ca/CEDB. In addition to the application form, the eligible business must submit

1. complete financial statements for the preceding taxation year (Income statement, balance sheet, statement of changes in financial position);
2. a copy of the T2 income tax return for the preceding taxation year;
3. a copy of the business' letters patent or articles of association containing the following prescribed restrictions and information as outlined in Section 4 of the *Community Development Equity Tax Credit Act General Regulations* (See CEDB Application Form and Guide for details):
 - a) restrictions on the business of the company or association to
 - i) operating or carrying on business that is an active business or to evaluating and making eligible investments in one or more active businesses based on a set of criteria defined by the company or association,
 - ii) providing information to and educating investors in the defined community as to the role of capital in business, the value of equity investments to the defined

- community and the rights and obligations of companies, associations and shareholders,
- iii) investing the capital raised, to which a tax credit pursuant to the *Community Development Equity Tax Credit Act* has been issued, in eligible business entities located within the defined community,
 - iv) exercising ownership rights with respect to the eligible investments made by the company or association, and
 - v) providing the administrative support necessary to carry on the business of the company or association, including preparation of annual reports and the holding of meetings of shareholders and the Board of Directors,
- b) a description of the defined community for which the company or association was formed, and
 - c) provisions for annual general meetings of the shareholders.
- 4. a copy of the current shareholders or members register; and
 - 5. a Community Economic Development Plan containing the following prescribed information as outlined in Section 2 of the Community Development Equity Tax Credit Act General Regulations (See CEDB Application Form and Guide for details):
 - a) a mission statement outlining the economic-development strategy of the proposed community economic-development business and the defined community it intends to serve;
 - b) the amount of equity capital to be raised under the plan;
 - c) the proposed use of the equity capital to be raised by the company or association;
 - d) a summary of the major business activities of the company or association, including major revenue sources; and
 - e) a listing of the directors of the company or association including their names, addresses, and background information.

Registration is also conditional upon the business obtaining a letter of non-objection from the Superintendent of Securities following a securities review of a proposed offering of shares.

Eligible Investments

Once the CEDB raises capital from a specified issue of shares, it invests that capital either in its own operations, or in one or more eligible local businesses. An eligible local business must

- 1. carry on active business;
- 2. have assets or revenues of less than \$25 million;
- 3. have less than 100 full-time employees; and
- 4. have at least 75% of its salaries and wages paid in Prince Edward Island.

Prohibited Uses of Funds - CEDB

Funds raised by the eligible business must be used in an active business and cannot be used for

- 1. lending;
- 2. purchasing shares, other than shares in other eligible businesses;

3. paying dividends;
4. purchasing services or assets provided by Her Majesty in right of the province;
5. redemption of shares or the funding of the purchase of all or substantially all of the assets of a previously existing proprietorship, partnership, joint venture, trust company, except where the firm is in receivership or bankruptcy; or
6. the purchase of assets or services by the eligible business for a price greater than fair market value.

The CEDB program is designed for community economic development. Investments in and by CEDBs must have a measurable financial return. The program is not meant as an alternative manner to finance projects that are more accurately described as municipal infrastructure. For example, a community may want to develop a local park that it feels will benefit the local population. While this may be a worthwhile endeavour, it would not produce a cash return to CEDB investors and therefore would not be an eligible use of funds raised through a CEDB.

Community Economic-Development Defined

Community Development

Community development is the process of assisting residents to take responsibility for their community development, of identifying specific community development needs, and of assembling the resources required to respond to those needs.

Economic Development

Economic development (growth promotion) programs help communities to adjust to changing economic times by preserving and stimulating businesses, by helping the community expand and diversify its economic base, by removing barriers to economic growth, and by encouraging new businesses to locate in the community.

Community Economic-Development

Community economic development combines community development and economic development principles to regain some control of the local economy from external markets and from government. It is a locally driven process to improve the economic viability of communities and to focus the resources of the area on economic growth. It leads to increased employment and income and to an improved quality of life for citizens of the community.

The CEDB program is an approach modeled after similar programs in other jurisdictions that encourages the formation of capital pools throughout the many diverse regions of Prince Edward Island. Tax credits offered to eligible investors in CEDBs are intended to accelerate the pace at which communities develop and implement viable business projects.

What is a CEDB?

CEDB

A CEDB is a company or co-operative association registered to sell shares to persons within a defined community, and to operate or invest in local business. A CEDB can be either a company formed under the Prince Edward Island *Companies Act*, or a co-operative association formed under the Prince Edward Island *Co-operative Associations Act*.

A CEDB must either carry on active business in the Province or restrict itself to investing in active businesses within the Province. A CEDB cannot be charitable, non-taxable, or not-for profit, and must have at least six directors elected from its defined community.

A new or existing businesses will register as a CEDB as a means to obtain capital and to invest it within a defined community. In order to raise capital from the public, the CEDB must follow Prince Edward Island securities laws, including the preparation and issuance of a formal offering document for prospective investors.

A CEDB - whether a company or association - will operate as one of three basic types:

1. **Direct investment CEDB** - A registered CEDB that raises capital from the public and invests that capital directly in its own active business as a key economic driver of the community;
2. **Flow-through investment CEDB** - A registered CEDB that allots its raised capital to one or more previously identified active business opportunities within its defined community; or
3. **Portfolio investment CEDB** - A registered CEDB that plans to invest its raised capital in one or more yet to be identified active business opportunities within its defined community.

Getting Started

How to Organize a CEDB

A CEDB must develop within a defined community. A CEDB must also be organized as either a company or a co-operative association formed and governed under Prince Edward Island laws. A CEDB must also have six directors selected from its defined community, two of whom must be considered independent directors.

Any individual or group may investigate the possibility of raising capital through a registered CEDB. Start-up capital may be required to plan and organize a proposed CEDB. All businesses also incur some ongoing administrative costs. There is no direct funding available to cover the costs of startup, or to cover ongoing administrative costs to run a CEDB. Nevertheless, should a community offering be completed, the promoters of a CEDB can seek to recoup some or all of their out-of-pocket costs from the proceeds of the offering. Local business and economic development staff is available to work with interested persons to provide information and assistance on how to plan and organize a CEDB.

Defined Community

Each CEDB must operate within a defined community of its choosing. The type of defined community in which a CEDB operates is not prescribed. Nevertheless, it is important that some initial parameters be set within which to solicit support for the CEDB initiative.

A CEDB's defined community is defined in the *Community Development Equity Tax Credit Act* General Regulations as "a group of persons situated within the Province that may be reasonably distinguished by common geographic, economic or cultural characteristics. A "spirit of commonality" should prevail. The key is for the CEDB to define, from the outset, what the community will be that it intends to serve and from whom it intends to solicit investment capital.

When persons are deciding how to choose a CEDB's defined community, they should be mindful of the pros and cons of a broadly defined community. The broader the defined community, the larger the pool of potential investors and board members. This, however, must be considered against the lack of community identification and support if the defined community expands beyond a reasonable size.

Community Economic-Development Plan

Each proposed CEDB must also be based on a community economic-development plan, which is submitted as part of the application process. This plan provides a strategic framework for identifying economic goals and objectives of the community, and for outlining how a proposed CEDB initiative intends to accomplish those goals and objectives. Developing the plan encourages open communication and cooperation among community members, and thus can be a beneficial exercise in and of itself.

As outlined above, the contents of the plan will at least include

1. a mission statement outlining the economic-development strategy of the proposed community economic-development business and the defined community it intends to serve;
2. the amount of equity capital to be raised under the plan;
3. the proposed use of the equity capital to be raised by the company or association;
4. a summary of the major business activities of the company or association, including major revenue sources; and
5. a listing of the directors of the company or association including their names, addresses, and background information.

The plan requirements outlined above represent only minimum prescribed plan content for the purposes of applying for registration as a community economic-development business. Additional content may be provided and also form part of a community economic-development plan. This additional content will not be reviewed for application purposes. Please note, however, that any promotional material (including all or part of a community economic-development plan) that is used in connection with an offering of securities is incorporated by reference as forming part of that offering document.

The plan requirements outlined above represent only minimum prescribed plan content for the purposes of applying for registration as a community economic-development business. While additional content may be provided and also form part of a community economic-development plan, such material will not be reviewed for application purposes.

It is important to note, however, that any promotional materials (including all or part of a community economic-development plan) used as part of an offering of securities are incorporated by reference and form part of an offering document. All such materials must also be attached to that offering document. It is therefore important for a proposed CEDB to consider whether and how it intends use its community economic-development plan for purposes beyond the CEDB application stage.

CEDB Application

An eligible business must make application to the Minister of Finance and Municipal Affairs to obtain a certificate of registration as a CEDB. Application forms may be obtained from the CEDB Coordinator and are available for download at: www.gov.pe.ca/CEDB. As described above, along with the application form, business must submit

1. complete financial statements for the preceding taxation year (Income statement, balance sheet, statement of changes in financial position);
2. a copy of the T2 income tax return for the preceding taxation year;
3. a copy of the business' letters patent or articles of association containing certain prescribed restrictions and information as outlined in Section 4 of the *Community Development Equity Tax Credit Act General Regulations* (See CEDB Application Form and Guide for details)

4. a copy of the current shareholders or members register; and
5. a Community Economic Development Plan containing certain prescribed information as outlined in Section 2 of the Community Development Equity Tax Credit Act General Regulations (See CEDB Application Form and Guide for details).

CEDB registration is also conditional upon the business obtaining a letter of non-objection from the Superintendent of Securities to conduct a specified issue of shares. The letter of non-objection process is explained in the next section.

Securities Review

The process of making an offering of shares to the public is one that must be completed under strict conditions. It requires the development of a formal offering document, a legal requirement that must be completed carefully, accurately and completely. While there is nothing inherently difficult about the process, a lack of familiarity with such legal documents, as well as the amount of information required, does make for a lengthy procedure.

The offering document outlines what the proposed investor is buying with his or her investment funds. It details who is making the shares available, what the total value of the offering is, and how the funds are to be invested. Completing this document to the satisfaction of the Superintendent of Securities is key to establishing a CEDB.

It is advisable that, concurrent with applying for registration as a CEDB, the business also begin the process of obtaining a letter of non-objection from the Superintendent. This process involves the development and submission of an offering document by the proposed CEDB to the Superintendent for review and comment. Offering document templates may be obtained from the office of the Superintendent of Securities and are available for download at: www.gov.pe.ca/securities.

Required attachments to the offering document include

1. the T2 and financial statements of the company or association for the preceding taxation year, if applicable (i.e. this will not apply to a newly formed company or association);
2. a copy of the proposed CEDB's letters patent or articles of association;
3. a copy of the proposed CEDB's community economic development plan; and
4. any other information that may be required in order to determine compliance with Prince Edward Island securities law.

After reviewing the draft offering document and all required attachments, the Superintendent may provide written comments outlining required changes or edits. Once the Superintendent receives a draft offering document that is deemed to meet all pertinent securities requirements, the Superintendent will notify the department of Finance and Municipal Affairs of his or her intention to issue a letter of non-objection for the proposed CEDB offering.

Upon confirmation that all pertinent CEDB application and securities requirements have been met, a certificate of registration from the Minister of Finance and Municipal Affairs and a letter of non-objection from the Superintendent of Securities will be sent concurrently.

Before the Superintendent issues a letter of non-objection to an offering document, a CEDB promoter may talk individually or in group situations with potential security holders to give them an informal general overview of the offering, including:

- identifying the CEDB;
- providing an indication of the amount of money needed to be raised;
- offering a general description of what use will be made of the money raised;
- giving an outline of the tax incentives; and
- gathering the names of potential security holders who might be interested in the offering.

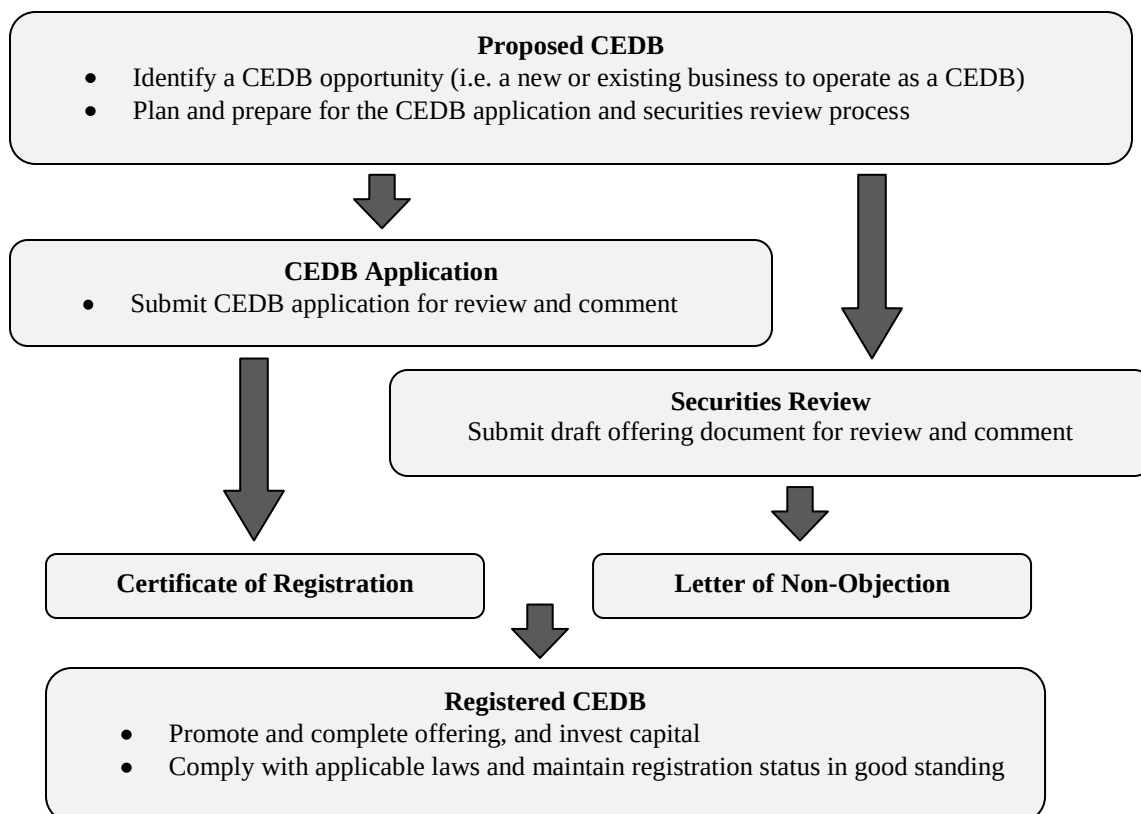
A CEDB promoter must not use or distribute promotional material or expression of interest forms without prior written non-objection of the Superintendent. A CEDB promoter must also not accept any binding commitments or binding expressions of interest, whether oral or written, or consideration in any form from potential security holders before the Superintendent issues a letter of non-objection to the offering document.

Any promotional material that is used in connection with an offering is incorporated by reference into the offering document, must include a disclaimer as required by the Superintendent, and must be submitted to the Superintendent and receive the written non-objection of the Superintendent before its use.

After the Superintendent issues a letter of non-objection to an offering document, the CEDB must file an amendment to the offering document for any material change in the affairs of the CEDB or the terms and conditions of the CEDB offering.

Please note that subscribers to an offering have certain statutory rights of action, including a right of action for damages for misrepresentation in an offering document.

Process Overview



Specific Roles and Requirements of Government Bodies

Department of Finance and Municipal Affairs

The Department of Finance and Municipal Affairs is responsible for the granting of registration certificates upon satisfaction of stated requirements, and for the issuance of individual tax receipts. This department is the agency responsible for policy changes affecting this program. Applications for registration of a business as a CEDB are submitted to the CEDB Coordinator within Department of Finance and Municipal Affairs.

The CEDB Coordinator within the Department of Finance and Municipal Affairs manages overall program delivery. Questions or comments regarding any aspect of the program may be forwarded directly to the CEDB Coordinator:

CEDB Coordinator
Economics, Statistics and Federal Fiscal Relations Division
Department of Finance and Municipal Affairs
PO Box 2000
Charlottetown, PE C1A 7N8

Tel: 902.368.4030
Fax: 902.368.4034
Email: CEDB@gov.pe.ca
URL: www.gov.pe.ca/CEDB

Department of Justice and Public Safety

Since this program involves the sale of securities to the public, the issuance falls under the jurisdiction of the office of the Superintendent of Securities within the Department of Justice and Public Safety.

The Department of Justice and Public Safety administers the Securities Act, which provides protection for Prince Edward Island resident investors in the securities markets in the Province. Investor protection is effected by rules requiring proper disclosure of relevant information to permit investors to make informed decisions and requiring fair practices by market participants.

Securities regulation is not primarily concerned with passing judgment on the investment merits of particular securities. Rather, it has as its focus investor protection. The office of the Superintendent of Securities fulfils its investor protection mandate, first and foremost, through prescribed disclosure requirements to equip investors with information they need to make informed investment decisions.

Business and Economic Development

Information and assistance on planning and organizing a CEDB is available from business and economic development staff throughout the Province.

Business and economic development staff across various government departments and agencies has information on a wide range of public and private programs. All of these departments and agencies work together to ensure the public has access to the right federal, provincial, or municipal programs to fit individual or group needs.

Business and economic development staff can provide initial guidance and information regarding the CEDB program, final approval for registering a CEDB lies with the Department of Finance and Municipal Affairs, while the office of the Superintendent of Securities is responsible for regulating public offerings in the Province.

Note: No government body assesses the reasonableness or merit of a particular CEDB applicant or its offering. More specifically, no government body will assess

- whether a CEDB applicant has sufficient financing or managerial expertise to accomplish its stated objectives;
- whether management of the CEDB applicant has the reputation and commitment to conduct its business with integrity and in the best interest of security holders;
- whether the promoters or management of the CEDB applicant are receiving unconscionable benefits at the expense of security holders; or
- whether any financial forecast or projection in the CEDB applicant's offering has a reasonable basis.

Company vs. Co-operative Association

The organizational form of a CEDB can be either a company or a co-operative association. The application process to be followed is virtually identical and there is no inherent advantage to either structure. The decision on organizational form should be based upon the experience of the organizers.

The fundamental difference between companies and co-operative associations is the manner in which the shareholders exercise their voting privileges. In a company, individuals vote based on the number and type of shares they own. In general the largest equity investors have the greatest say in the affairs of the business. Co-operative associations, on the other hand, grant each member a single vote, and therefore, the size of investment made does not bear on the relative influence an individual has in matters brought to a shareholder vote. This basic difference between companies and co-operative associations is highlighted in the table below:

Company		
Individual Investment	Shares @ \$10 per share	Votes
\$1,000	100	100
\$5,000	500	500
\$10,000	1000	1000

Co-operative Association		
Individual Investment	Shares @ \$10 per share	Votes
\$1,000	100	1
\$5,000	500	1
\$10,000	1000	1

When determining the structure of the CEDB, persons should consider the types of investors it plans to target and whether these individuals would be more supportive of one form over the other. People tend not to invest in things they do not understand, and as a result, the structure chosen is important to the viability of the organization.

Risk and Return Expectations

Investors in a CEDB have no assurance of a financial return, let alone of quantifying an expected return with any reasonable certainty. When evaluating any CEDB, potential investors should consider it a high risk long-term investment with limited options for eventual liquidity. Specifically, potential CEDB investors should be at least aware that

- they are required to hold a CEDB investment for at least five years, and if they dispose of their investment within this five year period, they shall be required to repay a prorated amount of the tax credit received;
- while initial tax benefits may be calculated, any potential return generated from CEDB operations will depend on the performance of investments made by the CEDB;
- they will only be entitled to dividends if and when declared at the discretion of the CEDB board of directors;
- a CEDB has no inherent right to retract previously issued shares from their investors, and CEDB investors have no inherent right force a CEDB to redeem their shares;
- there may be a low probability of any eventual sale of the CEDB to a third party purchaser;
- there may also be a low probability of any eventual public listing of the CEDB's shares on a regulated exchange;
- the CEDB may, but is not inherently obligated to, offer to repurchase their shares after at least five years; and
- any eventual sale of CEDB shares to a third party must comply with securities laws, and any third party purchaser of those shares would not be eligible for a provincial tax credit.
- the federal government has implemented restrictions on holding a investment in an RRSP or RRIF when ownership is 10 per cent or more.